

**Title of meeting:** Cabinet

**Date of meeting:** 8<sup>th</sup> December 2016

**Subject:** Utility and Engineering Trading Company

**Report by:** Owen Buckwell - Director of Property

**Wards affected:** None

**Key decision:** Yes

**Full Council decision:** No

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**1. Purpose of report**

- 1.1 To seek approval for the formation of an arm's length trading company for the purpose of delivering energy and engineering services to a wide range of external organisations, and capable of operating as a provider of district heat and power. The company will seek to increase income to the council through an appropriate commercial and legal framework.

**2. Recommendations**

That Cabinet approves to the following recommendations:-

- 2.2 To instruct the City Solicitor, in conjunction with the Leader of the Council and the Cabinet Member for Resources, to form an arms-length energy and engineering services company as a group company under a wholly owned holding company, and capable of delivering and operating district heat and power schemes, as described in the Appendices to this report.
- 2.3 That the City Solicitor, the Director of Finance and Section 151 Officer, in conjunction with the Leader of the Council and the Cabinet Member for Resources, be authorised to enter into such company constitutional documents and service and supply agreements with the company as are required by the company for its operation, and for the Council/holding company to most effectively manage its operation.

**3. Background**

- 3.1 A proposal for an energy services arm's length company has been drawn up to assist in the delivery of services and supplies (described in the accompanying *business case*) to external public and private sector organisations, to increase

income to the Council, whilst helping to achieve the Council's commitment to reduce regional carbon emissions and improve the profitability and environmental conditions of neighbouring organisations.

- 3.2 The Council's energy services activities already involve providing services external organisations such as Southampton City Council schools, Gosport Borough Council and the University of Portsmouth. The Council have other potential clients keen to utilise the range of energy services.
- 3.3 In order to trade in services and supplies for a profit, the Council is obliged to operate through a company, so the creation of a company will enable the Council to access a wider customer base - and will allow for a profit to be realised on the provision of services and will allow the Council to act on a commercial basis, enabling it to compete for business.
- 3.4 It is anticipated that the Council brand will be a unique selling point of the company, and is expected that the company will help to grow and develop the Council's brand. Whilst other organisations within the market place offer similar services, none are known to offer complete solutions delivered entirely in house.
- 3.5 The company will support local and regional organisations by reducing their operational costs associated with utilities, whilst reducing carbon emissions and improving internal environmental conditions.
- 3.6 The target market for the company will initially be local organisations with a combined utility expenditure of £30,000 per annum which represents approximately 20% of all business within the UK. The majority of these organisations do not have any utility or engineering expertise in house.

#### **4. Reasons for recommendations**

- 4.1 In order to carry out activities for the purposes of realising a profit, the Council needs to do so through a company. On the basis of the findings referred to in the business case, it will:
- 1) Generate income from the sale of utility and engineering services to the non-domestic sector; by employing Council officers via a resourcing agreement, generating interest on lending, and paying the Council as the single shareholder a dividend of the company's profits.
  - 2) The retention of profits by the company will help mitigate against the additional investment risk from this new area of commercial activity.
  - 3) Achieve the full potential of delivering services that would otherwise be limited, due to restrictions on the amount of allowable activity in the private sector. Some of the services available are expected to be highly profitable compared to the amount of resources and capital required to

deliver these services. Profit margins such as these would not be realised under direct-provision arrangements.

- 4) Enable a separate, more responsive and commercial operation.
- 5) More economically address the council's sustainability agenda.
- 6) Limit liability and risk to the Council.

4.2 Whilst Arm's Length Companies are increasingly becoming a feature of local government. A number of other local authorities have companies which deliver some of the services outlined in the Business Case, however no other provider, as far as has been determined, are offering the range of commercial services proposed.

4.3 The company operations will be undertaken by the Authority's existing staff via the resourcing agreement. However, should the company require further dedicated resources in the future then these will be employed directly and funded wholly by the company.

## **5. Equality impact assessment (EIA)**

5.1 A preliminary EIA was considered but after proceeding through the process it was assessed that an EIA would not be required in this instance. The traded services proposal relates to a commercial enterprise which will operate externally to the Authority and will not impact the equality groups. The customer base will be medium to large sized companies in the southern region. The decision whether to proceed with delivering services to these external companies would be based purely upon a financial appraisal and will not impact negatively on residents/customers of various protected characteristics across the city.

## **6. Legal implications**

6.1 The Council has the power to set up, participate in, and appoint directors to a company for the purposes set out above.

6.2 The Council may also provide services and support to the Company, provided they are on commercial terms.

6.3 As the Company will be operating on a commercial basis, in order to comply with the rules on state aid, in most instances its relationship with the Council will need to be commercial. Loans, and service-support, should not be at an undervalue, and should be commercial.

- 6.4 The Company will be owned 100% by the Council. It will require bespoke Articles of Association, a shareholder's agreement, and a strategic/partnering agreement, in order to properly empower it, creating certainty for both it and its directors, but appropriate oversight and control for the Council.
- 6.5 For example, powers may be reserved, appropriate limits on the powers of the Directors in relation to the disposal of assets, setting of pay, and participation in subsidiary companies or partnerships, and an investment strategy may be set.
- 6.6 Bespoke articles would also include powers for the Council, as shareholder, to replace directors if they are no longer officers or members of the Council.
- 6.7 The use of bespoke articles and a shareholders agreement may also be used to address any other issues relating to the company.
- 6.8 Once the company is set up then secondment and services agreements will be needed to enable directors appointed to operate. It will need to enter into secondment agreements for the directors and appropriate service contracts with them.
- 6.9 The Council will also have to set up appropriate service agreements with the company to provide it with legal, HR, finance and other professional services.
- 6.10 There are a number of names under consideration for the Company; a name will be decided upon following approval of the proposal to set up the company.
- 6.11 As is set out in the report it will be essential to obtain specialist tax advice the Company to ensure that there are no adverse consequences either for it or for the Council in any specific transaction.

## **7. Finance comments**

- 7.1 This report seeks to present the business case for the formation of an Arm's Length Company, with the primary objective of delivering energy and engineering services that will maximise the return to Portsmouth City Council.
- 7.2 The company will initially have no funds of its own. A temporary finance provision would need to be made to cover company formation and development costs and it is proposed that these costs, totalling £60,000, are funded from the existing Utilities Management scheme in the approved Capital Programme. This financing would be repaid with interest accrued at a commercial rate, once profits are generated.
- 7.3 The anticipated costs will include:
- The cost to the Company of Council staff time via the resourcing agreement during the setup phase;

- Marketing and web services;
- The cost of the Company's formation with Companies House;
- The cost to the Company of Council staff time via the resourcing agreement for initial business development and non-capital projects, such as consultancy work.

7.4 In the event that the Company identifies further investment opportunities that deliver a positive financial return for the City, a further report will be brought to Cabinet, backed by a sound business case and a robust financial appraisal approved by the Director of Finance and Section 151 Officer, prior to further investment into the Company being approved.

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Signed by:

**Appendices:**

Appendix A Initial Business Case to set up Holding Company

Appendix B Consideration and Way Forward

Appendix C Service Description

The recommendation(s) set out above were approved/ approved as amended/ deferred/  
rejected by

..... on .....

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Signed by: