

Cherwell District Council and South Northamptonshire Council

Joint Commissioning Committee

1 December 2016

<p>Progress on the Establishment of a Joint Revenues and Benefits Teckal Company</p>

Report of Assistant Director - Transformational Governance

This report is public

Purpose of report

To update members on progress with regard to the legal and financial due diligence with regard to the setup of joint local authority owned companies and in light of this request members to amend their decision set out in Minute 33, resolution 5 of 15 September 2016 meeting.

1.0 Recommendations

The meeting is recommended:

- 1.1 To note the progress on activities that is taking place with regard to the establishment of the companies.
- 1.2 To agree to amend their decision as set out in Minute 33, resolution 5 as set out in recommendation 1.3 and 1.4 below.
- 1.3 That officers be requested to establish and register a joint local authority owned teckal company limited by guarantee operating within a Mutual Trading Status with South Northants Council and Cherwell District Council as equal members of the company to deliver in the first instance a revenues and benefits service to the councils.
- 1.4 That subject to further tax advice officers be requested to establish and register a joint local authority owned sister trading company with South Northants Council and Cherwell District Council as equal owners, either through company limited by shares or a company limited by guarantee, as appropriate based on financial and legal advice.

2.0 Introduction

- 2.1 At the last meeting of the Joint Commissioning Committee on 15 September 2016, the committee considered a report to enable the establishment of joint local authority owned companies to enable the establishment of a teckal company, in the first instance deliver revenues and benefits back to the council and a trading subsidiary to sell services. Since the last meeting KPMG have been carrying out tax modelling to ensure that the form of the companies takes the most effective tax position for the council. At the last meeting based on initial legal advice and subject to legal and financial review agreed the following resolution:

Minute 33

- (5) That the South Northamptonshire Council Cabinet and the Cherwell District Council Executive is requested to establish and register joint local authority owned companies limited by shares comprising a principal Company to be wholly owned by the Councils in equal shares and a subsidiary trading company to be majority owned by the principal company with a minority interest owned by the Councils to enable the Revenues and Benefits Business Case and other future commercial opportunities to be achieved.

- 2.2 Since this time following detailed discussions with KPMG and Trowers and Hamlins, it has been established that the most effective model for the Council is for the teckal company to be a company limited by guarantee with South Northants Council and Cherwell District Council as equal members of the company. Similarly in order to protect the tax efficiencies created by the company limited by guarantee operating within a Mutual Trading Status with the councils, external trading should not be through a subsidiary company but through a sister company owned equally by the councils, which will most likely be a company limited by shares or a company limited by guarantee, subject to further consideration of tax implications.

This report requests members to amend their decision made at the last meeting in light of the information contained in this report.

3.0 Report Details

Background

- 3.1 The Revenues and Benefits Business Case was considered and approved by the Joint Commissioning Committee in May 2016 and Cabinet and Executive in June 2016. The business case set out the proposal to establish a Joint Revenues and Benefits Service across Cherwell District Council (CDC) and South Northamptonshire Council (SNC). The new joint team would be established and fully resourced in time for the insourcing of the current CDC capita contract in May 2017.
- 3.2 On implementation the new joint service would deliver the current revenues and benefits functions for CDC and SNC (including managing the Capita contract at CDC). The capacity of the service would then need to be increased in preparation

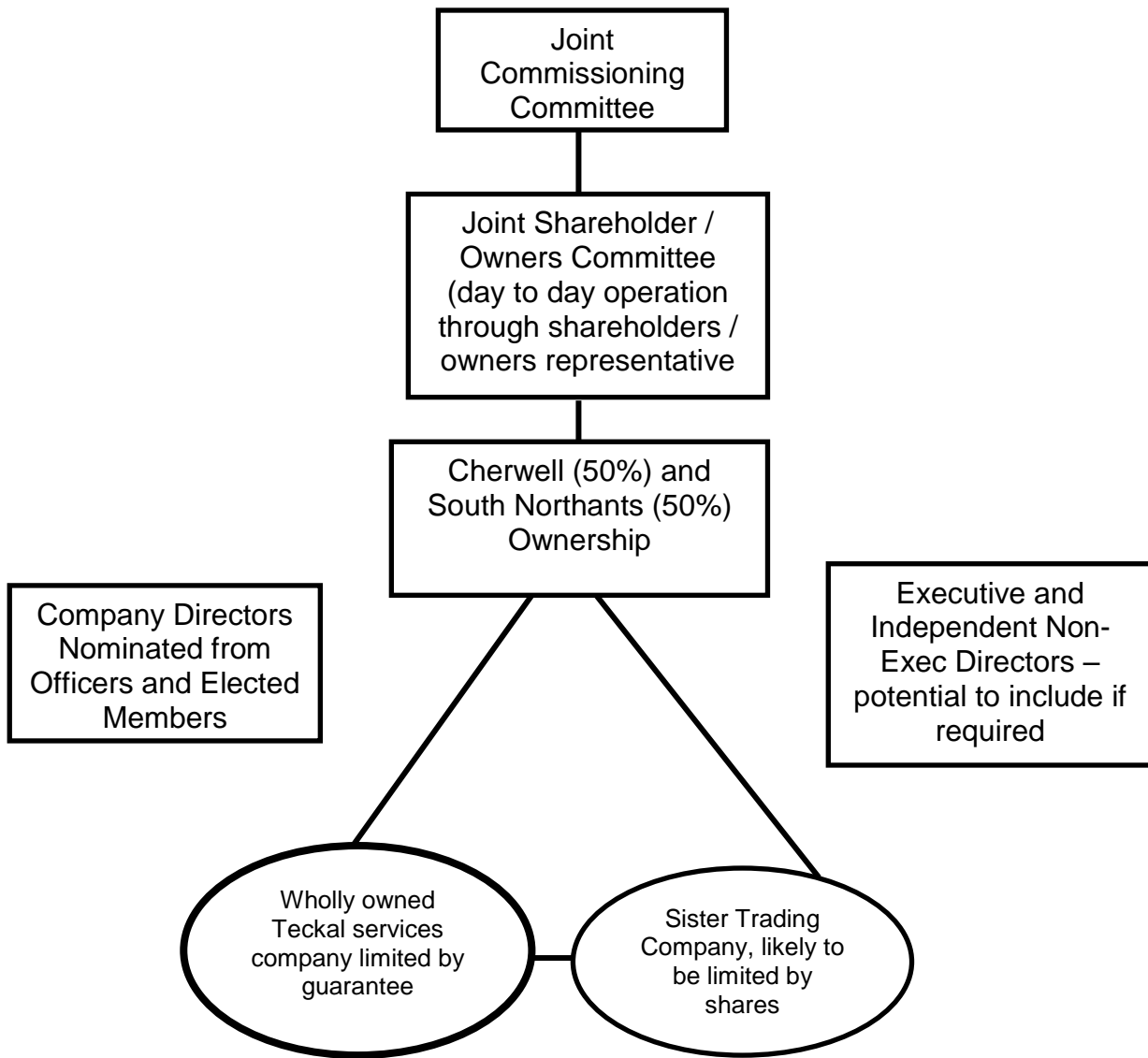
for the insourcing of the current CDC Capita contract. The proposal represents an opportunity for both Councils to deliver significant revenue savings of approximately £260,000 from 2017/18 onwards.

- 3.3 In addition to the financial savings, the business case provides an opportunity to maintain and improve performance, harmonise ICT and processes and integrate first point of contact delivery with the proposed Joint Customer Service team. The business case provides an opportunity for the Councils to create a service that is aligned to the Councils 'Confederation approach' and is capable of being delivered through an alternative delivery vehicle.
- 3.4 It was agreed in the business case that the additional staff that would need to be recruited to enable the joint service to deliver the CDC insourced service would be appointed by a wholly council owned company as part of the confederation model ahead of the implementation of this business case.
- 3.5 Following the insourcing of the Capita contract in May 2017, the remainder of the Revenues and Benefits service would transfer into this company structure (subject to separate decision and appropriate consultation with staff and trade unions).

Legal, Financial and Human Resources Work Update

- 3.6 Since the last meeting there has been good progress in establishing the company to deliver revenues and benefits. There have been regular meetings of the officer project team with a number of work streams, project plan and risk register established. Work is progressing well on systems harmonisation, procurement of an alternative pension scheme, admitted body/recognition of pension status, work on pay grades and reward package, business and financial model, service specification and initial engagement meetings have taken place with existing staff.
- 3.7 As reported at the last meeting detailed work has also taken place to consider the optimum trading model to ensure tax efficiency. KPMG have shared their draft report with the council last week and subsequently a conference call together with Trowers and Hamlins at the end of last week.
- 3.8 Whilst the most tax efficient model for the company would be a Limited Liability Partnership (LLP), where the company would have the same tax status as its partners (Cherwell and South Northants, which as councils are not subject to corporation tax), this is not possible from a legal perspective as whilst local authorities can create an LLP for non-commercial purposes which would be the case in terms of providing services to the councils, it would not be in accordance with the Limited Liability Partnership Act 2000, where an LLP can only be incorporated if it has been set up with 'a view to making a profit' which in turn is prohibited by the Localism Act 2011.
- 3.9 Companies acting under a Non-Trading Status (NTS) or a Mutual Trading Status (MTS) benefit from exemption from Corporation Tax as long as the conditions are met. The conditions for achieving NTS are not prescriptive in nature, but rather judgement based. As such, it can be difficult to guarantee that NTS will be awarded to a company. Even though the revenues and benefits company is not envisaged to be profit making, it could be viewed as having a profit making motive. A company may still be classed as trading even with no profit seeking motive.

- 3.10 The conditions for achieving MTS are prescriptive in nature with limited elements of judgement. This offers more certainty, provided the conditions are met, that income from the Councils should not be subject to CT. Trading with third parties (and other entities within the proposed structure) will be liable to corporation tax under normal rules. The advantage of seeking MTS, rather than NTS, is that if MTS is not granted on the grounds that an entity is not trading, it would have NTS and thus, also not be subject to tax on this basis. The conditions to achieve MTS broadly require a significant majority of income generated to be from members (those who 'own' the company) and for any surpluses to be returned in a way that reflects the contribution each member has made. Should it be desired, new Councils should be able to join and leave tax efficiently, on a piecemeal basis.
- 3.11 A company limited by shares is not permitted to have Non Trading Status or Mutual Trading Status and would therefore be subject to corporation tax. Whilst it is clearly not in the council's interest to be liable for corporation tax on providing its existing services which are currently exempt from corporation tax, clearly this does not apply to the trading activities of providing services to third parties which would be for profit and therefore the payment of corporation tax is a legitimate expectation. From a VAT perspective advice indicates that the company should be VAT registered and that it is preferable for VAT to be charged and then recovered by the councils, giving an overall VAT neutral position.
- 3.12 Based on this advice and in order to trade and ring fence risk a principal Teckal company limited by guarantee operating within an MTS should be created which would employ the staff and deliver services back to the council and a sister company should be created which would ring fence the risk of any trading or tax liability and also allow the Councils to provide consultancy/advisory services to public sector customers through the teckal company and the councils supplying staff to the trading company. Further VAT advice has been requested on the supply of staff from the teckal company to the trading company.
- 3.13 Below is a revised proposed structure, which will be reflected in the constitutional documents (Memorandum and Articles of Association) illustrating:
- The Councils' shared 100% ownership of the companies
 - Accountability firstly to the Joint Commissioning Committee
 - Company Directors for both companies (Elected Members and Officers)
 - Principal Company
 - Sister Trading Company



4.0 Conclusion and Reasons for Recommendations

4.1 The recommendations set out in this report are in line with the agreed recommendations of the Revenues and Benefits Business case, the legal and financial advice received and are necessary to ensure that the business case can be delivered and the associated savings achieved.

5.0 Consultation

Consultation has taken place on the original Revenues and Benefits Business case with staff, trade unions and elected members. The transfer of staff into the company structure will be subject to separate decision and appropriate consultation with staff and trade unions.

6.0 Alternative Options and Reasons for Rejection

- 6.1 The following alternative options have been identified and rejected for the reasons as set out below.

Option 1: To agree the recommendations as set out in the report

Option 2: To amend the recommendations as set out in the report

Option 3: To reject the recommendations as set out in the report. This is not recommended, as the recommendations set out what is believed to be the optimum operating model. In addition the councils' will reduce the potential to deliver the revenues and benefits business case savings unless a suitable employment vehicle is established.

7.0 Implications

Financial and Resource Implications

- 7.1 The proposals set out in this report are in accordance with tax advice received from KPMG.

On-going work on with Trowers and Hamlin and KPMG is funded through transformation budgets. The cost of registering the required companies and domain names is around £60, which can be met through existing budgets. The detailed financial modelling for the company and draft business case will be subject to separate member approval when these are available and the creation of budgets for these companies will form part of the 2017-18 budget setting exercise.

Comments checked by:

Paul Sutton, Chief Finance Officer - 0300 003 0106

paul.sutton@cherwellandsouthnorthants.gov.uk

Legal Implications

- 7.2 The proposals set out in this report are in accordance with the legal framework and legal advice received from Trowers and Hamlins.

Comments checked by:

Kevin Lane, Head of Law and Governance – 0300 0030107

kevin.lane@cherwellandsouthnorthants.gov.uk

Risk Implications

- 7.3 Risk will be considered fully as part of the legal and financial work being undertaken. This report in itself is as a result of due diligence and the consideration of risk.

Comments checked by:

Ed Bailey Corporate Performance Manager - 01295 221605

edward.bailey@cherwellandsouthnorthants.gov.uk

8.0 Decision Information

Key Decision

Financial Threshold Met: No

Community Impact Threshold Met: No

Wards Affected

All

Links to Corporate Plan and Policy Framework

Grow the District (SNC)
Sound budgets and customer focused council (CDC)

Lead Councillor

Councillor Ian McCord, Leader of the Council, SNC
Councillor Barry Wood, Leader of the Council, CDC

Document Information

Appendix No	Title
None	
Background Papers	
Draft Report of KPMG – Tax Advice on group structure Exempt from publication by virtue of paragraph 3 of Part 1, Schedule 12A	
Report of Trowers and Hamlins Vires for an LLP - Exempt from publication by virtue of paragraph 5 of Part 1, Schedule 12A	
Report Author	James Doble, Assistant Director - Transformational Governance
Contact Information	01295 221587 james.doble@cherwellandsouthnorthants.gov.uk