

FLINTSHIRE COUNTY COUNCIL

REPORT TO: **HOUSING OVERVIEW & SCRUTINY COMMITTEE**

DATE: **FRIDAY, 13 DECEMBER 2013**

REPORT BY: **CHIEF EXECUTIVE, HEAD OF LEGAL AND
DEMOCRATIC SERVICES AND HEAD OF HOUSING**

SUBJECT: **LEGAL AND GOVERNANCE ISSUES AROUND
ESTABLISHING A PROPOSED HOUSING COMPANY**

1.00 PURPOSE OF REPORT

1.01 To explain the legal and governance issues around the establishment of the proposed housing company and to approve its creation.

2.00 BACKGROUND

2.01 At its meeting on the 15 October Cabinet resolved:

- (a) That urgent work be commissioned to develop the legal and governance model for the company; and
- (b) That officers report back to Cabinet and the Housing Overview and Scrutiny Committee with detailed proposals for establishing the company.

2.02 In complying with that resolution officers have used the feedback gained from an Overview and Scrutiny seminar (to which all Councillors were invited) which took place on 11 October as well as advice from external solicitors to draw up some proposed governance arrangements for the housing company. The need for the company is understood and its purpose widely supported by members and officers. Further assurance is required over the governance of any such company and how it can be appropriately controlled by the Council.

2.03 When establishing a company of this sort there is a fundamental question to be decided about the level of independence to be enjoyed by the company. In summary, the less control the Council has over such a company, the greater its freedom from other regulatory burdens such as reporting and the public procurement rules. In this instance it is appropriate that the level of Council control should be very high (at least during the company's early years). This will mean it is subject to quite a high level of regulation but this should not prove a hindrance to the company's ability to achieve its desired aims.

3.00 CONSIDERATIONS

3.01 There are a range of issues that need to be considered when setting up a company of this type. For the purposes of this report these issues are presented under the following headings:-

- Purposes
- Corporate Model and Statutory Powers
- Council Control
- Employment
- State Aid
- Reporting and Accountability
- Internal Controls and Governance
- Business Planning

3.02 Purposes

During its early years this particular company would be expected to undertake the following activities:-

1. Owning and letting its own properties.
2. Leasing and sub letting properties.
3. Letting and managing properties on behalf of private landlords.

In future years it is possible that, as the company grows it can expand and take on further roles such as property development/house building. It would be possible to establish the company with just a limited range of purposes at the outset and to add additional powers as and when ready. However, it would be the preferred option to establish the company with wider powers at the outset and then to restrict its activities through its business plan and control of the board, allowing it to expand and grow as it proves itself in governance and performance. Given the high level of control that will be exercised by the Council over the company, officers advise that it is safe and appropriate to give it unlimited powers from the very start.

3.03 Corporate Model and Statutory Powers

There are different legal entities that can be used to establish a company of this sort:- a company limited by shares (CLS), a company limited by guarantee (CLG) and an, industrial and provident society (IPS). The two company models are the most flexible. They would enable the Council to tailor the corporate arrangements to suit its purposes, whilst still building in sufficient safeguards to protect the public interest.

3.04 Both models have a board of directors that 'run' the company. They also have owners (either members for a CLG or shareholders for a CLS) who set the strategic direction. A CLG is no more flexible and offers no more security than a company limited by shares. By contrast, a company limited by shares makes it easier to have different levels of ownership rights (by issuing differing categories of shares with fewer or

greater rights) and in addition the existence of shares will make it easier to raise investment (by selling share capital) or to dispose of the company as a whole should that be desired in the future. Officers recommend using the CLS model.

3.05 It is intended that the company will generate a trading surplus by its activities, which will be subject to Corporation Tax. That net surplus could either be reinvested in the company or could be distributed to the Council for it to spend on delivering local public services. For it to be able to distribute its surplus in that way the company cannot be a charity nor can it be established under the Council's well-being powers pursuant to the Local Government Act 2000. It is therefore recommended that the company should be established under S.95 of the Local Government Act 2003.

3.06 **Council Control**

The Council will be able to exercise control over the company through two routes:-

- Ownership of shares; and
- Control of the board of directors

Company shareholders fulfil a strategic role by approving certain matters at shareholder meetings such as the annual business plan and accounts. It is possible to stipulate that certain matters must be approved by shareholders or even that specific shareholders must approve particular decisions. So for example, it would be possible to say that the holder of the Council's share must approve decisions on the distribution of any surplus. This will in effect give the Council an appropriate 'veto' over key decisions. It is recommended that such a veto be reserved to the Council in respect of the issue of share capital, the distribution of any trading surplus, the approval of the business plan and the disposal by way of long lease or sale of the freehold of any properties owned by the company and securing any borrowing by the company against its assets.

3.07 In addition, the Council can reserve the right to appoint directors to the board. Officers would suggest that the board be limited to about 5 or 7 positions with the majority being held by councillors. There should be an officer to act as executive director who can actually carry out decisions on behalf of the company and the board. There should also be some form of non executive appointment of a person with expertise in the housing field but who is neither a councillor nor an officer, in order to give a fresh and external perspective.

3.08 **Employment**

Whilst the company is still small it is expected that it would buy whatever services it requires from the Council. Council employees

would remain employed by the Council but could also undertake functions on behalf of the company. They would not be paid any extra for doing so, the role being built into their job description as an extension of their current role, and the payments made by the company for the services would be an income stream for the Council. In some circumstances this will not be appropriate, for example where Council employees do not have the necessary skills or experience or the time and capacity to undertake the work, or where the company needs independent professional advice e.g. where it is entering into a legal agreement with the Council it will need its own separate legal advisor.

3.09 Given the high level of Council control over the company, it will be a “contracting authority” within the public procurement rules. That means that it will need to follow the EU procurement rules to let any contract with a value of more than £174,000. Given the small scale of the company during its early years, it is unlikely that any contract placed with the Council will exceed that sum.

3.10 **State Aid**

If the Council sells its services to the company and charges for any other benefits e.g. the company will need a registered address, then it is unlikely that arrangements between the Council and the company will be classed as state aid. However, should the Council give the company any form of asset or service at a reduced or nil cost then the state aid rules might be engaged. Specific external legal advice is being sought about the transfer of gifted properties from the Council to the company.

3.11 **Reporting and Accountability**

It is proposed that the Council would exercise control over the company through appointing its directors and by reserving the right of approval over certain matters. Those already powerful controls can be further enhanced by careful allocation of those roles.

3.12 The right to cast the Council’s vote as shareholder should be exercised by the Cabinet Member for Housing. This which will ensure that key decisions are taken in accordance with the wishes of the Cabinet. Any officer appointed to the board should be a senior one but below the level of chief officer. This will mean that the head of service is free to exercise control/accountability over the officer appointed. Likewise, councillors on the board should not be on the Cabinet. In that way, Cabinet members will be free to debate issues affecting the company without needing to declare a personal and prejudicial interest under the Code of Conduct.

3.13 Ordinarily, a company produces an annual report for its shareholders which is received at the Annual General Meeting (AGM). Given the level of control that the Council wishes to exercise over the company, it will

be appropriate for it to give more frequent and transparent accounts of its activities. It is recommended that the company should report regularly to Cabinet and the relevant Overview and Scrutiny Committee at a frequency to be agreed and no less than six monthly

3.14 The company will be required to produce its own set of annual accounts including: balance sheet; profit and loss account; director's report; and an auditor's report following the audit of the accounts. An annual corporation tax return will need to be completed. The accounts will be filed with Companies House and will be available for public inspection.

3.15 As a wholly owned subsidiary of the Council, the company's accounts need to be incorporated with our own accounts to form group accounts. The group accounts will be subject to scrutiny every year by the Audit Committee and Full Council as at present.

3.16 **Internal Controls and Governance**

Once the company is established it will need to draw up its own procedures and systems to ensure good governance. For example, it will need its own financial procedure rules, arrangements for ensuring internal control and rules for placing contracts. In order to ensure that those procedures are sufficiently rigorous and transparent the Council can require them to be approved by the board of directors.

3.17 **Business Planning**

The Head of Housing has commissioned the preparation of a business plan for the company. The business plan will cover:

- the objectives of the company
- the investment and other resources required to achieve the objectives
- any risks to the business; and
- the expected financial results of the business.

The business plan will need to be checked and approved once it is complete.

3.18 **Recommendations that will be made to Cabinet**

The following recommendations will be made to Cabinet in order to take this matter forward:

1. That the housing company is established as a company limited by shares as set out in the report on the basis that the Council is assured of having a sufficient level of control of the body.
2. That the Chief Executive, Head of Legal & Democratic Services, Head of Finance and the Head of Housing Services in

consultation with the Leader and the Cabinet Member for Housing be given delegated authority to take all necessary steps to establish the company.

3. That the Chief Executive in consultation with the Leader and Cabinet Member for Housing be given delegated authority to approve the business plan.

- 3.19 In addition, because of the complexity of setting up a company and because it is the first time that this has been undertaken for a very long time, a multi-disciplinary group consisting of Finance, Housing and Legal officers will be formed in order to ensure that all necessary issues are addressed.

4.00 RECOMMENDATIONS

- 4.01 That the Committee passes its views on the proposed legal and governance arrangements to the Cabinet meeting on 17 December.

5.00 FINANCIAL IMPLICATIONS

- 5.01 There is a small cost to establishing the company and to taking the necessary legal, financial and tax advice to set it up. This can be met within existing budgets.
- 5.02 The business plan currently being prepared for the company envisages that it will not require any start up capital from the Council. In the future the company may wish to borrow money and might ask the Council to stand as guarantor (due to the Council's very high credit rating) and each such request will be considered on its merit at the time.
- 5.03 Should the company not prove to be successful then the Council will not be responsible for its debts which will be paid off from the company's assets. It is possible for the Council to place a restriction on the disposal of any houses owned by the company so that they will continue to be used for public purposes even if they need to be sold to clear the company's debts.

6.00 ANTI POVERTY IMPACT

- 6.01 At present average earnings within the county are below the level required to afford average rental incomes. Whilst mortgages are cheaper, it is still difficult on the average county income to save the required level of deposit to purchase a house. Therefore there are people within the county who can neither afford to rent nor to buy at market levels but who do not qualify for social housing. It is anticipated that by letting properties below market rents, but above social rents, the housing company will assist such people.

7.00 ENVIRONMENTAL IMPACT

7.01 None.

8.00 EQUALITIES IMPACT

8.01 Currently, there are elderly residents within the County who are living in houses that are larger than their needs and are thus difficult to heat and maintain. However, because they own an asset, they do not have sufficient points to be eligible for sheltered accommodation. The housing company could take a lease on their properties during their lifetime enabling them to move into sheltered accommodation whilst freeing up much needed family sized accommodation.

9.00 PERSONNEL IMPLICATIONS

9.01 The workload involved in establishing and working for a company can be accommodated within existing resources.

10.00 CONSULTATION REQUIRED

10.01 None.

11.00 CONSULTATION UNDERTAKEN

11.01 A seminar has been held on this issue for all members of council and its views taken into account in drafting these proposals. All appropriate senior officers have been consulted. External expert advice has also been obtained.

12.00 APPENDICES

12.01 None.

**LOCAL GOVERNMENT (ACCESS TO INFORMATION ACT) 1985
BACKGROUND DOCUMENTS**

As referred to in the report.

Contact Officer: Gareth Owens
Telephone: 01352 702344
Email: gareth.legal@flintshire.gov.uk