Manchester City Council
Report for Information

Report to:	Resources and Governance Scrutiny Committee – 7 September 2021
Subject:	Council Wholly Owned Companies
Report of:	City Treasurer and Deputy Chief Executive

Summary

This report addresses the Committee's request to consider the spend, financing and governance of its wholly owned companies. It draws out the lessons learnt from recent Best Value and Public Interest reports on failings in other local authority companies, as well as considering the spend and financing arrangements through the case studies in the report.

Recommendations

The Resources and Governance Scrutiny Committee are requested to note the content of this report and comment and question as appropriate.

Wards Affected: All

Environmental Impact Assessment - the impact of the decisions proposed in this report on achieving the zero-carbon target for the city
This report is for information in relation to the lessons learnt from recent public interest reports and governance and oversight of Council wholly owned companies and does not directly propose decisions affecting the achievement of the zero-carbon target.

Our Manchester Strategy outcomes	**Contribution to the strategy**
A thriving and sustainable city: supporting a diverse and distinctive economy that creates jobs and opportunities	Through the companies that the Council owns, these have created jobs and continue to create employment opportunities across a wide range of sectors.
A highly skilled city: world class and home-grown talent sustaining the city's economic success	
A progressive and equitable city: making a positive contribution by unlocking the potential of our communities	

A liveable and low carbon city: a destination of choice to live, visit, work	
A connected city: world class infrastructure and connectivity to drive growth	

Full details are in the body of the report, along with any implications for

- Equal Opportunities Policy
- Risk Management
- Legal Considerations

Financial Consequences – Revenue
There are no revenue consequences arising specifically from this report.

Financial Consequences – Capital
There are no capital consequences arising specifically from this report.

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Background documents (available for public inspection):

The following documents disclose important facts on which the report is based and have been relied upon in preparing the report. Copies of the background documents are available up to 4 years after the date of the meeting. If you would like a copy please contact one of the contact officers above.

Not Applicable

1. Introduction

1.1 The purpose of this report is to provide Resources and Governance Scrutiny Committee with "a report on spend and financing of external wholly owned organisations including Manchester Central. To include lessons learnt from Public Interest Reports." The report also reflects upon the way in which Manchester is governing its companies in light of the recent reports and how the Council is further strengthening its approach to the implementation of robust and sound commercial governance.

2. Background

2.1 Since the 2011 Localism Act gave local authorities new powers to trade, there has been a steady increase in the creation of new companies owned by Councils. Local authority trading companies (LATCs) now deliver a wide range of services across the country. These range from wholly owned companies, joint ventures with either the public or private sector, to social enterprises.

2.2 LATCs offer some clear advantages over other service delivery models. They mean councils can keep direct control over their providers, offering an opportunity for any profits to come back into the authority. Equally the chance to change local authority terms and conditions, particularly with regard to pensions, can bring significant reductions in the cost base of the service.

2.3 Creating a separate company also lets the service becoming more agile, focused and responsive to changes in demand or funding. In addition, the powers to trade provide the companies with the opportunity to win contracts elsewhere and allows the company to bid contracts and access funding that it otherwise would not be able to as a department of the Council.

3. Commercial Governance

3.1 For a number of years, Manchester City Council has been pro-actively involved in a range of company activity, with a range of entities which it owns or has some degree of shareholding in. The Council currently has eight active wholly owned companies which undertake different type of activities that provide economic and social benefits to the City and support the Council's policy aims. These company are all varying in scale and size, as well as level of activity and turnover.

3.2 To ensure that there was more of a detailed oversight of company activity and performance, in 2018 the Council established a new Commercial Governance service area. The initial emphasis of the service was to perform a consistent company secretarial function under the guise of Manchester Professional Services Limited (MPSL), a wholly owned council company established for this purpose, which supports over 40 different Boards at present. The purpose of the establishment of MPSL was to provide an independent Company Secretary service which would have its own autonomy despite being wholly owned.

3.3 The unit also provides a corporate co-ordination and oversight function for companies, joint ventures and charities which the Council is involved in either wholly owns or has a stake in to ensure that information on all entities is held in one centralised place, bringing together information from both legal and finance, as well as looking to standardise process and embedding good practice through the approach we take to company operation. Activity undertaken by the Commercial Governance service is monitored by the Commercial Board, which is an officer meeting and chaired by the Deputy Chief Executive & City Treasurer.

3.4 A particular area of focus for Commercial Governance in recent months is review of a range of Best Value and Public Interest reports into Local Authority commercial ventures. This has been due to the high profile failing of some companies which have put some Councils in financial distress. Following analysis of the published Best Value and Public Interest reports, there is a similar pattern of areas of weakness in those failings that have been highlighted:

- Limited or no reporting back to the Council as Shareholder;
- Lack of scrutiny of business plans in order to highlight risks to the Board and / or Shareholder;
- Unclear company objectives or purpose;
- Boards not relevantly skilled to lead specific types company activities or understanding of the Council's role as Shareholder and Council Members and / or Directors not appropriately trained to fulfil their duties.

3.5 There has been a thorough assessment undertaken on the Manchester approaches the issues outlined at 3.4. It is to be noted that there have been no specific weaknesses found in the way in which the Council operates or structure its companies. There are already a number of areas where the Council is embedding good practice, but through the reflection on current practices, this has provided an opportunity for further enhancements to current ways of working with appropriate. These include:

Establishment of a Shareholder Panel

3.6 From reviewing the findings of a number of the recent reports into Local Authority commercial activity, lack of Shareholder oversight was found to be a consistent weakness. Whilst the Council does maintain a regular overview of company activity, it was felt that this need to be further formalised to ensure consistent oversight. This would be additional governance and oversight to that provided through the bi-annual Register of Significant Partnerships assessment process.

Introduction of Directors training programme

3.7 Work is currently underway with CIPFA to design a training programme for both Members and Officers who are taking on roles as Directors. There will be two training cohorts – a refresher session for more experienced Directors who already have a Directorship(s) and a session for those new to undertaking a company Director role or about to become a Director.

Member Oversight

3.8 Member oversight is already strong, with all wholly owned companies been established as a result of Executive and Key Decisions. This has been strengthened in recent years with the Register of Significant Partnerships which reports to Audit Committee twice a year and includes an updated risk assessment of all of the Council's significant partnerships so Members are aware of any changes and developments which may affect the viability of the entities so that any early actions can be identified.

4. Wholly Owned Companies

4.1 The COVID-19 pandemic has posed a challenge to a number of Council wholly owned companies. Due to their robust and resilient business plans and careful financial planning, these entities have mitigated the impact and challenge of COVID-19 on their trading activities as far as possible. The sections below provide some case studies into Council wholly owned companies in terms of current trading position and examples of good practice in terms of adopting a strong approach to governance.

4.2 In order to demonstrate in more detail some of the wide range of companies which the Council own, the case studies below provide some further detail and context about these wholly owned ventures.

4.3 Manchester Central Convention Complex Limited (MCCCL)

4.3.1 Manchester Central Convention Complex Limited (Co. No. 00953285) is a subsidiary of Destination Manchester Limited (Co. No. 05360083), which Manchester City Council the owner of and ultimate controlling party. Destination Manchester Limited acquired G-Mex Limited in 2005, which was renamed to Manchester Central Convention Complex Limited in 2007.

4.3.2 MCCCL was initially established in partnership with GM authorities to covert the empty station into a conference centre. This would not have been achievable if still within the Council. The main function of MCCCL is the hosting of conferences, exhibitions and events at Manchester Central Convention Complex, with additional income derived from rental income from adjoining properties. In addition to this the company also provide retail catering, hospitality and event services to Manchester Town Hall and Central Library, since winning the contract in April 2013. The March 2020 accounts show that the event sector of the business continued to growth from strength to strength, with turnover increasing by 4% attributable to the events and conferences held at Manchester Central.

4.3.3 The success of Manchester Central has not only been measured through financial performance but through the contribution to the wider economy as a whole. In 2020, it was estimated that every £1 of direct spend in the venue, a further £5 was spent elsewhere in the city. In addition to this, for overnight delegates staying in the city centre, it estimated that this has an average impact of £358 per person.

4.3.4 The sectors in which Manchester Central operates in has been amongst the worst affected by the COVID-19 pandemic, with by far the most significant loss of revenue stream is from conferences, exhibitions and events. Throughout this period, Manchester Central has fared much better than most of its peers due to the NHS occupancy of the venue as a Nightingale Hospital.

4.3.5 Alongside the rental income generated by the use of the facility from the NHS and government programmes such as the Job Retention Scheme (Furlough) this helped sustain Manchester Central through this challenging period. Prudent financial planning, with strong governance and oversight by the Board, facilitated MCCCL's survival through the most of challenging times.

4.3.6 At present, MCCCL's business recovery plan is currently in the process of being implemented. The plan is structured around three core themes of:

- *Respond* - Dealing with the present situation and managing continuity,
- *Recover* - Learning and emerging stronger and
- *Return* – Preparing for and shaping the "new normal".

4.3.7 Pre pandemic, MCCCL had a strong operating base with many bookings made in advance and a range of regular and returning bookings. As part of the recovery planning, a detailed analysis has been undertaken on the range of sectors and potential timeline of impact on business from these sources in order to be able to plan booking and income trends. There is a degree of confidence that the venue will recover over the coming months but there still remains an element of uncertainty how quickly full recovery could happen. To try and further negate the impacts, MCCCL are looking to the future and what events make look like moving forward and ensuring that their business model is adaptable to changing customer needs.

4.3.8 With regard to funding streams to operate the entity, these primarily derive from income generated through the hosting of events. It is to be noted that the Council did provide a loan to MCCCL in 2010 for £11.8m for a term of 17 years. Repayments on the loan are up to date but given the challenges faced by the business through COVID-19 restrictions, some flexibility has been provided in terms of timing of payments due within the 2021/22 financial year; the loan repayment will be made in one lump sum in March 2022 rather than on a quarterly basis throughout the year in order to maintain a strong cash balance in the accounts whilst trading re-commences.

4.3.9 A direct financial return is also provided to the City Council each year through a profit share arrangement. In 2019/20 this was £xm. Whilst it dipped in 2020/21 to £xm this is expected to recover back to its original level in the next couple of years.

4.3.10 In the last full set of accounts for the year ended 31 March 2020, Manchester Central Convention Complex Limited turned over more than £19m and made an operating profit of more than £1m. The venue was attended by more than 415,000 visitors and the economic impact on the City was £113m.

4.4 Manchester Digital Creative Assets

4.4.1 The Manchester Creative Digital Assets (MCDA) (Co. No. 10300159) was created to manage and operate a number of council assets (The Sharp Project, Space Studios Manchester, Arbeta and Screen Manchester) with the purpose of identifying gaps in provision and bring forward strategies to help digital businesses. It supports growth in an important part of the Manchester economy, which has enabled the regeneration of the former Fujitsu tower site in Gorton which is now a successful film studio. The key priorities for MCDA are as follows:

- To help fuel Manchester's ambition to be a city of digital enterprise with enviable skills and businesses;
- To enable such growth by creating innovative production and digital workspaces that combine technology with commerce to create a successful modern city; and
- To nurture and invest in local entrepreneurial talent, developing the skills to drive and support sustainable growth.

4.4.2 In this case, the Council's investment has been via the provision of 'invest to save' capital investment by the Council has enabled the successful redevelopment of Sharp, Arbereta and Space Studios. The investment is due to be repaid over the next 25 years and has helped secure a number of jobs and create benefits for the wider local economy. The Sharp Project is now home to over 60 creative digital businesses specialising in content production across animation, gaming, video and mobile tech. Space Studios Manchester is a purpose built facility for high end TV, film & commercial production. The site has more than 85,000 sq ft of high spec stages. Recent productions filmed at Space Studios include 'Cold Feet' (ITV), 'Dragons Den' (BBC), 'The A Word' (BBC) and upcoming Sky Atlantic drama 'Curfew' as well as commercial productions for a wide variety of international brands. There is a £922k income surplus returned each year which is used to pay down the debt incurred to fund the capital works previously undertaken.

4.5 Manchester Heat Network (Civic Quarter Heat Network)

4.5.1 Manchester Heat Network (MHN) is a Special Purpose Vehicle that has been established to oversee the operation of the city's Civic Quarter Heat Network, supplying heat and power to a range of commercial and Council buildings. This forms an important part of the Council's zero carbon ambitions.

4.5.2 The project is funded by a combination of debt and equity from the Council, alongside an element of government grant. A SPV structure was required to be established to allow the heat network to trade with external customers in order to generate sufficient income to cover the operating contract for network and also repay the finance which the Council had out in the venture. One of the key rationales for supporting the project was due to the network's contribution to reducing the Council's direct carbon emissions by approximately 2,200 tonnes of CO_2 when fully operational with 1,600 tonnes being saved in the first year of operation alone.

4.5.3 The SPV is not yet an operational entity but careful consideration has been given to its governance and structure to ensure that there is a robust oversight of the entity but balanced against the need for the SPV to trade autonomously. In order to ensure that there are the right controls in place, the Council has instigated the following:

- *Appointment of Non-Executive Directors*: Given the specialist nature of this particular company and reviewing lessons learnt from Robin Hood Energy in Nottingham, ensuring that there is an appropriately skilled Board in place to oversee operations has been a key activity area of focus. An extensive recruitment process for the appointment of Non-Executive Directors (NEDs) was undertaken to bring on board three specialists with relevant industry knowledge and experience. NEDs have been appointed to both the boards of HoldCo and TradeCo, with a further skills audit now being undertaken to identify any other particular areas which the Boards could benefit from. It is proposed for all new ventures, that NEDs should be appointed.

- *Delegations Matrix*: Clarity on decision making and what is required to be reported through to the Shareholder is a key area that needs to be understood by any Board. To outline these limits of authority, a clear and transparent delegations matrix has been put in place. This outlines the level of responsibility each element of the SPV has and the decision making flow through the company structure, along with the decision making that is referred into the Shareholder. It is felt that is an example of good practice and will be adopted as part of any new company set up moving forward.

- *External Assurance*: The provision of external assurance on a number of aspects of the establishment of the Heat Network has been critical to formulating the approach to effectively operate the SPV. A team of external advisors were brought together to focus on particular aspects: Browne Jacobson as legal advisors, EY provided assurance on the business plan and KPMG to prepare and review financial modelling for the duration of the heat networks operation. The independent assurance is a key factor to ensure that as a Council we are getting the balance of commerciality vs public authority accountability and that we are not becoming involved with something that has significant and inherent risk running through it.

3.5.4 The total capital budget for the CQHN is £24m. The Business Case was approved by the Executive in June 2021 and confirms that the funding model for the company. The capital has been provided via a mixture of debt and equity with interest payments on the loans commencing in 2021, and capital repayments within the first three years. There will also be savings on the Council's energy costs. The full Business Case was included as a Part B report due to the commercially sensitive information contains.

3.5.5 The Council also expects to generate income in the longer term from the investment in the Civic Quarter Heat Network. After the initial connections have been completed, the CQHN will seek additional customers which will generate further income that could result in an income stream from the dividends generated by the company. The generating capacity of the CQHN has the ability to be expanded through the addition of a second engine which would substantially increase the number of customers that can be connected to the network.

5. Risk Management

5.1 As highlighted earlier in the report, recent Public Interest and Best Value Reports have highlighted a number of weaknesses in how Councils, from a Shareholder perspective, have not been fully sighted on the performance of companies which they own, and any emerging risks connected with the type of activities which these entities deliver. The report sets out the steps the Council has taken to ensure the learning has been taken from these reports and identifies that whilst there are always some areas for improvement, effective governance and oversight is maintained.

5.2 Each company has a range of risk associated with it which Boards are designed to oversee, track and mitigate appropriately. Given the some of the challenges linked more recently to COVID-19, the Council, as Shareholder, has been asked to provide some assistance through short term flexibilities. This has been mainly in the form of reprofiling payments due to the Council from loans or dividends to later times within the same financial year, to allow the business build up sufficient financial resilience now COVID related restrictions have been lifted and companies can now trade more freely. The impact on the Council’s bottom line has been relatively limited as the companies all have their own risk management strategies and reserves, and by virtue of being private companies have been able to access government Covid support directly. The Council has supported some of its wholly owned companies by allowing in year payment profiling to protect cash positions. There are no outstanding or overdue debts owed by these companies to the Council.

6. Conclusions

6.1 Reviewing the approaches of other Local Authorities and lessons learnt from recently published reviews has been something which the Council has both compared ourselves against and reflected upon. There are strong governance arrangements in place from concept through to implementation and beyond, with clear lines of accountability to the Commercial Board, Scrutiny Committees and ultimately the Executive. In addition, there a number of areas where there are robust assurance process which are already established and working well. The Council will continue to regularly review and reflect upon the way in which we operate our wholly owned ventures to ensure they remain fit for purpose and continue to deliver benefits for the City as originally intended.

6.2 As well as ensuring effective governance, officers continue to closely monitor the financial performance of the wholly owned companies to ensure risks can be mitigated and to maximise the return for the Council.