

Manchester City Council Report for Information

Report to: Resources and Governance Scrutiny Committee - 25 May 2023

Subject: **PART A** - Commercial Activity, Investments and Governance

Report of: Deputy Chief Executive and City Treasurer

Summary

The Council is involved in a wide range of commercial activities, including, but not limited to, provision of loans to third parties, Joint Ventures, investments into a range of initiatives and property transactions. This report provides an overview of key aspects of the commercial portfolio as well as outlining the governance and assurance activity which take place before, during and post completion of commercial transactions.

Recommendations

The Committee is recommended to:

- (1) Note the content of the report and comment / question the information presented to the Committee as appropriate.
-

Wards Affected:

All

Environmental Impact Assessment - the impact of the issues addressed in this report on achieving the zero-carbon target for the city

This report does present information or propose decisions that have direct implications for the delivery of the Council's zero-carbon targets.
--

Equality, Diversity and Inclusion - the impact of the issues addressed in this report in meeting our Public Sector Equality Duty and broader equality commitments
--

Consideration of equality, diversity and inclusion issues for Manchester residents and businesses have been taken into account in the development and delivery of the specific schemes covered in the report.

Manchester Strategy outcomes	Summary of how this report aligns to the OMS/Contribution to the Strategy
A thriving and sustainable city: supporting a diverse and distinctive economy that creates jobs and opportunities	Through a number of the commercial activities and / or companies that the Council wholly owns or is a party to, jobs have been created and will 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	It is anticipated that the commercial activities outlined with the report will act as a catalyst for investment through supporting infrastructure, innovation, and people, providing a significant boost to the future economic growth for the local area.
A progressive and equitable city: making a positive contribution by unlocking the potential of our communities	The commercial activities which the Council is a party to, primarily through Joint Venture arrangements, act as a regeneration catalyst delivering positive socio-economic changes for communities.
A liveable and low carbon city: a destination of choice to live, visit, work	A number of the commercial activities and investments act as a catalyst for regeneration.
A connected city: world class infrastructure and connectivity to drive growth	Infrastructure improvements are an integral part of commercial activities the Council are a partner in delivering to ensure that opportunities are accessible to all.

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 direct capital consequences arising specifically from this report.

Financial Consequences – Capital

There are no direct capital consequences arising specifically from this report.

Contact Officers:

Name: Carol Culley
Position: Deputy Chief Executive and City Treasurer
Telephone: 07717 545785
E-mail: carol.culley@manchester.gov.uk

Name: Tom Wilkinson
Position: Deputy City Treasurer

Telephone: 07714 769347
E-mail: tom.wilkinson@manchester.gov.uk

Name: Sarah Narici
Position: Head of Programme Management Office: Commercial Governance
Telephone: 07971 384491
E-mail: sarah.narici@manchester.gov.uk

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.

- Resources & Governance Scrutiny Committee: Tuesday 7 September 2021 – Spend and financing of external wholly owned organisations.
- Audit Committee: Tuesday 14 June 2022 – Register of Significant Partnerships

1. Introduction

- 1.1 This report provides an overview of commercial activity which Manchester City Council is a party to. The report details the range of commercial endeavours covering a broad spectrum of activities such as wholly owned companies and Joint Ventures, development agreements, loan arrangements and equity investments into various ventures.
- 1.2 The sections below cover a number of aspects related to commercial activities including:
- Governance, assurance and oversight structures
 - Summary of key Joint Venture arrangements
 - Activities to close companies that are no longer required
 - An overview of the Council's commercial loan, equity and shareholding portfolio
 - A summary of the work being undertaken on the commercial and development estate
 - Regulation of commercial activity
 - Reflections on the review of Public Interest and Best Value reports into other Local Authority commercial activities

2. Background

- 2.1 The Council's Capital Strategy, approved by Executive in February 2023, sets out the priorities for capital investment in line with the delivery of the Our Manchester Strategy. These include
- Investment in growth and regeneration to support employment growth through a strengthening and diversification of the economic base and efficient use of land and investments which is catalytic in supporting recovery and economy and delivery of the Recovery Plan
 - The delivery of major regeneration schemes in the north and east of the city: North Manchester including North Manchester General Hospital, Victoria North, Back of Ancoats and Holt Town and Eastern Gateway
 - To promote the role and continuing growth of the City Centre as a major regional, national and international economic driver.
 - Securing investment for an internationally competitive cultural and sporting offer
- 2.2 The strategy also sets out the principles that govern investment decisions and to ensure that the limited capital resources available are prioritised to achieve best value for money:
- The Council will not invest in capital schemes purely for yield, although some schemes will be financed all or in part from returns on investment. Usually, investment will be within the local authority area although there may be exceptions if it is within the relevant economic area and meeting a key regeneration or zero carbon objective. The Prudential Code and Public Works Loan Board (PWLB) criteria will be followed.

- Assets will be reviewed to identify assets to realise capital receipts to support future investment priorities.

- 2.3 These are longstanding priorities and principles which have framed the Council's commercial activities and for many years, Manchester City Council has been at the forefront of utilising a variety of vehicles and structures to facilitate the delivery of commercially orientated schemes to deliver these priorities to the benefit of Manchester residents and the local economy. This has been evident in the way in which the city has recovered post COVID-19, with significant levels of investment continuing to take place in Manchester post pandemic, demonstrating the continued confidence in the future of our city.
- 2.4 In September 2021, Resources and Governance Scrutiny Committee received a comprehensive report that brought together all aspects of the Council's commercial activities. This report is the annual update on the progress being made.

3. Commercial Governance and Assurance

Strategic oversight of companies, Joint Ventures and charities

Commercial Governance inc. Manchester Professional Services Limited

- 3.1 Manchester City Council has been pro-actively involved in a range of commercial activity, with a range of entities which it owns or has some degree of shareholding in. The Council is currently involved with over 80 active companies, Joint Ventures and charities which undertake different type of activities that provide economic and social benefits to the City and support the Council's policy aims. These company vary in the scale and complexity, as well as type of activities delivered and level of turnover.
- 3.2 To ensure that there is robust oversight of company activity and performance, in 2018 the Council established a Commercial Governance service. The objectives were to ensure corporate co-ordination and oversight for commercial activities. The service subsequently developed to include the company secretarial function under the guise of Manchester Professional Services Limited (MPSL) and to ensure robust shareholder governance in place for commercial ventures. MPSL is a wholly owned council company established for this purpose, which supports 36 different entities. The function was previously hosted by GMCA and was transferred to provide an independent Company Secretary service which would have its own autonomy despite being wholly owned by the Council.
- 3.3 The Commercial Governance service provides a corporate co-ordination and oversight function for companies, joint ventures and charities which the Council is involved in. This is to ensure that information 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. Work is currently underway to refine and standardised processes to review companies

and create a 'house style' financial model to test the financial viability of all projects in the future. In addition, officers from the commercial governance and finance functions are undertaking knowledge share sessions, facilitated via external consultancies to ensure that processes are effectively embedded and lessons are learnt from any Local Authorities who have had challenges with commercial activities.

- 3.4 Commercial Governance proactively review the Best Value and Public Interest reports into Local Authority commercial ventures to review any lessons learnt and learning that Manchester can apply. It should be noted that there have been no specific weaknesses found in the way in which the Council operates or structures its commercial activities but there is no room for complacency and this has provided an opportunity to strengthen practice.

Commercial Board

- 3.5 The Council's Commercial Board, chaired by the Deputy Chief Executive and City Treasurer, was established in late 2018 with an initial focus on major projects and significant investments, to ensure alignment with corporate priorities, value for money and benefits realisation. Over time, the remit of the Commercial Board has increased to cover matters such as procurement, income generating contracts fees and charges, spend on agency staff and new policy areas such as the Subsidy Control Act. The Commercial Board doesn't have any formal decision-making powers and acts in a capacity of oversight / monitoring and a check and challenge function prior to commercial proposals being progressed for decision making through agreed constitutional governance routes.

Directorship Training

- 3.6 To ensure that there is a consistency of approach as to how Members and Officers undertake company Director role(s), the Council has co-produced a company Director training programme with CIPFA which all Members and Officers fulfilling a Directorship role are required to attend. At the time of writing, the Council has 59 seats on a wide range of company Boards. Three successful training cohorts have already been completed, with 24 Members and Officers attending the sessions. Further training is being scheduled for those performing a Directorship role unable to attend previous sessions in Autumn 2023. It is to be noted that a lack of sufficient training for those undertaking a company Director role has been highlighted as a key issue in a number of Best Value and Public Interest reports into failings in the operation of Local Authority commercial ventures.

Shareholder Panel

- 3.7 In 2021, the Council established a Shareholder Panel. The panel meets on a monthly basis to review the performance of various entities, provides assurance on compliance with Shareholder Agreements, has oversight of company reviews and addresses any issues in relation the operation of any of the companies, Joint Ventures or charities which the Council is involved with.

The Shareholder Panel is chaired by the Deputy City Treasurer and involves representative from Commercial Governance, Financial Management and Legal Services. Following a recent workshop session with officers who attend the group, a clear action plan prioritising key activities for 2023/24 has been devised. The current priority is to ensure the enforcement of Shareholder and Member Agreements which the Council has in place to ensure that the terms and conditions are complied with.

Due Diligence Framework

- 3.8 In July 2022, Commercial Governance led the design of a Due Diligence Framework (DDF). The purpose of the DDF is to provide financial and reputational assurance to the Council via the analysis of the performance and sustainability of the organisations which the Council are currently working or proposing to contract with. The framework and supporting pre / during / post transaction monitoring forms are designed to enhance existing approaches and formalise the way the Council conducts due diligence in relation to arrangements with third parties. At present, the DDF is being applied to loan agreements and equity investments, development agreements and major contracts that are classified as 'gold'. Following initial testing over the last six months, there have been some areas identified which require further strengthening, with an action plan established to progress the improvement areas to ensure that the DDF is providing the optimum level of assurance.

Register of Significant Partnerships

- 3.9 The Register of Significant Partnerships is an annual assurance process undertaken on partnership arrangements that are considered to be of the highest significance, could result in material implications to the financial position / reputation of the Council or to the delivery of corporate and Our Manchester objectives. These arrangements include; Joint Ventures, wholly owned companies, statutory groups, Private Finance Initiatives (PFIs) as well as a variety of other types of collaborative structures. The partnerships have varied approaches to governance which are deemed appropriate to their scale, legal status and delivery objectives.
- 3.10 Through the process, the partnerships are rated based upon the information provided by the officers completing the form. The assessment ratings are: substantial, reasonable, limited and weak. The rating is generated on the assessment on areas such as finance, audit, risk and governance. At present, there are 47 partnerships on the register which is reported to Audit Committee on a bi-annual basis; one report on the assessment of all entities received in June and an update report on those rated as reasonable, limited or weak in November / December.

4. Commercial Activities

- 4.1 Due to the commercially sensitive and confidential nature of section 4, this is being treated as a Part B item. The areas which the Part B report covers are:

- Companies that are included in Council group accounts outlining their structures and financial arrangements which the Council has in place with these entities
- An overview of some of the Joint Ventures which the Council is a party to and their current status
- Details of the companies which the Council either wholly owns or is a party to that are intended to be closed over the next 12 months
- A schedule of the Council's loan, shareholding and equity portfolio
- Details on any guarantees the Council provides to third parties
- An overview of the development estate including asset performance and impacts on the development estate

5. Regulation of Commercial Activity

- 5.1 The commercial activities of Councils are regulated in a number of ways through a number of interdependent codes and regulations, including the Treasury Management Code, the CIPFA Prudential Code, the CIPFA Financial Management code and PWLB guidance, all designed to ensure sound financial management of long-term assets and liabilities held by the Council.
- 5.2 Recent revisions to CIPFA's Prudential Code include the risk management framework local authorities should follow to manage debt and investments and requires authorities to include within their Capital and Treasury Management Strategies the approach that they take in relation to non-treasury management investments, including equity and loans to third parties.
- 5.3 The Code includes two specific categories of non-treasury investments:
- being service investments that are made to support service provision and for which the return on the investment is not the primary reason for it, and
 - commercial investments where the yield on the investment is the primary reason.
- 5.4 The Council does not make commercial investments, as defined by the Code. The activities noted above have been undertaken to support service provision and regeneration activities within the City of Manchester, and whilst there are commercial elements of the investments they are not held solely for financial return and yield.
- 5.5 The commercial activities detailed above are classed as assets and form part of the Council's annual accounts and are therefore reviewed regularly. All shareholdings and equity investments are valued on an annual basis using the latest financial information available for each company, and for loans an annual assessment is made of any potential losses for bad debts.
- 5.6 Any proposed equity investment made by the Council, and any loans longer than 12 months in duration, must be classed as capital expenditure and therefore are subject to the Council's capital approval process. This allows

them to be scrutinised before they are progressed, with the reasons for making the investment clearly set out and linked to the Council's priorities.

6. Public Interest and Best Value Reports

6.1 Several Public Interest and Best Value reports into Council commercial ventures, issued between 2020 and 2023, have highlighted a number of flaws with regards to Local Authority oversight and monitoring of such activities. These reports have often drawn attention to Local Authorities' pursuit of an objectives with no effective scrutiny and challenge before or during the implementation of the commercial initiative. The reasons for the failure of Local Authority companies are wide-ranging but primarily centre on two key points:

- ineffective governance arrangements; and
- commercial propositions that are fundamentally challenged from the outset.

6.2 This has provided some salutary lessons for councils about conducting appropriate due diligence when investing and lending to third parties. Undertaking robust due diligence, with support from an appropriately qualified external advisory team, when required, is absolutely critical.

6.3 The importance of thorough consideration has recently been underlined in Manchester through the due diligence undertaken on the potential acquisition of a solar farm. The comprehensive due diligence process highlighted a number of areas which posed potential significant material risks to the Council and therefore it was agreed that this particular opportunity should not be progressed.

6.4 Given the important part which Commercial Governance played in the due diligence of the large-scale energy opportunity, the service is going to play an enhanced role in being the lead for due diligence on investments and transactions that have potential material implications for the Council.

6.5 In 2022, CIPFA produced a Local Authority Owned Companies good practice guide, outlining processes and procedures councils are recommended to follow when considering progressing with commercial ventures. Manchester is cited twice in the guide, highlighting good practice examples linked to the Register of Significant Partnerships and the delegations matrix that has been put in place for the Manchester Heat Network, which clearly outlines the companies decision making authority and what needs to be referred back to the Shareholder for consideration. It is to be noted that other Local Authorities have contacted Manchester for further information about both these examples in order to assess how these approaches can be applied in their respective councils.

7. Risk Management

- 7.1 Robust risk management is a key tool that needs to be deployed effectively to ensure that any emerging issues are addressed in a timely way to effectively negate any impacts for the Council. As part of the assessment for any commercial activity and investments, a thorough assessment of potential risks is undertaken and outlined as part of the decision-making process. Detailed risk registers are also in place and reported at the relevant Board meetings.
- 7.2 Through the Council's Commercial Board, Shareholder Panel and Due Diligence Framework, these routes provide further risk management and oversight to ensure that the Council's interests are protected.

8. Conclusions

- 8.1 The Council has become a party to a broad range of commercial arrangements that have been facilitated through, for example, equity investments, development agreements and company structures. These arrangements all vary in size, scale and complexity, all of which have some form of potential for material implications for the Council's finances and / or reputation if not managed and monitored correctly. Through the continual improvement of the processes that have already established and further embedding of the importance of assurance and due diligence throughout the lifetime of transactions, it provides senior leadership with the confidence that Manchester won't be in a similar position to those councils where commercial activities have failed and resulted in government intervention.