SPECIAL REPORT IN ASSOCIATION WITH

Commercialisation

Safeguarding the future of local public service delivery

NICK GOLDING
EDITOR

Many have noted irony in ministers latterly urging caution about commercialism in local government.

These same ministers have not themselves been so cautious about the impact on local services as councils' central funding has been halved this decade. In response to the slashing of resources, local government has had little choice but to look for new sources of revenue, including through trading services and by seeking to earn money through its extensive property holdings. Ministers are in effect being charged with criticising the inevitable impact of their own policies.

However, any ministerial opposition to local government's commercialisation should not be overestimated. In an LGC interview last month, local government minister Rishi Sunak said there would not be a "general clampdown on councils being entrepreneurial, commercial or doing things pragmatically and sensibly that economically benefit their areas".

The concern was more levelled at a "handful of people who are doing something quite significantly out of the norm", presumably the small number of districts who have borrowed heavily to invest in property.

While there are legitimate worries, local government's commercialisation will intensify in the coming years. A survey of senior officers undertaken as part of this LGC research in conjunction with DWF shows that two-thirds believe their authority's revenue from commercial activity will rise by between 0-25% over the next three years.

However, entrepreneurialism is not risk-free. It is only by employing those who have knowledge of the commercial world that councils can hope to profit. There are numerous legal, staffing and financial implications, not to mention ethical ones, such as whether councils could potentially have an unfair competitive advantage.

Nevertheless, commercialisation offers local government huge potential to provide revenue to improve or safeguard services or to improve local areas – and it can ensure other public or private bodies are well served with quality services. We hope this research will inspire you.

JONATHAN BRANTON
PARTNER, HEAD OF PUBLIC SECTOR, DWF

As an adviser to many public sector bodies, DWF has seen a pronounced increase in commercial activity among local authorities in the past decade. Activities as diverse as the formation of local authority trading companies, joint ventures, enterprise zones or housing and development companies, property acquisition, grant and loan funding, consideration of future business rates and the renegotiation of PFI contracts have increased the sector's demand for (and reliance on) sound commercial and legal advice.

Broadly speaking, we know that the increase in commercial activity is being driven by the fact that authorities have had to seek new ways to deliver more for less and generate income for frontline services, but there are vital questions to be answered that could help authorities and legal advisers navigate future commercial opportunities more effectively.

DWF has worked with LGC to create this special report on commercialisation, assessing the challenges organisations are facing, the commercial models available and the strategies being adopted across the UK. We consulted over 150 organisations through a survey, in-depth interviews and a roundtable, gaining views from senior executives, elected members, trading company directors, local enterprise partnerships (LEPs) and the private sector to provide real insight into this rapidly developing agenda.

Some of the critical questions we address are:

- How do we define commercialisation in the public sector?
- How financially viable is commercial activity and what are the options for the sector?
- Are we likely to see commercial activity increase or decrease in the future?
- What can we learn from the successes and failures of authorities so far?
- In which areas do you expect additional revenues in the future?
- Does the sector have the skills to deliver its commercial objectives?

We hope that the survey results, case studies, and roundtable discussion serve to inform public sector officers and elected members looking to understand the current commercialisation landscape and the implications for the future.

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Surveying the commercial landscape

Our survey of senior local government officers reveals the expectations and priorities for commercial activity. **JIMMY NICHOLLS** reports

The halving of central funding for local government in the first seven years of this decade makes it essential that councils find new sources of income.

Advocates believe that commercialisation, broadly defined as a council charging for services that it is not legally obliged to provide, can ease financial pressure.

Commercial operations such as council-owned companies selling services to either the public or private sectors, or local authorities earning an income from the property they own, offer a means of providing the funding for services which would otherwise have to be closed.

An LGC survey in conjunction with DWF, to which 145 council chief executives and senior officers responded, sheds new light on the extent they believe commercialisation offers opportunities. However, it also shows real concern that councils lack the capability and skills to act as commercial entities.

> Our government funding was disappearing and we needed to fill that gap. Not all that gap could be found by making savings

One sceptic told us: “The idea that councils can successfully engage in significant commercial activity is a dangerous fantasy.” But this is not the experience of most.

Peter Fleming (Con), leader at Sevenoaks DC, explained that plugging funding gaps was a key motivator in his council’s decision to commercialise. “Our government funding was disappearing and we needed to fill that gap,” he said. “Not all that gap could be found by making savings.”

However, he argued that investment income was not “an end in itself”, but instead “something that allows us to continue to deliver public services”.

This was backed up by Tracey Lee, chief executive of Plymouth City Council. She said that her authority saw commercial “in the widest sense”, helping the council fulfil its ambition for social good. “But many of the things we do make an impact on the bottom line,” she said.

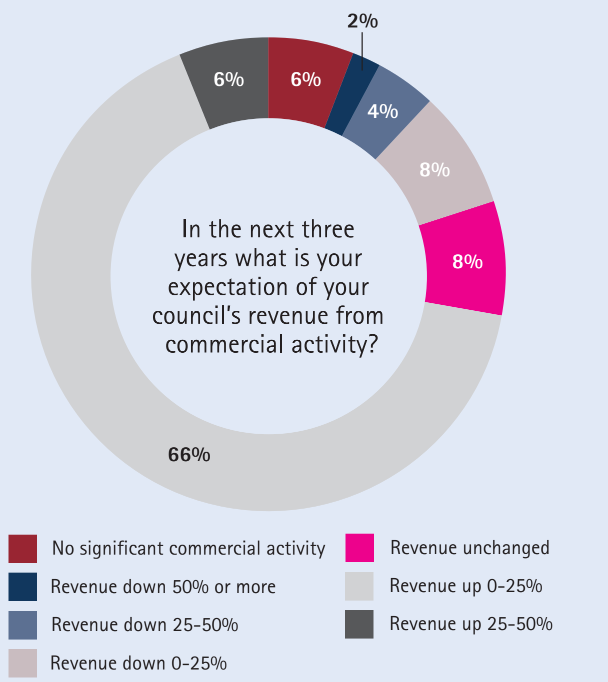
Two-thirds of survey respondents expect their revenues from commercial activity to rise up to 25% in the next three years – though in some cases this may be from a low base. A further 6% expect it to rise between 25-50% over the same period, while 12% expected commercial revenues to drop 0-50%.

Alongside the forecasts of increased revenues from commercialisation, most survey respondents were able to specify in which channels they expected to see increased revenues.

Some 61% of those surveyed said they would generate more revenue from council-owned trading companies, 59% reported property sales would see a rise in income, with 53% expecting the same from property rental.

Such projects can offer income for a council or save it money. Wirral MBC and Cheshire West & Chester Council set up Edsential to support schools, saving “a significant amount of money”, according to Wirral chief executive Eric Robinson. Plymouth City Council’s CATERed, set up with local schools, now serves 2.5 million meals each academic year, with profits reinvested in the service.

However, councils’ commercial activity can prove controversial. Earlier this year the Chartered Institute of Public Finance & Accountancy warned local government not to expose public funds to “unnecessary or unquantified risk” when borrowing to invest in commercial property.



In October, research by The Bureau of Investigative Journalism, in conjunction with LGC, found the number of councils investing in assets they deemed "investment property" increased from 35 in 2015-16 to 71 in 2017-18. According to Freedom of Information responses from 309 out of 353 councils contacted, the amount spent on properties bought specifically for investment purposes has risen from £76.4m in 2014-15 to £1.8bn in 2017-18.

In the local government financial settlement in December, housing and communities secretary James Brokenshire said there were ongoing talks between the Ministry of Housing, Communities & Local Government and the Treasury on possible "further intervention" where councils are deemed to be exposing themselves and taxpayers to too much risk.

Local government minister Rishi Sunak later clarified to LGC that ministers will not curtail most councils' commercial investments, and that concerns about overexposure apply to only a "handful" of authorities.

Perhaps just as controversially, car parking revenue increases were expected by 56% of LGC's respondents. Such fees are often criticised by struggling high street retailers. In November, the RAC Foundation reported that in 2017-18 income from parking operations by 353 English local authorities was £867m, having risen by a third from £658m in 2013-14.

Westminster City Council led the field with a surplus of £57.6m for 2017-18, with other London boroughs close behind. Brighton & Hove City Council was the only authority not from the capital in the top 10 surplus-generating authorities.

> "The dinosaurs in finance don't move quick enough. Four years of pushing and we're nowhere!

One comment illustrates the mix of pitfalls and opportunities that council officers feel in relation to commercial projects. "We are selling off the family silver," the respondent said. "The council has set up a property company to develop properties but don't understand how to do it."

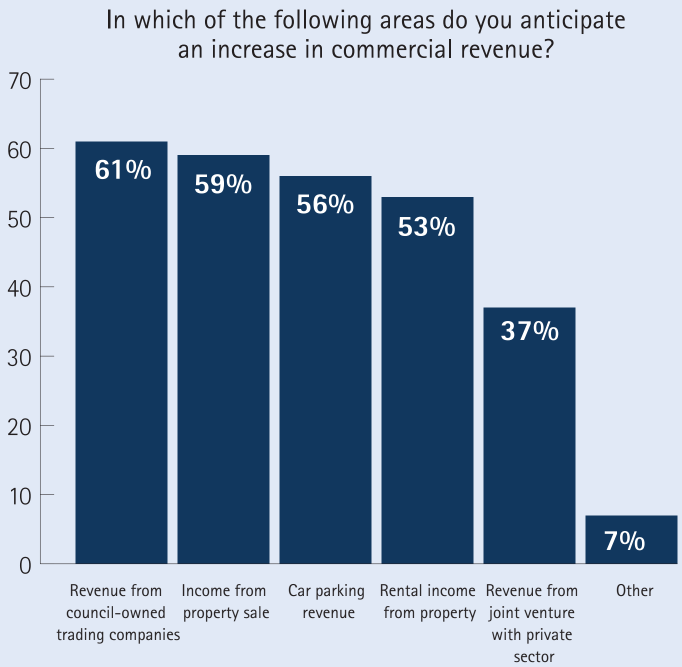
However, they said that in their role they had a successful trading unit "that needs to go private" to fully exploit the market. "The dinosaurs in finance don't move quick enough," they added. "Four years of pushing and we're nowhere!"

Outside of parking and property, councils have set up commercial projects in a number of different fields. According to the survey, some 22% of councils provide a commercial service in energy, 46% in legal services and 32% in care services.

Over the next three years many survey respondents are considering commercial projects across these areas. Some 21% of respondents' councils want to set up a trading service for energy in this period, 14% in commercial waste and 12% in education services.

Not all such projects have been successful. One survey respondent said: "Although there are several traded services currently, they are under review and commercial success has proved elusive. It is likely that the review will result in several of these services being brought back in house at significant cost."

There were also signs of unexplored potential to monetise existing services. Another respondent said:



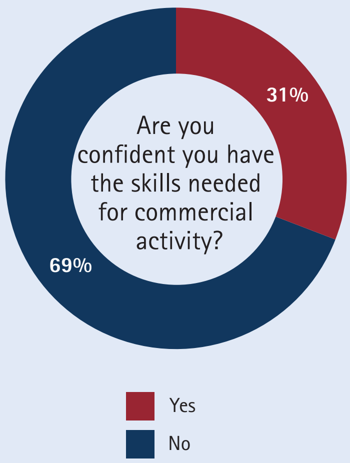
"This council tends to charge other departments within for these services but is for some reason reluctant to bring money in by charging outside of the council for them."

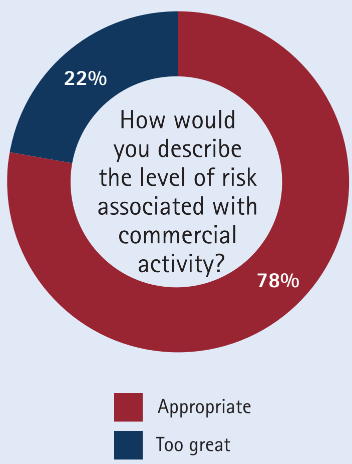
There remains a lot of concern that councils lack the skills needed to commercialise successfully. Some 69% of respondents said they were concerned that councils lack such skills, with 31% saying they were confident of the opposite.

Ms Lee said that in Plymouth they "felt it was very important to make sure we had the right expertise" for the council's property portfolio. The council had a history of internal expertise, so made the decision to build on that rather than rely extensively on third-party expertise.

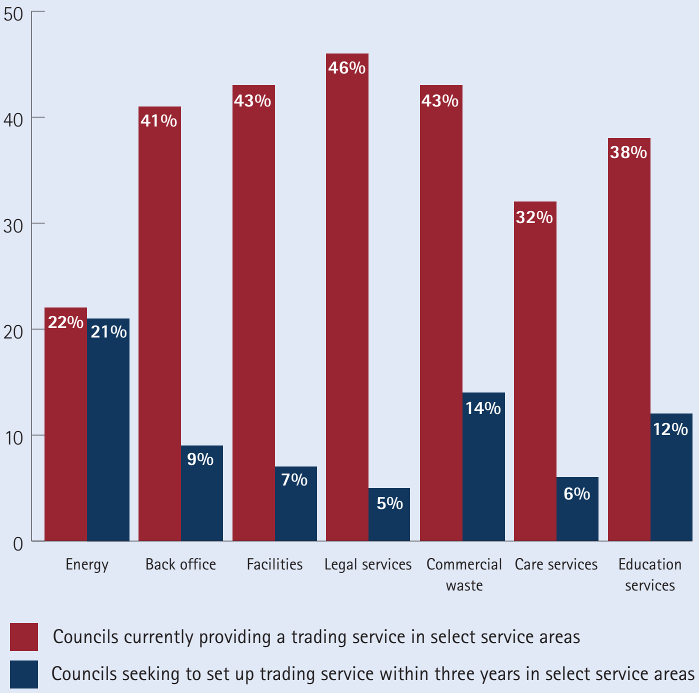
"For us, our internal expertise absolutely understands the local market and has built good relationships with the property sector within the city. We have brought in some extra skills into the team as the portfolio has grown," she said.

"This is not preaching about what's the best way. Everybody must make their own decisions."





Areas councils are currently providing trading services in or seeking to provide trading services in within next three years



Cllr Fleming said that as a smaller district council without a lot of property stock, Sevenoaks DC lacked the right expertise. Its strategy was to hire somebody for a short time to enable it to ask the right questions.

The council then approached an estate agent to access a suite of skills in the property market. Explaining the approach, Cllr Fleming said: "Part of it is about relationship building, and part of it is about going to the right people at the right time."

Much expertise within the property market is associated with protecting against potential downside – and there is risk attached to all commercial projects. Some 78% of those surveyed believed that the commercial risk their council faced was appropriate, with the rest saying it was too great.

Cllr Fleming noted: "The value of investment may go down as well as up. If you're looking for investment income there's always a risk attached to it." But he added that money kept in bank accounts or stuffed under the mattress will be devalued through inflation – itself a risk.

"When we were first having these conversations as a council we had money in the bank. When we looked at it against inflation we were losing value every single day. When we looked at it in those terms the risk of doing nothing was as great as doing something."

Ms Lee said it was important to "make sure you've got a diversified portfolio", that you take account of costs and that you have a long-term strategy. Plymouth has previously invested in direct development where the council felt there was a gap unfilled by the private sector.

"With all of those things you don't go into them lightly, but we're not frightened of part of the investment fund doing direct investment," she said.

COMMENT

JAMES LUPTON
Partner, DWF

Diverse approaches will demand diverse skills

LGC's Confidence Survey 2018 showed a sector in financial distress, with 34% of respondents expecting to issue a section 114 notice within four years. In our survey many were expecting to rely on increasing revenues from commercial activities, with two-thirds of survey respondents expecting their revenues from commercial activity to rise by up to 25% in the next three years.

It appears that part of the answer to generating more income relies on selling more services to third parties. Some 61% of respondents were looking to rely on this activity. Trading with third and private sector parties requires compliance with the provisions of the Local Government Act 2003 or the Localism Act 2011 and the statutory guidance. This requires each local authority looking to trade to form a company, and ensure that trading only commences following approval of a business case and a business plan.

Other key revenue streams are: property sales, as indicated by 59% of respondents; rental income, as indicated by 53% of respondents; and income from commercial development. Local authorities have the powers to be able to dispose, acquire, set up joint ventures, pursue commercial objectives and develop land for commercial returns.

> "Local authorities have the powers to be able to dispose, acquire, set up joint ventures, pursue commercial objectives and develop land for commercial returns. The key to getting this right is obtaining the best commercial advice

The key to getting this right is obtaining the best commercial advice to inform decision making and internal governance approvals. The spotlight is clearly growing on this activity, particularly as this has seen some authorities undertake substantial commercial investments.

As we all know, the value of these investments may go up as well as down.

It is clear there are various approaches to commercialising activities, and it might be this diversity means not all authorities will be wholly confident in their own internal skills, resources and capacity to deliver what is expected. This is surprising given the talent that we encounter when working with in-house colleagues at local authorities.

At DWF, we believe it is vital that external advisers transfer knowledge to local authority clients to leave a legacy of self-reliance. We also see many of our public sector clients increasingly benefitting from speaking to colleagues from other authorities to share knowledge around commercial strategies.

Corporate modelling

From hotels and shopping malls to leisure and commercial waste management, councils are adopting varying strategies in the search for income. **CHRIS MAHONY** reports

Champions of outsourcing and privatisation might sleep uneasily in hotel beds if they knew they were owned by local authorities. Some councils have had stakes in the hospitality business and other surprising sectors for decades, and austerity has given fresh impetus to the search for new income sources.

More mundane – and safer – trading in legal, town planning and back office services is frequently overshadowed by councils borrowing to invest in shopping centres and retail property. The range in commercial activity prompts inevitable questions about what structures and strategies councils are using to make a return.

"It is well documented that some local authorities – largely but not entirely districts – have increased their leverage and exposure to high levels," says Martin Reeves, chief executive, Coventry City Council, and finance spokesperson, Society of Local Authority Chief Executives and Senior Managers.

"It's a mixed picture. Some councils have a history of income generation and working in joint ventures. They have a very strong commercial strategy linked to their medium-term financial plan. They have parameters with areas where they will not go. Others are searching for fast returns on investments that are not part of a coherent strategy."

Councils' strategies span between well-researched local regeneration investments, selling their professional services to other councils and playing the property market. There is a world of difference between these things, says Clive Betts (Lab), chair of the House of Commons housing, communities and local government select committee, and MP for Sheffield South East.

"There are certainly some circumstances where it is part of the local authority's duty to intervene and purchase empty or failing properties in their city centres as part of a plan to develop the area," he says.

"Local authorities can borrow cheaply for such investment, but they need very good data and expertise. That is very different to buying a shopping centre elsewhere in the expectation of raising money quickly."

ALAMY

> We are not frustrated private traders: we are driving income to raise revenues for services

Looking inside

Away from property, there is a lot of other investment activity – some traditional, some novel. Nottingham City Council's cautious expansion

Clockwise from top left: hospitality, waste management, leisure and retail offer investment opportunities for local authorities

has come via its direct labour organisation. A wide range of business units, from leisure to waste management, are clustered together within a broadly conventional council department.

"Even though officers get quite excited about different structures like companies, the waged workforce don't and it causes uncertainty," says Andy Vaughan, corporate director for commercial operations at the council.

"Remaining as a council department rather than a company or joint venture doesn't mean the commercial approach isn't there. You need a strong corporate centre and then it's about leadership and the culture."

Each of the business units has a five-year strategy, with an annual business plan and performance management meetings every six weeks. Mr Vaughan is big on "profit with a purpose" to rebuff the idea that councils should not be making money and that they must always spend big on external expertise.

"We are not frustrated private traders: we are driving income to raise revenues for services," he says. "It is about understanding the market we are working in and rigorous performance management."

He adds that his council has the skills necessary to do that.

The money-making jewel in the department's crown is the commercial waste service. When the council intensified its hunt for new revenue sources in 2010, opportunities for it quickly emerged, Mr Vaughan says. Trade Waste sells its services to businesses locally and in neighbouring areas, and has deals with Derby City Council and Rushcliffe BC.

Nottingham moved in as Rushcliffe exited the sector, while Derby formally delegated trade waste collection in the city early in 2018. Turnover has risen from £4.3m in 2013 to £6.8m in 2018, with a four-fold rise in its surplus to £1.7m over the same period.

"We compete on quality and price," Mr Vaughan says. "We had the capacity to dispose of the waste and with our collections we are now achieving economies of scale. Our own domestic waste takes priority, but it is about knowing the local market and being savvy about using the lorries at your disposal.

"That means having anchor customers but then offering deals to other customers so we don't have trucks coming back half-empty. Rather than a council fees system, our sales force can use flexible pricing."

Trade Waste is now "being more discerning" because it is running out of capacity to dispose of the waste, Mr Vaughan says. His team will explore supply chain integration to address that long term.

This reflects the "incremental versus strategic" approach to commercialisation in Mr Vaughan's mind. The former is doing "a bit more" than statutory responsibilities, but "does not provide enough income now", he says. Strategic commercialisation involves mergers and acquisitions to raise significant profits for other frontline services.

Regeneration game

In Durham, commercial activity is focused on regeneration, the "top priority" for the council, according to Jeff Garfoot, Durham CC's head of corporate finance and commercial services.

"Many of the things we have been doing to further that aim could be deemed commercial," he says. "With austerity many authorities are moving to commercial activity to make money to protect frontline services.

"Our regeneration activities have been turning a profit but it's important to have an effective medium-term financial plan that has given us a strong balance sheet. That gives the cabinet the confidence to engage in commercial activity."

Much of this activity focused on economic development has been delivered through Business Durham, charged with driving the development of new business in the county. This sits within the council as part of regeneration services, but has its own brand.

Business Durham has also invested in a portfolio of offices and laboratories, including the North East Technology Park (NETPark) which the council says is one of the fastest growing science, engineering and technology parks in the UK. As well as being the landlord, Business Durham provides specialist support services for the hi-tech tenants.

The branding is important in winning business round, Mr Garfoot believes, given that companies "often see councils as a waste of time and effort". "From my viewpoint it has always been arm's length, with its own office," he says. "It has been recognised as 'slightly less council' and that has helped it."

Like Mr Vaughan, Mr Garfoot says that larger councils do have a lot of expertise in-house. He argues several factors shape an individual authority's approach. "What people do with commercialisation would depend on size," he says.

Durham CC also raises funds through more conventional local government trading activity, offering professional services to other councils and businesses inside and outside the county. These include the school improvement service, health and safety, and occupational health.

Perhaps more controversially, given criticism about local government's flirtation with the property market, is the creation of the £20m venture capital fund Finance Durham, an extension of the Business Durham brand. The funds are drawn from the council's capital programme, with the fund set up in 2017 and starting to invest a few months later.

So far 10 projects have been invested in on an equity or loan share basis. As part of the agreement, the fund managers and Business Durham provide the firms they invest in with business support intelligence.

The council anticipates its £20m investment being worth £27m by 2027. Mr Garfoot says the council accepts that some projects will fail, and its financial planning does not depend on such a return.

"We expect it to be an evergreen fund: as loans are repaid or we liquidise the equity that money goes back into the fund to be reinvested," he says. "If we were to take £27m out in 10 years' time that would be a windfall to the council."

Commercial activity in Durham is focused on regeneration, including NETPark

Probing partnerships

In nearby Stockton-on-Tees BC, the investment strategy is aimed at both income generation and regeneration. In December the council approved a £30m fund which will be used to buy, rebuild or refurbish property and land in its six town centres.

Chief executive Neil Schneider says the fund will build on existing efforts to repurpose the town centres as multi-purpose rather than retail-focused. This follows significant investment in town-centre based libraries, leisure centres, public spaces and public art.

"We are bucking a trend and we recognise that some of these investments either won't produce a return or will only do so after many years," he says. "It is about regeneration and investing in the place. No-one else is going to do it and the local authority has to have ambition and provide leadership for its place so that we enable the private sector to invest."

Several other major investments by the council are set to produce either savings or profits to fund frontline services. The Hampton-by-Hilton hotel opening in the next few month is fully owned by the council and budgeted to provide a £250,000 profit. A new crematorium developed and owned by the council is expected to contribute a similar surplus.

In each case Mr Schneider says the council engaged external advisers and explored either joint ventures or going out to tender. It decided to press on as sole investor, taking out a £17m loan.

The hotel will be managed on the council's behalf by an external firm, with the council paying to use the Hilton brand. Mr Schneider says that at least six private businesses, including bars and restaurants, have opened within 1,500 metres of the hotel since the decision was taken.

Stockton-on-Tees BC has

We are bucking a trend and we recognise that some of these investments either won't produce a return or will only do so after many years

also embraced the joint venture route. The council is working with a Scottish charity to build a specialist children's home, budgeted to save it at least £200,000 a year by reducing out-of-area placements, in turn improving outcomes for its residents. It will also be building a town centre housing development in a joint venture with a home builder.

Warrington BC is dabbling in the financial sector. It analysed and consolidated its diverse commercial activities into a commercial strategy in early 2017.

Several years before the council partnered with Capita and Lloyds TSB to provide mortgages to local people. Some 200 local households benefited from a scheme that around 60 councils signed up to, later pulled when the government launched its help to buy scheme. With Lloyds TSB publicly owned, the bank felt continued participation in the local government scheme, which had provided around 5,000 mortgages, was inappropriate.

Since then, however, Warrington has gone a step further by establishing its own bank in a joint venture with a City of London financial adviser. Danny Mather, the council's head of corporate finance, says the main reason for doing so was that since the 2008 crash banks have stopped lending to small and medium-sized businesses.

"We were being approached by small businesses and research suggested a £34bn shortfall in lending," he says.

"That was a particular issue in the north-west and we started looking at this at about the same time that the term 'Northern Powerhouse' was first being used."

After significant due diligence and an options appraisal, the council decided to create a bank that would lend on a national basis to small and medium-business, with Mr Mathers saying the national focus was needed to create economies of scale. Four years after the idea was first floated, the bank is operating with a southern base just outside Luton, with six employees at its Warrington office.

Changing times

While councils' approach to investment is attracting rising attention, Mr Reeves argues that fashions in local government's strategy for commercialisation tend to come and go.

"There was a wave a decade ago where councils liked joint ventures where they owned 51% of the stake. In the last 5-10 years the sector has been asking more what they want to achieve in terms of the investment and whether they are looking for a short or long-term return. They've tended to develop a commercial strategy – in other words," he says.

"That is one reason we're now seeing more hybrids: in some case councils are cosying up with community groups in joint ventures, while in others they're creating a big structural organisation."

Still, Solace's Mr Reeves has little time for those who contend that councils lack the right expertise nationally.

"The idea that we as a sector get outmanoeuvred by the private sector is rubbish. The best in the public sector matches the best in the private sector. There is much greater variation within sectors – we are great, for example, at understanding conveyancing and constructing deals," he says.

Such confidence might help those sceptical hotel guests sleep a little easier in their publicly-owned beds.

COMMENT

COLIN MURRAY
Partner, head of local government, DWF

Legal powers exist for all the models councils need

Many authorities have adopted corporate models when looking to trade, deliver homes, acquire assets or regenerate areas. While sometimes this is a legal requirement (pursuant to the Local Government Act 2003 or the Localism Act 2011), there are other occasions when this model is adopted for governance or political reasons.

For example, a local authority may feel the need to set up a separate legal entity to allow the company to be fleet of foot, responding to and engaging with the market. Setting up and operating through a company can ensure that the new activity is released from the bureaucracy associated with the sector.

When setting up a corporate entity, several key decisions need to be made and questions asked: what type of corporate entity is best suited to meet the objectives, who will own the company, who will act as a director of the company, how will the company report back to the authority on progress against the business plan (including approval of the annual budget, and monthly monitoring of performance) and how will it manage state aid considerations?

Many authorities are now well versed in dealing with these issues, having set up and operated companies for several years. Indeed many now have complex group companies to allow different companies to pursue different objectives.

Setting up a company is relatively straightforward. The key is ensuring that the company has a sound business plan which supports a profitable and solvent operation. Depending on its purpose and

"Setting up a company is relatively straightforward. The key is ensuring that the company has a sound business plan which supports a profitable and solvent operation

objectives, the company may need employees, property, an initial cash injection, contracts with third parties and to provide services back to the authority.

Other authorities are more inclined to focus on collaborations with other public sector bodies. This can involve one authority providing services for reward on a commercial basis to another. The Local Authorities (Goods and Services) Act 1970 provides the necessary power to do this, and the arrangement is no different from one where the purchaser buys such services from a third party in the private sector. This is a simple and well-trodden path.

Finally, some authorities agree to delegate functions to another authority. Delegation involves one authority taking over almost entirely the provision of a function from another. Even when payment is involved, it is still a reorganisation of administrative responsibilities between different public bodies.

So while no one size fits all, we are confident the legal powers exist to support the various models that local authorities are adopting to deliver the sector's commercialisation agenda.

COMMENT

MANJEET GILL
Managing director, Chameleon Commercial & Business Improvement

Commercialisation must be guided by a clear strategy, regularly refreshed

As councils grow their commercial approaches – whether from trading internal services or creating housing companies – having a clear strategy is crucial.

A strategy guides what it means to be commercial, what a council wants to achieve and how it can realise its commercial ambitions. It will help provide the focus for where public resources are deployed and how the commercial work will be governed, including monitoring return on investment and managing risks.

Honest conversations about strategy with elected members, management, partners and staff not only helps to locally tailor the focus but allows ownership by all those involved in the commercial approach.

In my experience, it also prevents well-intentioned commercial projects or business plans being dismissed out of hand, demotivating staff and partners.

Commercial strategies should stem from the council's vision and political priorities for its area. They should be based upon a good internal analysis of the council's present assets, strengths, culture and risk appetite.

It should also be honest about its red lines. Some councils wish to reduce workforce costs such as pensions, while others wish to embrace the living wage and avoid creating a two-tier workforce. It is for each council to decide, but these strategic conversations are needed.

Some of the best commercial strategies help internal and external audiences with a

corporate overview of all aspects of what 'commercial' means.

One council I advise on implementation and governance arrangements for its commercial strategy has brought together six strategic themes: land and property, regeneration, trading, companies, commissioning and procurement. It is building on this strategy to increase commercial capability, culture, skills and governance.

As noted above, it is also vital to define what the council means by commercial. For some it is purely about financial return, but

> LGC award winner Rushcliffe BC had clear structured governance from a focused strategy

for many it is also about social good. There may be different strategies for different commercial ventures.

As an example, a commercial strategy for housing development and regeneration will help in defining the council's key projects, the type of returns it seeks and its investment approach.

A council I recently worked with had different political views about the focus for their housing companies. For some it was about financial return, and for others it was about affordable housing. A clear strategy helps to manage tensions within the council and provides clear direction on where resources should be focused.

This brings me to governance. A strategy must clarify the arrangements for governance and define how commercial ideas will be encouraged, developed and appraised.

When we judged 2017's LGC Entrepreneurial Council award, the winner, Rushcliffe BC, had clear structured governance that flowed from a focused strategy, adding value to its community needs as well as generating income. This meant sound management of funding and risks, while allowing innovation and staff creativity.

Governance arrangements, especially for arm's-length vehicles such as companies, are commonly an issue and demand strong mechanisms for performance and risk management, alongside wider oversight. A good strategy should give the principles for governance but allow flexibility and adaptability.

I have also found it is important to refresh commercially strategies regularly. Over time a council may have developed trading arms or companies but as times change or original objectives are met, these will need updating. You can always learn from the past.

CREATING A SUCCESSFUL COMMERCIAL STRATEGY

- Be clear about what you want to achieve and how you will measure success
- Consider the social return as much as the financial ones
- Involve stakeholders, especially councillors and staff, in defining the approach
- Ensure the governance is right for commercial projects and companies
- Recognise and invest in developing capabilities, skills and culture
- Focus on strategy, leadership and governance
- Recognise the process is not simply about creating companies
- Avoid making the process transactional
- Do not assume risk is simply about a risk register
- Expect returns not to appear overnight
- Avoid using commercialisation to do things contrary to the council's values and policies

COMMENT

JOANNE PITT
Policy manager, local government, Chartered Institute of Public Finance & Accountancy

Fears over property investment must not overshadow other commercial success

Local government has seen a decade of austerity, with falling funding and rising demand. When faced with that landscape it is natural any organisation would seek new ways to improve delivery and efficiency. This often presents itself as becoming more 'commercial', but it is important to consider what that means for local government.

Local authorities will be unsurprised that the government is increasingly concerned that some council strategies risk over-dependence on property investments to fund statutory services. In the summer we saw guidance published that was intended to make authorities more cautious when investing, and the policy comments from Whitehall have repeated this line for some months.

But there are two sides to every story, and the other side to this one is that local authorities are trying to balance their budgets and need ways to do this. Options are limited.

Local authorities have reduced the money spent on services and back office support. Where possible, they are raising income through fees and charges. Using reserves is not a long-term strategy, so a rise in more commercial activity seems a natural progression.

This was made possible through the 'general power of competence' introduced in the Localism Act 2011, allowing local authorities to take a more commercial approach to providing services. Through this legislation, authorities can set up trading companies to generate a profit through external trading, and charge for in-house discretionary service.

These companies became popular by offering similar benefits to outsourcing – which local authorities have become disillusioned by – and through their utility in providing shared services. While not all these companies or shared services have been successful, the sector has benefited from the collaborations and co-operation introduced through these trading arrangements, which brought in new skills and experience.

Another form of this activity is found in 'mutual to provide' services. This is where organisations, often under employee control, provide services under contract to the local authority. It can be successful where organisations are looking to generate social gain and improve commercial activity. Although not huge income generators, these arrangements can often find favour with a sector that values local knowledge.

The rise in commercialisation has not been restricted to the creation of trading companies, as local authorities have explored new ways of working with the private sector, which has often developed into business partnering. Examples of this type of commercialisation include joint ventures or local asset-backed vehicles.

While this activity has been challenged, recent case law such as Peters v LB Haringey and Lendlease strengthened the position of local authorities that wish to take a joint venture approach to development. In the High Court case in March 2018, the judge agreed that Haringey LBC's involvement in the development plans was primarily to obtain outcomes in the public good and was consistent with its role as local authority.

Staying with development, we could use the example of 'earn back' as another commercial approach, perhaps best shown by the Greater Manchester CA in the 2012 city deal, under which it could keep £300m worth of additional annual tax receipts after investing £1.2bn in improving infrastructure. This allowed the council to establish certainty for developers, and form a new funding stream, aiding long-term planning and leading to a better financial position.

All of these are examples of commercialisation within the local government sector, and it is a continuing trend that builds and gains momentum on the experience of those involved. Local authorities are taking seriously the skills needed to develop commercially, and staff are now being trained to support this agenda, including by improving their understanding of governance and accounting practice.

It would be a huge loss to the sector, both culturally and financially, if the growth in commercial property investment throws a shadow across these other areas of commercial activity. Entrepreneurial local government, once seen as a paradox, should be open to thrive. But we must find the right balance for local government in this new wave of commercialisation.

> "Local authorities are trying to balance their budgets and need ways to do this. Options are limited… Using reserves is not a long-term strategy, so a rise in more commercial activity seems a natural progression

Wirral MBC

Commercialisation is a bit of moot point for Eric Robinson, chief executive of Wirral MBC. “What we’re actually talking about is income generation,” he says.

In a sometimes clouded debate about what counts as commercial, Mr Robinson’s view is straightforward. Like many local government leaders, he is keenly aware that central government funding is dwindling, and that his council needs income to afford the future.

Wirral has adopted a more commercial approach since Mr Robinson took office three years ago. “Partly I was recruited because I’d set up a lot of new ways of delivering services – a lot of integrated public services,” he says.

Wirral Growth Company is a joint venture geared towards regeneration, including Birkenhead market

The direction was sanctioned by the council, he says. “It just didn’t know precisely how to do it or precisely how it would look.” This is despite Wirral being a Labour-led council, sometimes thought of as less open to taking a business-like approach.

“The phrase income generation is a less politicised phrase than commercial, but actually it’s about broadly the same type of thing,” Mr Robinson says. He adds that generating “social value” is tied in, combining “a private sector head and a public sector heart”.

To effect this change in approach, the council brought in new directors of finance, business support services and even human resources. It even set up a commercial department to bring together all the contracting and commissioning, as well as to provide support for the rest of the council. “What we wanted to do is to get the right permanent people in post here and then create the right cadre of managers,” Mr Robinson says.

Several models have emerged out of this. One is focused on the Floral Pavilion Theatre, located in New Brighton to the north end of the Wirral. Previously it lost the council £500,000 a year. After constructing a business case and examining its options, the council decided it would be best to let a private firm run it without subsidy.

“What you’ve gone through is not a dogmatic view, but a view that is based on a proper piece of work and evidence,” Mr Robinson says. “Actually amassing the evidence is a critical part of that and of finding the best way to solve these problems.”

The council pursued another model for Edsential, a company set up with Cheshire West & Chester Council with a commercially-minded chief executive to better support schools. According to Mr Robinson this has saved the council “a significant amount of money” while maintaining the public service.

> “Each particular area of council activity will have a bespoke answer as opposed to all of them having the same answer

“Each particular area of council activity will have a bespoke answer as opposed to all of them having the same answer,” he says.

Wirral MBC has also done a lot of work integrating various services with other partners to save money, including around community safety, health and social care, and business support activity – the latter involving the local chamber of commerce.

Another big commercial project is the Wirral Growth Company, a joint venture set up with Muse Developments directed towards regeneration. The idea stems from, in Mr Robinson’s description, the council having lots of assets and scarce funds, while partners in the private sector have funds but a lack of assets. In the first three years the company plans to bring in £260m of private sector investment.

This will earn the council a dividend, council tax revenue and business rates. Earnings will be worth £6m next financial year, £8m the following year, and £12m the one after that. “That’s an imaginative and creative way of again doing something that’s needed – regeneration – but actually doing it in a way that earns the council a very, very significant amount of money,” Mr Robinson says.

Given the scope of its activities, Wirral MBC is also integrating its risk management processes more closely, moving from a project-by-project model to a holistic one. Projects are initially assessed on their own merits for risk, then they are considered in the context of other investments. “Now we’ve got enough projects that are moving in this direction we realised we need to look at our risk from the whole of our portfolio,” Mr Robinson says.

Sevenoaks DC

Like many district councils, Sevenoaks DC has in recent years been forced to respond to dwindling financial support from central government.

As Peter Fleming (Con), leader of the council, says: “We had an issue with our revenue budget. Our government funding was disappearing, and we needed to fill that gap. And not all that gap could be found by making savings.”

Commercialisation therefore became a necessity to support public services.

By the council leader’s estimate, some 80-85% of commercial income comes from its property portfolio. Among the assets owned are a pub, a petrol station, office buildings and development sites. The council also charges for green waste collection and runs a garage for MoT tests.

A lack of previous property experience meant that finding expertise from outside was vital. The council brought in expertise in the short term to educate itself and ask the right questions of future partners.

The council ended up using a large real estate company to give it access to a range of skills. “Part of it is about relationship building. It is about going to the right people at the right time,” Cllr Fleming says.

> I think being entrepreneurial is about your ability to see an opportunity

Investing in property is not without risks, a fact highlighted by suggestions from housing and communities secretary James Brokenshire that the government might intervene in council investments. But managing risk for investments does not unduly faze Sevenoaks’ leader.

The council’s 10-year rolling budget also gives it a sense of what the years ahead look like and makes it easier to balance peaks and troughs along the way.

“I think when we were first having these conversations as a council we had money in the bank,” he says. “When we looked at it against inflation we were losing value every single day. When we looked at it in those terms the risk of doing nothing was as great as doing something.”

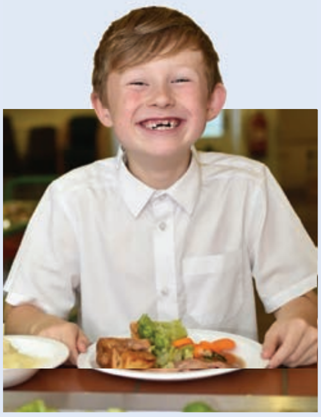
Plymouth City Council

Plymouth has big growth plans. The historic naval city, currently with a population of 264,000, is hoping to grow to 300,000 by 2032. When austerity hit, it opted not to cut back its resources for planning and economic development but to become more commercial.

Tracey Lee, Plymouth’s chief executive, says: “We see the commercial in the widest sense, helping us to fulfil the ambition of the council and the place.”

As well as making money, the council wants to pursue social good. One key example of this is CATERed, a co-operative catering firm giving children hot meals in school and tackling holiday hunger, serving 2.5 million meals each academic year. Both the council and the schools have a stake in improving the lives of the children being fed. Some 67 schools own 49% of the firm, with the council holding the rest. Any money made goes back into services.

> We see the commercial in the widest sense, helping us to fulfil the ambition of the council and the place



Co-operative catering firm CATERed provides hot meals

Plymouth also jointly owns IT company Delt with Northern, Eastern & Western Clinical Commissioning Group, providing the council with a full range of IT services and contributing to health and care integration. The council also has an asset investment fund to contribute to regeneration.

For property, the council has developed significant internal expertise. “We are a council that had quite a large property portfolio anyway, so it was something that we had,” Ms Lee says.

Plymouth has been willing to invest in direct development of factory units, and engage in forward funding agreements, for instance in out of town retail.

“We’re not frightened to do that where we feel there is market failure in terms of the private sector not making the direct investments when the market is there,” Ms Lee says.

Despite this broad array of commercial activity, she says she doesn’t define the council as a “strongly commercial organisation”, but rather one that seeks the best way to achieve things. “I think being entrepreneurial is about your ability to see an opportunity, co-create the solution for that and actually be really clear about the risks that you carry for doing that,” she adds.

Matching risks with returns

Falling funding levels are forcing councils to be more businesslike, but they need to change their culture, acquire the right skills and understand risk, reports **JIMMY NICHOLLS**

"Our section 151 officer may well have pound signs rolling on his eyeballs, but for me the only way we can move forward is if we take a long, hard look at ourselves."

In a single line Wendy Perera, assistant chief executive and director of strategy at Isle of Wight Council, summed up what many councils must feel as they prepare to commercialise.

The opportunity – indeed, necessity – to make savings and generate income is something that both officers and councillors are eager to seize on as austerity continues. The expectation from many is that commercial revenues will form more of council revenue budgets as time goes on.

It was this expectation that prompted LGC and DWF to convene a roundtable on the subject. "It's the single biggest factor of change that we see in our public sector practice," said Jonathan Branton, head of public sector at DWF.

"Councils can operate like businesses to raise money to ensure their services are still standing or ideally flourishing," said Nick Golding, LGC editor and roundtable chair. In doing this, he added, some councils are doing "really exciting things".

> Putting up the car parking charges for us was not commercialisation. That was taxation

PARTICIPANTS

Jonathan Branton partner, head of public sector, DWF
Philip Cox chief executive, Cheshire & Warrington Local Enterprise Partnership
Richard Dolan innovation and technology manager, Tricuro
Martin Farrow CEO, Optalis
Peter Fleming (Con) leader, Sevenoaks DC
Manjeet Gill managing director, Chameleon Commercial & Business Improvement
Nick Golding editor, LGC
Allen Graham chief executive, Rushcliffe BC
Donald Graham chief executive, Hertsmere BC
Colin Murray partner, head of local government, DWF
David Neudegg managing director, Publica Group
Mike O'Donnell associate director of local government, Chartered Institute of Public Finance & Accountancy
Wendy Perera assistant chief executive and director of strategy, Isle of Wight Council
Alison Waller managing director, Tricuro

Surprisingly, given the interest, it is not straightforward to define what commercialisation means for councils. Manjeet Gill, managing director at Chameleon Commercial & Business Improvement and a former local authority chief executive, warned against defining it simply as income.

"One of the things we used to say at West Lindsey [DC, at which she was chief executive for seven years] was 'what is not commercialisation?'," she said. "Putting up the car parking charges for us was not commercialisation. That was taxation."

By consensus, commercialisation is about a broader approach to running a local authority. Allen Graham, chief executive at Rushcliffe BC, noted three strands to his council's approach: investment, arm's length companies and income generation.

Investing income hinged on avoiding undue risk and having a clear strategy with clear governance, he said. Skills and governance are also vital in arm's length companies, he added, while income generation contributes to making the council self-sufficient.

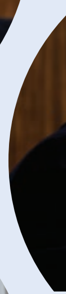
"That's the broad approach to entrepreneurialism and commercialisation within the authority and ensuring it's


Jonathan Branton


Manjeet Gill


Philip Cox


Colin Murray



PETER SEARLE


Donald Graham


Martin Farrow


Wendy Perera


David Neudegg


Peter Fleming


Allen Graham


Mike O'Donnell


Alison Waller


Richard Dolan

not just a buzzword or a fad," he said. "It's about growing it into a culture throughout an organisation that it's acceptable to think commercially."

David Neudegg, managing director of Publica Group, agreed, warning against defining commercialisation as "a collection of things". "Commercial approach is different to commercial trading," he said. "Both might be important, but I think the risk is that you narrow down the agenda and we lose sight of the why."

He also warned that traditional, hierarchical structures "are deeply rooted in local government". To some extent this even spills over to arm's length companies.

Richard Dolan, innovation and technology manager at social care firm Tricuro – an arm's length company – said: "While we inherited a degree of legacy culture from the local authorities that we were formed from, we've also got freedom to bring in new blood."

His colleague Alison Waller, managing director of Tricuro, said that in the three years the company has existed it had "seen a lot of cultural change" as it adopted a more commercial approach. "We've gone through two complete leadership changes in order to get the right commercial skills," she said.

Martin Farrow, chief executive of care service Optalis, added that creating a sense of "togetherness" was key. "If you start linking accountability with blame in a culture it's a real issue," he said.

The interaction between councillors and those carrying out a commercial strategy – be they officers or staff at an arm's length company – is key in defining how the commercial strategy will work out. Donald Graham, chief executive at Hertsmere BC, said: "Officers in my experience are more entrepreneurial than councillors because they're liberated from the electoral cycle."

One way in which this plays out is whether councillors sit on the board. The arrangement can vary, with some councillors insisting they sit on the board, others happy to be absent and some exercising governance through a shareholder panel.

"Where they're on the board they bring their political agendas into the board," Mr Graham said. "So you find instead of having an independent company, you have one with political considerations – especially leading up to an election – influencing those company decisions."

He added that a board's expertise can be bolstered by bringing in good non-executive directors (NEDs) without political affiliation. "That's easier said than done," he said. "It's taken me three years to get five NEDs onto our creative business."

The situation is different for local enterprise partnerships (LEPs). Philip Cox, chief executive at Cheshire & Warrington Local Enterprise Partnership, noted that his partnership had 12 private sector members and three unitary authorities, giving the board "a very commercial perspective".

"I've got the advantage of having three unitary authorities on my patch. Some of my colleagues have to deal with 15 local authorities, which is really challenging," he said. "But those three local authorities are seeing the opportunities of working through us."

Peter Fleming (Con), leader of Sevenoaks DC, replied that he was "trying to keep calm" about Mr Graham's comments about councillors, "as the

only elected member in the room”.

“The fact is that I don’t believe members are the barrier; I don’t believe officers are the barrier. I think some members are a barrier and some officers are a barrier, and some of those barriers come from a lack of skills and a lack of knowledge,” he said.

He added that councillors can supply “huge amounts of commercial skills” that officers cannot, including his own members “who run companies”, “who understand business” and lawyers with experience of commercial projects.

Colin Murray, head of local government at DWF, said that members had to be brought on board for commercial activity. “You’ve got to bring them with you in such a way that they’re on the right side of any governance, in terms of how they interact on a commercial level,” he said.

“Each authority is different. Some authorities are entirely right to have members on the board, because they have the skillset and they bring a lot to it. Whereas other authorities are much happier to take a backseat role and be reported to on an annual basis.”

Many authorities experience problems. Mike O’Donnell, associate director of local government at Chartered Institute of Public Finance & Accountancy, said: “Too often you see companies are being set up and there’s quite an immature relationship on both sides between the company and shareholder.”

He said that the company can want to be “completely arm’s length” and forget that the council is the investor, while councils can mishandle the shareholder function and get too involved in the detail. “These things get complex because they may be there as an investment for financial return but they’re also quite often providing key services in the community or to the council,” he said.

Mr O’Donnell added that within the governance of commercial projects risk must be “a key consideration”.

“That’s not about being risk averse, it’s about being risk aware and understanding what risks you are taking, what the scale of that risk is, and that mix of risks and how that fits into your overall financial strategy,” he said.

He added that councils’ awareness of risk was “variable” – his “diplomatic” view. “I think there are some councils who are very good at it,” he said. “There are some who perhaps a little more naïve and a little less thought-through on what the business case and business plan are for a particular venture.”

> “The appetite for risk absolutely differs between different authorities, and some of them really do have an appetite for risk

Mr Murray said: “The appetite for risk absolutely differs between different authorities, and some of them really do have an appetite for risk and others frankly shy away from what I’d consider to be the lowest risk.”

The day after the roundtable, James Brokenshire, the communities and housing secretary, suggested that central government might intervene in how councils are investing for commercial gain. Many at the roundtable referenced concerns around the property market, which has been a popular commercial target for councils.

Mr O’Donnell noted that if councils are looking at properties that private buyers are eschewing they should ask whether it is a good deal. This was backed up by Mr Cox. “Some local authorities march in, buy up a shopping centre at the same time as being very risk averse about something else,” he said.

However, Donald Graham argued: “We’re all very risk aware.” He said that officers had to measure the risk and point it out to elected members before the latter decide. “The duty of officers is to really point out whether it is a long-term risk, medium-term risk or a short-term risk,” he said.

Assessing risk will depend on the funding situation of a council or given service, as Cllr Fleming emphasised. “There are some services that absolutely are high risk services where you need low risk funding,” he said.

This was echoed by Ms Waller, who called risk “one of our biggest challenges, particularly when you’re dealing with people”. “Particularly in direct care delivery, it’s how do you take risk without putting people at risk,” she said.

However, Cllr Fleming was keen to note the fundamental relationship between risks and returns. “There is no return for no risk,” he said. “I think the biggest shift in my organisation was when members and officers realised the risk of doing nothing was greater than the risk of doing something. And most of the councils I’d argue should be at that state now. You’ve got to do something, because the money will run out.”

One less-discussed aspect of risk also emerged during the talks: whether councils may be creating problems by competing against each other. This could take the form of councils offering incentives to businesses to locate in their area. “Do we

foresee a situation where that could be a self-defeating effect around the public sector marketplace or do we think that competition actually is a really good thing?" Mr Branton asked.

Some were in favour. "We do need competition but you can only have competition if central government gives you the levers and the powers to set corporation tax, business rates, income tax. All of this has some localised element that allows you to drive the economy in your local area," Cllr Fleming said.

Mr Neudegg argued that other models were preferable. "You get all the benefits of competition through collaboration if you put your mind to it," he said. "There's nothing stopping councils collaborating, nothing at all – other than their own mindsets."

Allen Graham said the property market had already provided an example of the dangers of collaboration, as councils competed for the same property. "That was actually an ill-conceived thought for the sector to think actually we can just outbid each other and we're driving the yields down," he said.

"Competition can be damaging if you're not thinking through why you're trying to compete. Equally it's important you are able to collaborate and create competition and create alternatives."

Despite the broad agreement that commercial activity carries risk, there was a consensus that because of local government finances the move towards it was inevitable. As Mr Farrow said: "I think what we can agree around the table is you can't save your way to success. It just doesn't happen.

"From our point of view there are only two things that really matter. The people we support and the people who provide it. They're fundamentally what our organisation is about, and it's driven by the customer."

The debate ultimately turned to that age-old local government topic: devolution. As Mr Cox put it, the Ministry of Housing, Communities & Local Government will "decide where this is going".

"If they are prepared to allow devolution and if they're prepared to get that greater alignment of incentives between local authorities and the commercial sector, we can be more successful," he said. "They're struggling with that devolution agenda."

COMMENT

COLIN MURRAY
Partner, head of local government, DWF

Commercial approaches hinge on core questions

The roundtable discussion showed that each local authority has its own unique commercial objectives, means and methods of delivery. These objectives are often a product of the authority's history and strengths.

For example, Wirral MBC is keen to exploit its physical assets through the formation of an enterprise zone. Meanwhile Hertsmere BC's acquisition of Elstree Studios in 1996 has allowed it to create a unique and successful income source, and other authorities have commercialised their strongest service areas, including energy, legal and adult social care.

No one size fits all and that is why we always listen carefully to clients' commercial objectives before setting out how they can be delivered, both in accordance with the law and internal governance structures.

While it was evident from the roundtable that a tailored approach is vital when it comes to commercial strategies, there were several core legal questions that needed to be dealt with.

First, can the authority do what it wants to do and what powers can be relied on to achieve the commercial objective?

Second, what must an authority do to comply with any legal or procedural requirements? These can include consultation regarding a change in service provision, equalities impact assessment, state aid compliance, business case approval by elected members, avoiding procurement regulations through a regulation 12 arrangement and Companies House requirements.

Third, what legal structure and agreements are needed to document the new commercial activities? We find it often helps to draw the structure on a single sheet (setting out the parties, the ownerships and financial contributions) and simply list the agreements needed to put it into practice (including a brief description of each agreement's purpose and heads of terms). Once this is completed, the authority can move on to deliver its implementation plan against agreed dates.

Fourth, what governance arrangements are appropriate to support the delivery of the new commercial activities? These can take some time to agree and document but it is time well spent.

Fifth, do the commercial activities have an impact on employees' terms and conditions and pension benefits? Will it involve a TUPE transfer from day one, and what policy will be adopted on new joiners in due course?

Sixth, has the authority adopted a tax-efficient legal structure and have tax considerations (for the local authority, customers and companies) been included in the business case?

And finally, are there any insurance implications arising from the commercial activities?

It is important that the legal issues complement a thorough, realistic and stress-tested business plan. In our experience, the business plan is fundamentally important to the success (or otherwise) of any commercial activities. This is sometimes a legal requirement, and even when not formally required it makes sound commercial sense to sign off a detailed business plan.

COMMENT

JIMMY NICHOLLS
Features editor, Local Government Chronicle

Commercial activity is risky business, but local authorities have few alternatives

When Theresa May announced that austerity was over last October many in local government were justifiably sceptical. Central financial support for councils is fast disappearing, demand for social care is on the rise and nobody appears to be coming to the rescue.

As shown by LGC and DWF's research, many in local government decided to take matters into their own hands some time ago by seeking to generate income through commercial activity, with a majority of these intent on expanding their efforts.

Our survey reported that two-thirds of senior council officers expect commercial revenue will be up 0-25% in the next three years – though for some this will be from a low base.

In several categories more than 50% of respondents expected revenue growth, including council-owned trading companies, property sales, car parking and rental income. New trading services are expected in sectors as diverse as energy (21% of respondents), commercial waste (14%) and education services (12%).

> Commercialisation is not merely about money. For many the aim was 'to find ways in which people who are excluded or more vulnerable are able to benefit'

All of this will plug holes in council finances, which are expected to grow precarious for more councils in 2019. Some money can be clawed back through efficiency savings, and councils may also receive dividends from profitable services. In some cases profits are ringfenced and put straight back into the service that generated them.

But commercialisation is not merely about money. Eric Robinson, chief executive of Wirral MBC, speaks for many when he says the aim was "not just earning money but being able to find ways in which people who are excluded or more vulnerable are able to benefit".

Most of those spoken to in compiling this report emphasised the need for a clear strategy before commercial projects are embarked on, and this means thinking beyond the bottom line and doing the research before work begins, considering wider economic and social impact.

Plymouth City Council, which is looking to grow its population from 264,000 to 300,000 by 2032, pursues property projects with an eye on how it will affect housing and local jobs. Plenty of commercial projects also make use of local suppliers.

In all this governance is key, and the involvement of councillors somewhat controversial. A mix of models exists: some arm's length company boards have members sitting on them, while some do not, relying instead on supervisory panels. This is contingent on councillors' experience as well as their preferences.

> Some projects will inevitably fail, as with all business endeavours, and councils must assess risk within the context of their overall finances

Donald Graham, chief executive at Hertsmere BC, says: "Officers in my experience are more entrepreneurial than councillors because they're liberated from the electoral cycle."

But Peter Fleming (Con), leader at Sevenoaks DC, argues that both councillors and officers can be a hindrance or a boon. The debate will roll on.

What is not being debated is that getting the right skills for commercial projects is essential. Some councils, including Plymouth, have built expertise from an initial base in their property holdings. Meanwhile, Sevenoaks has looked externally for help. Many variations exist between these two models.

The risk of commercial projects is naturally at the heart of this search for skills.

As Cllr Fleming argues: "There is no return for no risk." Given the jeopardy of some council's finances, finding new funding sources is imperative for many. But some projects will inevitably fail, as with all business endeavours, and councils must assess risk within the context of their overall finances.

Whether central government will intervene if they feel a council's situation is too risky, as housing and communities secretary James Brokenshire suggested in December 2018, remains to be seen.

It is almost traditional to end these reports with reference to geopolitical uncertainty, and the UK's efforts to extricate itself from a local trading bloc. Given the speed of developments, speculation is itself risky. What is not in doubt is that it will have implications for local government finances.

Optimists may continue waiting for Ms May to make good on her promise to end austerity, in which case the need for commercial projects will dwindle, at least relative to funding. But in this case the maxim to hope for the best and prepare for the worst seems particularly apt.

Many councils are showing they are adept at using their local knowledge to plug gaps in existing commercial supply. Local government commercialisation is here to stay.

COMMENT

JONATHAN BRANTON
Partner, head of public sector, DWF

Strategy, accountability and the right legal structures can ensure commercialisation is a success

In developing this report, DWF and LGC looked to better understand the type of commercial activities being undertaken across local government, the challenges and the barriers that authorities face and some of the biggest successes to date. We hope that some of the fantastic insight that this report contains will help you shape future commercial strategies, and we wanted to highlight some key points.

1. Develop a sound and supported commercial strategy

It is vital to have a formal, concise commercial strategy that clearly articulates what you want to deliver, as Manjeet Gill showed on page 10 in setting out what steps she took as a serving chief executive. The strategy should be supported by senior executives and approved by elected members. This public document should inform employees of the corporate values and culture of the authority, providing a rallying call to commercialisation.

2. Make the right people accountable for delivery

Commercialisation will not happen without a concerted effort and needs to be

> "It is vital to have a formal, concise commercial strategy that clearly articulates what you want to deliver

implemented effectively. You should consider appointing a champion within the organisation who is responsible for delivery. We have seen an increasing number of commercial directors appointed over the last few years with a mandate to generate income, while other authorities have delegated authority to section 151 officers or other senior executives.

Once your strategy has gained full support, accountability for delivery should be incorporated into any delivery model. Whether it is the CEO of the new company or a head of service, when collaborating or contracting with other public sector partners the responsible individuals should report into the authority on performance against the business case. Monitoring and budget setting should be enshrined into the governance arrangements.

3. Adopt the right legal structure and document it

As we have seen in this report, local authorities have options available to them to deliver their commercial objectives. Before embarking on any commercial activity we advise that you conduct an assessment of which model best meets your needs.

The choice of model should only be made once you have a clear view on what you want to achieve; where the money is coming from; an understanding of the law which may require you to adopt a particular model or satisfy procedural requirements; implications of

> "Commercialisation naturally centres on financial prudence. One of the best ways to ensure success is to prepare a thorough business case

tax, insurance, employees, pensions, state aid, procurement and other regulatory requirements; and a business case and plan.

Once the legal structure has been selected, the new arrangements should be documented and kept up to date. This is not to be taken lightly, or omitted, as without it the formal glue supporting the new arrangements will not exist and as corporate memory fades, accountability and performance monitoring can falter.

4. Prepare a business case

Before proceeding with any commercialisation project, participating authorities will want to establish a robust financial analysis of the likely costs, the risks and anticipated financial benefits. This should cover budgeting, monitoring expenditure, income and cash flow, producing statements of accounts, audit requirements and taxation. The purpose of the business case is:

- To demonstrate to members, potential investors and the company board that the business is a viable enterprise, with an identified market, an achievable set of business objectives, and adequate managerial and other necessary skills and experience
- To assure potential clients the business is well-run and has the capability and resources to ensure reliability and quality
- As an internal management tool to ensure that all parts of the business work together towards common and consistent goals, and that these goals are based on sound analyses, assumptions and are consistent with the authorities' objectives

The business case will enable you to decide whether or not you should proceed with the commercial activity. You should not view it as a failure if the assessment results in the proposal being rejected. This is good governance (and financial prudence) in action.

5. Be brave and relentless!

Commercialisation involves varying levels of risk and it is important to tailor the level of scrutiny that you undertake to the level of risk. Many authorities have already taken significant steps to embrace the commercialisation agenda and we hope that through our work with LGC you feel better informed about what others are doing to develop and deliver commercial strategies.

We strongly advise that you reach out to others within the sector to learn more about how they have delivered their objectives. We look forward to working with the sector as it continues to embrace commercial agendas.