Grant Thornton

An instinct for growth™

The income spectrum

Helping local authorities to achieve revenue and strategic objectives to create vibrant economies

Contents

The evolving business case for change

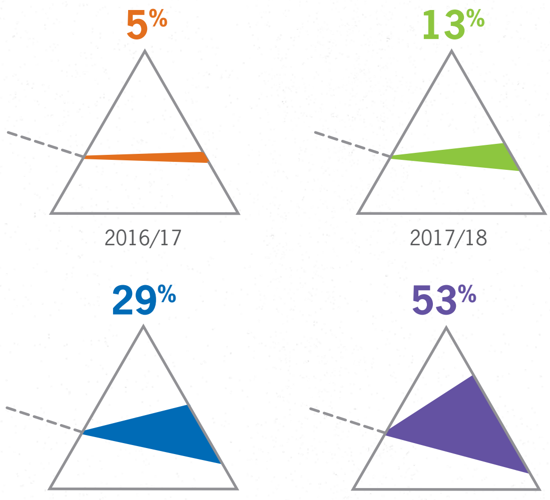
Income is a critical part of the path to financial sustainability alongside cost efficiency

Local government is under immense financial pressure to do more with less. The 2015/16 spending review is forecast to result in a £13 billion funding hole by 2020[1] that requires councils to make savings of up to 29 per cent. Despite this challenge, most councils continue to manage their finances proficiently and have become lean and many local authority chief financial officers (CFOs) are confident they can continue to balance the books. However, our research indicates (Figure 1) that a majority are concerned that reaching a tipping point is possible.

With further funding deficits still looming, income generation is increasingly an essential part of the solution to providing sustainable local services, alongside managing demand reduction and cost efficiency of service delivery.

This report shares the insights into how and why local authorities are reviewing and developing their approach to income generation.

Figure 1 CFO and auditor views on the year a financial tipping' point could be reached[2]



Report methodology

This report is for chief officers, elected members, directors of finance and other service leaders in local government who have responsibility for the strategic commissioning of outcomes. The report draws on:

- learning from public and private sector stakeholders
- Grant Thornton's own experience as an advisor to local government
- analysis from the Grant Thornton/CIPFA CFO Insights tool[3]
- insight from roundtables we convened on the topic in Leeds, Bristol and Exeter (refer to Acknowledgements section).

It also builds on our previous local government thought leadership on financial resilience, governance and alternative delivery models (ADMs), and place analysis.

Creating a sustainable financial future

Reforging local government

Better together

Vibrant Economy Index

1 http://www.itv.com/news/2015-11-29/councils-warn-of-13bn-funding-gap-by-2020-due-to-cuts-and-rising-social-care-costs/

2 Grant Thornton. Reforging Local Government, December 2015.

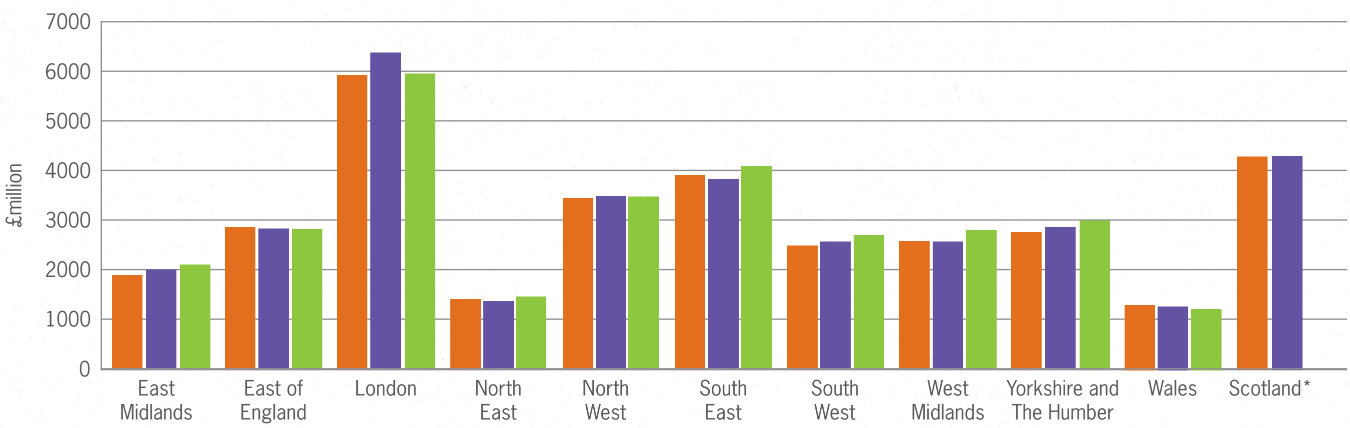
3 CFO Insights is an online financial analysis tool from Grant Thornton and CIPFA that gives those aspiring to improve the financial position of their organisation instant access to insight on the financial performance, socio-economic context and service outcomes of theirs and every other council in England, Scotland and Wales. Further details are available at http://www.cfoinsights.co.uk/

The national picture

The Grant Thornton/CIPFA CFO Insights tool shows change in local authority income generation across England, Scotland and Wales. For instance, English local authority service based income increased by 4.1% between 2013/14 and 2015/16. (Figures 2, 3 and 4). By region, the East Midlands had the most notable increase in income at 11.5 per cent, followed by the West Midlands (8.7%) and South West (8.4%).

However, despite the large increase in the East Midlands, it still has the third lowest income by region, indicating the scale of income generation across the country as authorities increasingly address commercialisation, even it had previously not been a priority.

Figure 2 Council annual income generation by country/region



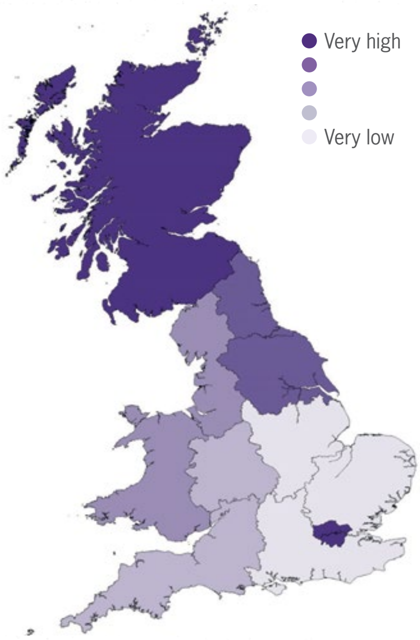
Source: CFO insights * 2016 data for Scotland not available

Figure 3 Country/regional variance in income

Region	% variance in income 2013/14-2014/15	% variance in income 2014/15-2015/16	% variance in income 2013/14-2015/16
East Midlands	6.12	5.05	11.47
East of England	-1.29	-0.13	-1.42
London	7.51	-6.54	0.48
North East	-2.67	6.20	3.37
North West	1.10	-0.41	0.69
South East	-1.98	6.76	4.65
South West	3.33	4.88	8.38
West Midlands	-0.10	8.84	8.73
Yorkshire and The Humber	3.54	4.57	8.27
Wales	-2.23	-3.75	-5.89
Scotland	0.43		

Source: CFO insights

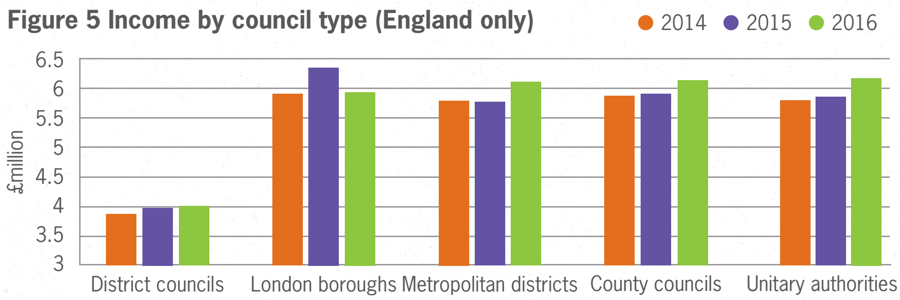
Figure 4 Range of income per capita



Segmentation by authority type in England shows that metropolitan, unitary and county councils saw significant increases in income generation in 2015/16 (Figure 5). Unitary authorities increased income by 6.5% between 2013/14 and 2015/16, followed by metropolitan authorities at 5.4%. This indicates that income generation is increasingly important to all council leaders regardless of the tier of government.

Local authorities are seeking to become more commercial and generate income in a variety of ways (see box out).

Figure 5 Income by council type (England only)



Source: CFO insights

Approaches to income generation

- **Fees and charges** – car parking, household garden waste, private sector use of public spaces
- **Asset management** – utilities, personnel, advertising and wifi concession license
- **Company spin-offs** – housing, energy, local challenger banks
- **Treasury investments** – real estate development, green energy, equity

Case studies

Cheltenham property purchase and lease

Cheltenham Borough Council bought 60,000 sq ft of commercial property for £14m which included a head lease which expires in 2023, generating annual rent of £1.3m and an annual investment return of 9%. The acquisition was financed through a combination of both internal borrowing and PWLB loans. The building will ultimately allow the council to relocate their headquarters in 2023 and facilitate the redevelopment of their current offices, which are in a prime town centre location, for mixed use development. The redevelopment aims to enhance Cheltenham's offering for residents and visitors; deliver additional jobs; business rates and rental income to support the council's budget and make a significant contribution to the local economy. The council is now exploring options to deliver the relocation and redevelopment earlier than 2023. Office development is one of a wider portfolio of treasury investments by the council, which also includes for instance, joint share ownership of Gloucestershire Airport Ltd.

Bristol Energy and Technology Serviced Ltd (BETS)

Establishing the council wholly-owned company is a central element of Bristol City Council's commercial agenda and vision as a European Green Capital. BETS will generate and supply low-carbon and affordable energy. It is one subsidiary of the parent Bristol Holding Company, along with Bristol Waste which provides waste management and street scene services. Following an initial investment from the council's general fund and European Investment Bank's ELENA programme[4], BETS is forecast to deliver a return within five years, with a rising return over the decade.

Flintshire off-street car parking charge

To maintain the vibrancy and vitality of the county Flintshire County Council is looking to provide a consistent approach to off-street parking through the expansion of pay and display for all town centre car parking provision of 40 spaces or more. The initiative will increase income by £0.4 million each year. By setting an effective pricing structure and tariff, charging has proved to be a mechanism to encourage commuters to use the car parks on the periphery of the town and community centres, while promoting town centre proximity spaces for short stay shoppers and visitors in support of commercial viability. The council's proposals were informed by its 'Big Budget Consultation' to gauge levels of support for difficult decisions ahead due to funding gaps.

[4] ELENA covers up to 90% of the technical support cost needed to prepare the investment business case and plan for implementation and financing local energy development.

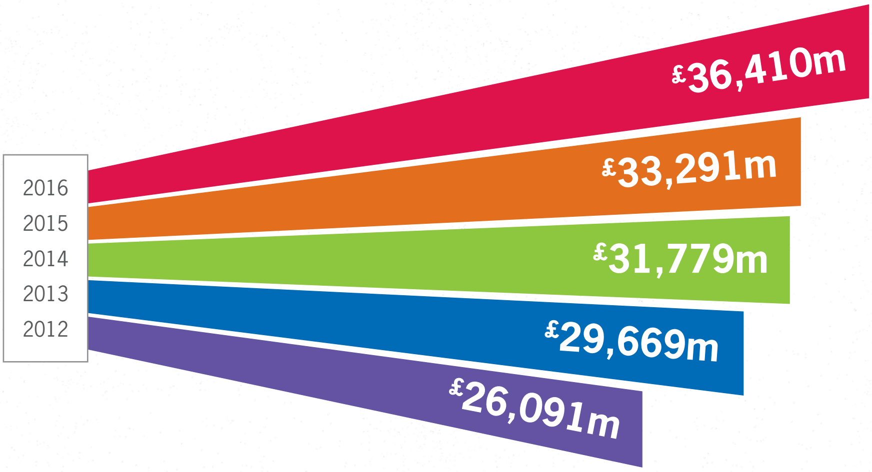
Income generation has been made increasingly viable by changing statutory powers and cross-market sector reforms.

2016 was a landmark year for income generation by the sector in a number of ways. Alongside income generation by local authorities having increased since 2013/14 by 4.11%, by the second quarter of 2016, less than half (48%) of all treasury capital was kept in banks; a significant contrast to a level of 72% in 2008/09. Councils are increasingly choosing to hold part of their assets in property and equity[5]. For instance, in terms of real estate development, local authority property deals were on track to break the £1 billion barrier. This is also reflected in DCLG financial data on English local government investments (Figure 6), which shows a year-on-year increase over the past five years to a high of over £36 billion in 2016/17[6].

This rise in income has been enabled by changes to councils' ability to trade, as well as by multiple market reforms.

Power to trade is evolving and varies across tiers of local government and nations.

Figure 6 English local government investments (£m)



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Powers to trade

England

- In England, the Localism Act 2011, building on the Local Government Act 2003, gives councils a greater General Power of Competence to trade and charge, to borrow and invest prudently.
- The Public Services (Social Value) Act 2012 also provides councils in England and Wales with commissioning obligations and powers to benefit from responsible procurement.

Wales

- The Well-being of Future Generations (Wales) Act 2015 places a new and additional duty on Welsh councils to consider the long-term sustainability of policy-making for different stakeholders over time.

Scotland

- In Scotland, the Local Government (Scotland) Act 1975 and the Scottish First Minister's Finance Circular 5/2010 sets out the statutory basis on which councils can prudentially borrow, lend and invest.
- At the same time, the Social Impact Pledge 2016 is a part of the Scottish Government's drive for a Fairer Scotland, which encourages councils to commit to changes within their policies and operations that will directly benefit communities.

[5] Room 151. Editor's Blog. 21 December 2016.
[6] DCLG Financial Statistics 2012-2016. HM Government. Year 2016/17 is based on live reporting of position as end of Q2 on 5 January 2017.

Multiple market reforms also present councils with new opportunities to commercialise. The reforms may be specific policy developments aimed squarely at councils, or general policy changes from which local government and other sectors can benefit. In terms of policy directed at councils, these include the New Homes Bonus (NHB) and localisation of business rates aim to incentive house building and economic growth respectively. Or, unprecedented low interest rates which make the cost of public borrowing to invest more attractive, that is 'speculating to accumulate'. Regarding other policy from which councils can benefit, these include new rules on eligibility to access alternative funding through Individual Savings Accounts (ISA), such as solar energy bonds. Or, the Water Act 2014, which will liberalise the retail end of the market, meaning that from April 2017 onwards local authorities and other non-domestic water users (industry, not-for-profits) can trade, similarly to like many councils are already doing in the energy market[7].

A council's ability to invest will vary again across tiers and regions of government, according to external and internal factors including: powers and delegated authorities; strength of balance sheet to borrow or invest; political willingness to accept risk; amount of local physical, natural and brand assets which can be exploited; and organisational culture and capacity to implement change. It is also a question of time sensitivity. For instance, while some councils may want to benefit from a period of cheaper borrowing because they are relatively asset poor, other councils may have healthier reserves in the short-term, but are concerned about revenue security in the long-term so the challenge is to convert capital to on-going revenue streams when market conditions are most favourable.

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The ideal scenario is investing to earn with a financial and social return.

Councils are now striving to generate income in a way which achieves multiple strategic outcomes for the same spend; examining options to balance budgets while simultaneously boosting growth, supporting vulnerable communities and protecting the environment. As illustrated in the cases on the next page, they are seeking a broad range of social returns from investments.

The Local Government Act 2003 requires councils to follow the CIPFA Prudential Code for Capital Finance. The objective is that statutory Section 151 officers – council CFOs – prudently invest the funds held on behalf of their communities. The guidance recommends that authorities should prioritise the highest rate of return for borrowing and investments according to security, liquidity and yield – in that order. However, what one council interprets as best value to communities may differ to another council.

[7] See for instance Nottingham's Robin Hood Energy Ltd or Peterborough's Blue Sky energy service company.

Case studies

North East Lincolnshire's infrastructure revolving fund

The South Humber Infrastructure Investment Programme (SHIIP) is a £29.5 million joint arrangement over 15 years between the Council and Greater Lincolnshire Local Enterprise Partnership (LEP) and Central Government's Local Growth Fund whereby the upgrading of employment land is leading to an uplift in local jobs created and business rates collected. This is a key part of the council's economic strategy which includes an aspiration to be a European green energy hub through the port's local enterprise zone (EZ). SHIIP will facilitate the development of 222,000 sq.m. of new floor space accommodating up to 4,000 jobs and improve the local economy by £146 million GVA. Extra business rate retention as a result of SHIIP is factored into the council's medium term financial plan (MTFP) funding projections, of up to £2.3 million by 2019/20. The council borrowed £15 million to joint fund the deal. The contribution is to be recovered from Section 106 (s106) planning agreements.

Wolverhampton's recruitment agency

The City of Wolverhampton Council established YOO Recruit as a wholly-owned company for the provision of temporary workers into the council. It was originally developed as an invest to save initiative, recycling an existing operating cost to generate income and boost quality job opportunities for in the local area. The company has a turnover of £7.4 million, a gross profit of £0.6 million and net profit before tax of £0.3 million (yet to be audited). YOO Recruit also reduces costs through less invoicing and agency fees and ensures 90% of workers live within the city and are paid the Living Wage.

Chorley's purchase of local shopping centre

The primary purpose of buying the Market Walk shopping centre was to provide Chorley Council with greater control and influence over the town centre and improve the local economy by creating more jobs and attracting more people and businesses into the town centre. A secondary purpose was to provide a new income stream. The £23 million investment has helped to rejuvenate the town centre and generates business rates and rental income of £0.75 million per year. Prior to the investment a number of the retail outlets were in a poor state of repair or unoccupied. Due to this success, the council is now proposing to invest a further £17 million in a Market Walk extension, responding to feedback that an improved retail and leisure offer is needed to encourage town centre visits.

Typically, a council seeks a 5-10% financial return on its investment. The ideal transactions however are those that offer multiple benefits for the same spend, without a trade-off between financial and non-financial benefits. Some councils may be willing to accept a lower financial return to accommodate additional social outcomes, especially if these benefits are felt locally. However, social returns may also be realised indirectly from financial gain when the money from them is then invested in local public services. Alternatively, some councils may not pursue an initiative with a high financial return if it does not align to their strategic priorities of directly benefitting local communities, or because they deem it unethical. For instance, not all councils are willing to enter into real estate developments outside of their authority's geographical boundaries.

The need to understand better the social impact of different courses of action has resulted in the emergence of a variety of codes, standards and tools from HM Government, professional service providers, think-tanks and non-profit organisations that provide guidance to local government. (See the box out.)

These initiatives are supporting and informing a number of councils decision to transfer to using outcomes based budgeting and strategic commissioning – as is the case with North East Lincolnshire and Wolverhampton – or, an interventionist approach to correct a perceived market failure – as is the case with Chorley. This business transformation is, therefore, not solely driven by a need to protect frontline public services when budgets are reducing, but more about a form of better government which secures greater impacts.

Guidance to local government

Green Book

HM Treasury's rule book for public policy appraisal includes guidance on multi-criteria analysis[8]. It applies elements of a full benefit-cost analysis which place an economic valuation on a transaction, in combination with a consideration of unvalued costs and benefits which have not or cannot be priced but which are also important to success. This is achieved through weighting and scoring of economic (eg attraction of £ private sector investment), social (eg number of local decent jobs created) and environmental benefits (eg decoupling of natural resource use from growth).

Place Analytics

Grant Thornton's online data platform is a subscription service which provides a geographical perspective on economic, social and environmental change. Reports tell a compelling 'story of place' by connecting service spend to service outcomes, thus informing public policy options.

Local Multiplier 3 (LM3)

LM3 was initially developed by the new economics foundation (nef) as a way of understanding the local economic impact of procurement contracts and regeneration schemes. LM3 is a tool to create a figure for an organisation's contribution to the local economy based on an analysis of financial records and a survey of staff and suppliers.

Social Return on Investment (SROI)

SROI is a framework based on social generally accepted accounting principles (SGAAP) that can be used to help manage and understand the social, economic and environmental outcomes created by an organisation. SROI seeks to include the values of people that are often [box out continues] excluded from markets in the same terms as used in markets that is money, in order to give people a voice in resource allocation decisions.

[8] HM Treasury 2011. The Green Book. Appraisal and Evaluation in Central Government.

Learning from new and innovative practice

When external borrowing is required to fund new income opportunities the PWLB is still the first point of reference, but this is not always appropriate and councils routinely use other internal and external mechanisms, and are experimenting with new alternative finance too.

Interest rates impact significantly on a council's decision to invest or to save. Since the 2007/08 global financial crisis and the ensuing UK recession, domestic interest rates have remained at historically low levels – 0.25% at the time of writing. This reflects the Bank of England's monetary policy to bring economic stability and resilience by ensuring the cost of borrowing is low (so people invest rather than save) and the Sterling exchange rate is more competitive (so industry exports more). The Brexit referendum in June 2016 created more market uncertainty which further strengthened the Bank of England's resolve to maintain low rates in the near future.

As a consequence of this PWLB rates are also at a historic low, which has prompted a huge spike in PWLB borrowing by councils (£1.3 billion was borrowed in June alone).

While PWLB is the best source of funds for many councils, councils do routinely make use of other financial mechanisms too (Figure 7). Councils are innovating on income generation by using alternative delivery models to fund as well as deliver these new income opportunities. This includes harnessing one or a combination of traditional and new investment instruments, with options related to facilitation and regulation, public funds, debt and equity. (The appendix provides a glossary for these financial terms). Local facilitation and regulation can be a core enabler and accelerator of the other forms, which is additionally attractive to councils as it may involve nil/negligible initial and on-going additional costs.

Historically, PWLB has typically been cheaper, less risky and easier to administer form of funding than other providers.

The Public Works Loan Board

The PWLB is a statutory body managed by the UK Debt Management Office (DMO), a part of HM Treasury. It is authorised to lend money to any UK local authority which has the power to borrow, offering a fixed rate loan (up to 50 year period with repayment due in half yearly intervals) or a variable rate loan (up to 10 year period with repayment due at 1-6 month intervals)[9]. It is essentially an 'IOU' between central government and local government, on which the DMO collects 0.8% interest income. Critically, some councils are borrowing from PWLB because they lack reserves to invest and it is the cheapest and easiest available option. However, some others are borrowing even when they have reserves to do so because they are hedging their bets that it is a missed opportunity not to take advantage of historical low borrowing costs.

While the Government recently announced it is abolishing the PWLB, its function is to retained, handled directly by HM Treasury and with the DMO acting as operating agent[10].

[9] UK Debt Management Office. PWLB Annual Report and Accounts 2015-2016.
[10] http://www.publicfinance.co.uk/news/2016/11/pwlb-be-scrapped-government-confirms

However, this is not universally so and is changing. For some councils, the PWLB is inflexible as it is not possible to negotiate a better rate or a bespoke repayment profile. So, for instance PWLB loans can be very expensive to repay early if a council unexpectedly finds its cash position is more positive than forecast. As the cases below show, this has given rise to alternative sources including pension funds and social impact investors (eg Luton), bonds (eg Aberdeen) and private bank loans – but critically also other public bodies including local authorities themselves (eg Warrington and Newham).

Rightly, there are political sensitivities associated with exploring these alternative sources of funding, whether to save or to borrow, especially in light of the Iceland Bank collapse and concern over the cost of Lender Option Borrower Option (LOBO) loans. Also there is an understandable, broader concern about 'over gearing' of councils – at present there is £88 billion of outstanding debt in English local government[11]. Hence, as the examples help show, robust due diligence is a core requirement of risk mitigation for business case development as part of effective council treasury strategy. This due diligence, again, includes financial and non-financial aspects (eg Glasgow and Swindon).

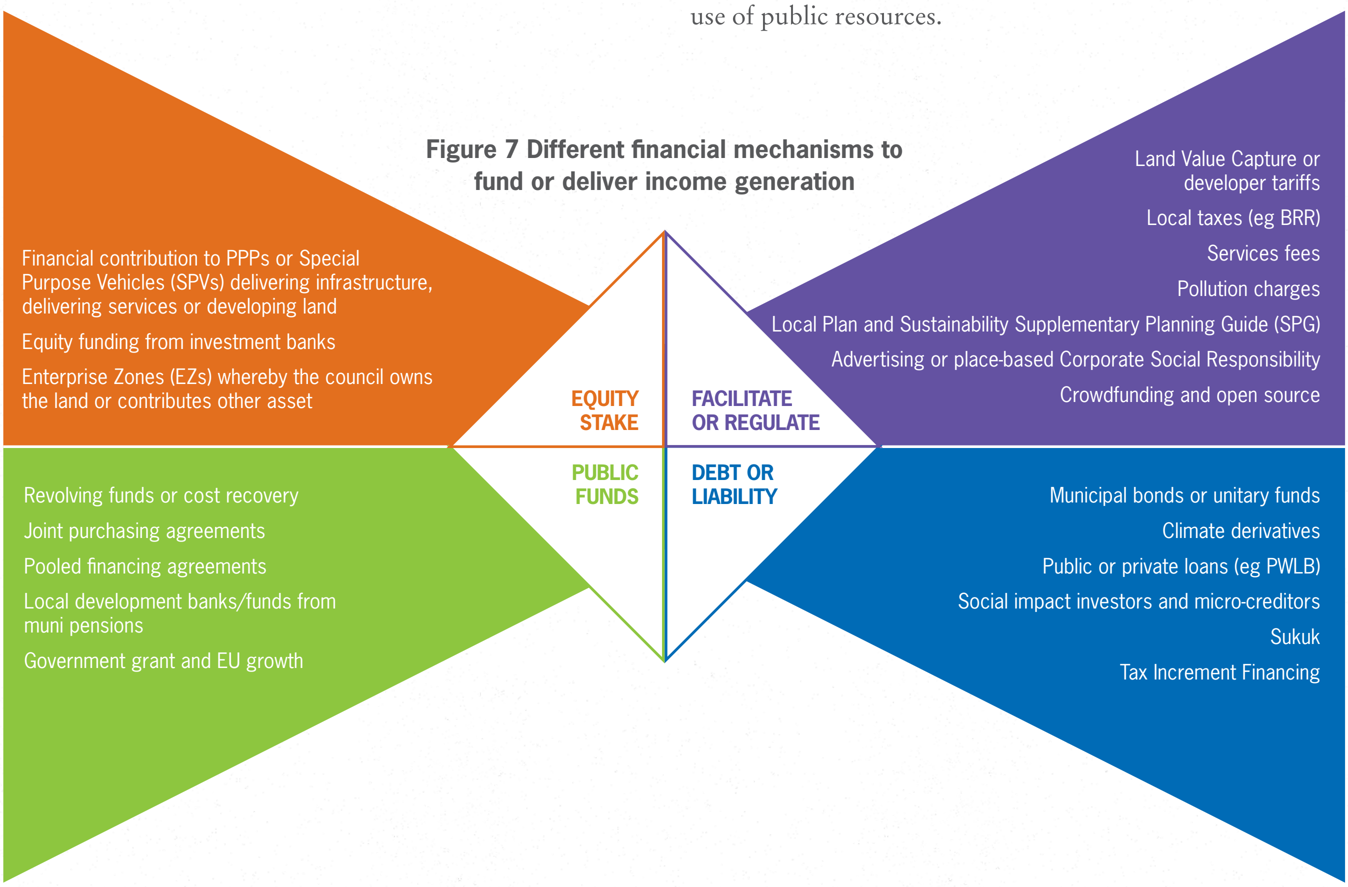
If aiming to deliver a financial and social return, some entrepreneurial councils not only aim to correct market failure but also act as an investor of first resort to help create new markets.

For some councils the idea that they should intervene in the market is anathema – for them this is the role of the private sector or central government. For other councils, however, market intervention is viewed as a fundamental duty, not just to reverse market shortcomings but even to create new markets. In the latter instance, considerations of social return may be both about a perceived public duty of care to do good or to do no harm, such as health and social care integration or climate risk[12].

Notable cases here include 'first of its kind' investment asset classes (eg Swindon, Aberdeen). It is also noteworthy that authorities are partnering with like-minded organisations from the private and investor community to make deals viable, in particular social impact investors and progressive fund managers (eg Luton with Cheyne and Big Society Capital).

In pursuing these market shaping activities, well informed councils are aware they need to comply with EU State Aid rules which prevent them from unfairly distorting market competition through inappropriate use of public resources.

Figure 7 Different financial mechanisms to fund or deliver income generation



[11] DCLG Financial Statistics 2012-2016. HM Government. Year 2016/17.
[12] Zurich Municipal in association with SOLACE. 2016. Worlds apart – the 2016 senior managers' risk report.

While PWLB is the best source of funds for many councils, councils do routinely make use of other financial mechanisms too.

Case studies

Swindon's crowdfunding with Individual Savings Accounts (ISAs)

Swindon Borough Council launched the UK's first ISA-eligible investment through its wholly-owned company Public Power Solutions (PPS). The bond uses new UK legislation that allows retail investors to hold bonds in an ISA portfolio. It is to support a £5.4 million scheme for a new solar energy farm which will deliver an average 6% return to bond-holders and generate rent, business rates and green tariffs for the council as shareholder. Part of the revenue from generating green electricity will be set aside to fund local community projects. Funding is comprised of £3 million of council money and £2.4 million from the bond issue, with the offer open to the general public including other investors from outside of the borough. ISAs are attractive to investors as they are tax free.

Luton and Cheyne Social Property Impact Fund

In response to social impact investor demand, private fund manager Cheyne launched its £1 billion Social Property Impact Fund to deliver extra affordable homes and care facilities to non-profit organisations. Its seed investor is Big Society Capital. Luton Borough Council and the Fund entered into a 21 year agreement to build and lease 80 new one and two bedroom apartments, close to the town centre with good access to amenities and transport links. Housing allocation is based on a clear measure of prioritised need, with rent set below Local Housing Allowance (LHA) rates. The Fund took all the development, financing and construction risks to provide a turnkey solution to the council. The council pay a Consumer Price Index (CPI) linked lease to the Fund and create an annual operating surplus from its management and maintenance role.

Aberdeen bond to grow local economy

Aberdeen City Council is the first Scottish council to gain a bond issuer credit rating (Moody's, where it is rated Aa2) after launching its new funding model to finance its long-term capital programme from financial markets. The £370 million bond is to support the city's growth and diversification as part of a £1 billion development programme for redeveloping the exhibition and conference centre, new schools, transport improvements and 3,000 new homes to be built over the next 15 years. The council's innovative funding mechanism was supported by the Scottish Government due to the nationally strategic importance of the projects to anchoring the city's status as a competitive global energy hub on the international stage.

Newham joint investment in a solar farm

The London Borough of Newham is one of four councils jointly investing £60 million in a solar energy farm in Wroughton which will deliver a 6% return by generating enough green electricity to power 12,000 homes. HSBC will pay to take power from the site as part of a 15 year agreement. Instigated and coordinated by Warrington Borough Council, the scheme Rockfire Capital is attractive to Newham, Thurrock, Warrington and a fourth silent council partner as it not only aligns to statement of investment principles for ethically-responsible investment in commercially-viable projects, but also because the four investing councils are able to lower the transaction cost by sharing fees paid for due diligence, thus increasing the profit margin.

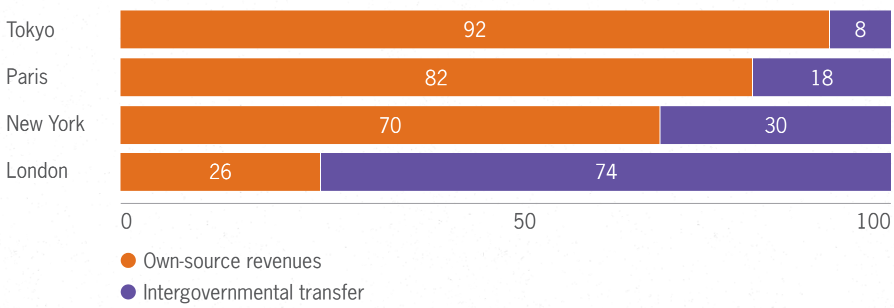
Innovation in the form of collaboration as well as investment type provides new ways to add value, including public-to-public (P2P) transactions across geographical boundaries.

It is often quoted that 'necessity is the mother of invention'. Yet despite a wave of local devolution over the past half-decade, UK government is still heavily centralised. Compared to their international counterparts, UK local authorities are much more dependent on central government transfers. Even London only generates 26% of own-source revenues (Figure 8), in significant contrast to Tokyo at the other end of the spectrum which produces 92%. Changes to business rate retention and council tax precepts to incentivise growth and metro mayor models respectively will shift the balance further in favour of local government leaders, but at the same time, due to revenue pressures councils are striving to innovate in new and different ways on income generation.

Councils are being creative not only in terms of new types of investment class but also how they co-produce solutions. Most notable is the rise of P2P investments where two or more local authorities come together as an investor or investee.

One factor driving this trend is 'disintermediation': lowering a transaction cost by reducing the fees of (or need for) professional service firms. For instance, sharing the risk and cost of due diligence. This trend is particularly interesting as it can involve local authorities trading outside of their immediate geographical areas (eg Warrington, Newham and Thurrock). Transacting at the national level is anticipated to rise in the future, especially as new vehicles emerge, such as the UK Municipal Bonds Agency[13].

Figure 8 Public sources of council revenue



This trend may also extend to the global domain too, given it is not uncommon for council treasury strategy to include seeking to borrow or invest on the international stage. Again new vehicles have emerged to advance this option, for instance the Local Pensions Partnership (LPP) has a £5 billion global equity fund.

At the individual authority level, there are several examples of councils seeking to attract or invest overseas money, ranging from London (£2.1 billion HS1 acquisition by Ontario pension fund), Sheffield (£1 billion real estate investment with China's Sichuan Guodong Construction Group) and Manchester[14] (EIB borrowing and Singapore bank equity). Taking the latter, Manchester City Council has a capital financing requirement of £0.9 billion and its current treasury strategy to both borrow and invest includes scope for international ventures, ranging from a £100 million loan facility with the EIB through to stock holdings in AAA rated countries such as Germany, USA and Singapore.

Just as interestingly, a number of authorities are, again, also aiming to borrow or invest at the global level to generate income that also requires a social return (eg Glasgow).

[13] The LGA-sponsored MBA follows overseas examples from France and New Zealand (eg Agence France Locale).

[14] For example, Manchester City Council's Treasury Strategy 2016-17 (dated 4 March 2016) has a capital financing requirement of £0.9 billion and its current treasury strategy to both borrow and invest includes scope for international ventures, ranging from a £100 million loan facility with the EIB through to stock holdings in AAA rated countries such as Germany, USA and Singapore.

Case studies

Warrington's challenger bank status

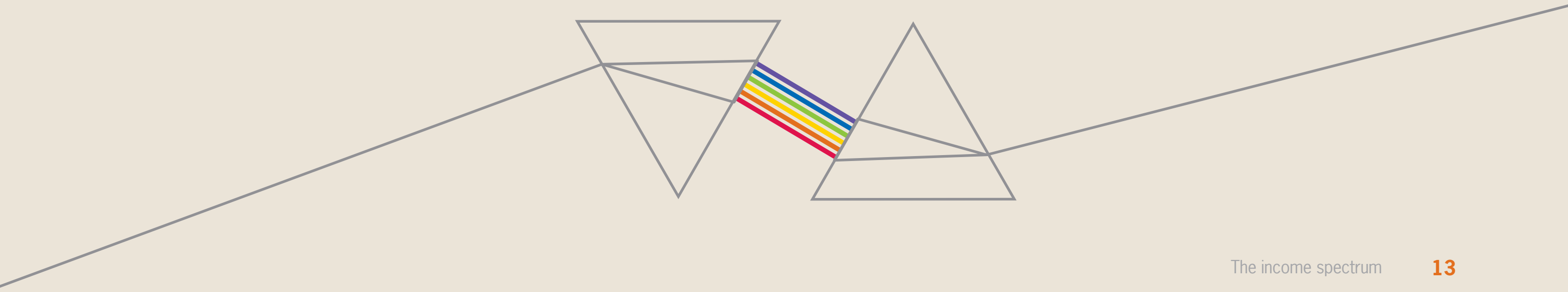
Warrington Borough Council has joined the ranks of a new cohort of local authority banks such as Cambridgeshire and Counties Bank and Solent Bank in acting as a provider of financial services to other local SMEs and public bodies. The council has approved plans to invest £30m and take a 33% share in the new Redwood Bank. The deal for the bank is subject to receipt of a license from the Bank of England. It will enable the council to help more businesses than by authorising loans directly, by taking deposits from SMEs and getting a gearing effect, whereby for every £10m investment the bank is forecast to make £50m of loans. Surpluses from the JV will be invested in local public services. This new JV is the latest in a series of financial innovations by the council which harness its role as a facilitator of development through alternative funding. For instance, seperate to the Redwood Bank deal, Warrington increased its ongoing lending to housing associations to £300m and 10 providers and is negotiating three further deals. The purpose is two-fold: to promote house building and regeneration; and to earn interest that is reinvested in frontline services. Interest payable is 1.25 per cent above the PWLB's rate at the date of each drawdown. Borrowers to date have included Warrington HA, Plus Dane, Helena, Your Housing and others. The council has carried out a full comprehensive risk assessment on the loan. This includes an independent due diligence exercise on Housing Associations and a detailed risk matrix drawn up in consultation with the council's treasury advisors, leading banking lawyers, bankers, its auditors and members.

Glasgow's participation in the Carbon Disclosure Project (CDP)

Glasgow is one of over 200 cities around the world which participate in the CDP to maintain their attractiveness to institutional investors. For instance, reporting on plans to address heat island effects through cooling measures in major buildings. CDP's cities programme provides a voluntary climate change reporting platform for city governments to disclose their environmental performance to pension funds and fund managers. The programme is open to any city government, regardless of size or geographic location.

Rushcliffe's shift from Teckal company to social franchise model for Streetwise

The Rushcliffe Borough Council currently operates a wholly owned company trading in environmental, grounds maintenance and on-street services that is subject to Teckal exemption. The exemption allows a council to award contracts directly to the company for up to 80% of its trade. With a turnover of £1.5 million the council has achieved efficiency savings of £0.4 million. Going forward, Streetwise's aim is to meet growing demand to deliver services to local public sector peers and so it is revisiting its operating model to allow this new commerce. Social franchising will enable other organisations to trade under the Streetwise banner and benefit from the existing support infrastructure, allowing Streetwise to share risk and lower its operating costs. Being agile in this way will allow it to thrive going forward.



Critical success factors to review and develop your strategy and implementation plan

Use the key elements of a quality framework for design and delivery.

Regardless of a council's objectives for, or experience of, generating income, good management disciplines should be applied so the intended benefits are planned and achieved.

Choose the best opportunities available to you given your unique context.

Prioritisation is required to filter a long list of options to arrive at a short list.

The opportunity matrix (Figure 9) helps a council to appraise all its possible options to arrive at a list of the most appropriate ones. It contrasts the potential contribution strategic priorities (financial and non-financial) with the level of difficulty to implement (risk and effort). The most promising income opportunities will populate the top right hand corner of the matrix.

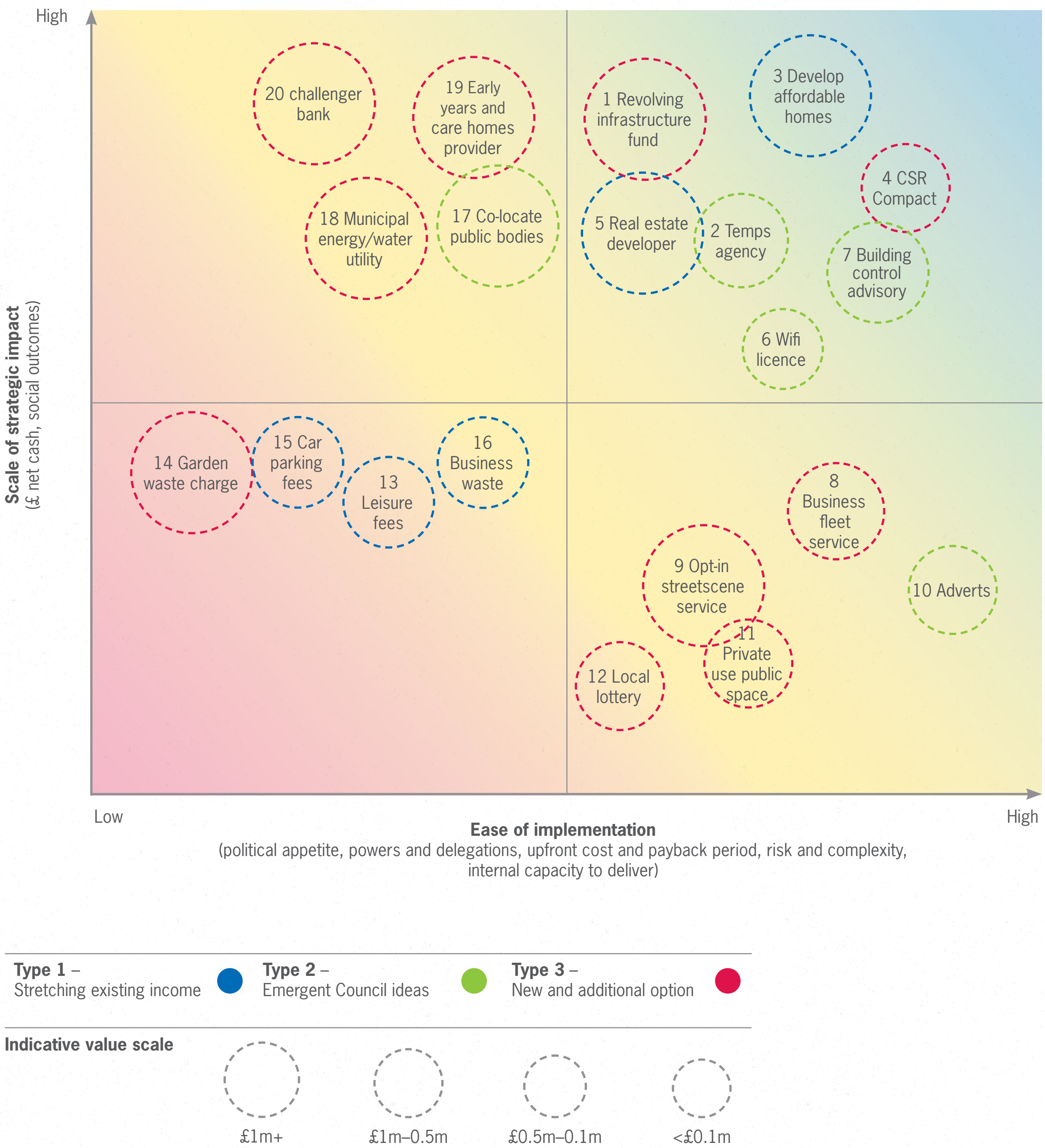
If a council is able to answer the questions below with confidence, then this is a really good start to refreshing or developing an income strategy, to make these opportunities a reality.

- Align commercial aspirations to core mission and outcome-based performance
- Secure political buy in for this commercial new or refreshed angle
- Understand your baseline position on commercialisation including how it compares to peers at a local and national level
- Put a robust appraisal framework in place to prioritise and scrutinise the latest and best business cases for you to commercialise
- Get a grip on the profit and loss of your current commercial activities and full cost recovery of non-trading statutory services
- Understand how traditional and alternative financial instruments will fund new options
- Determine your capacity and culture change requirements to implement this new commercial programme
- Devise a clear and simple communication plan to bring internal and external stakeholders along with us on this complex journey of change

Questions to help ensure success

- *Have all your options to maximise use of revenue and assets been explored?*
- *Do we understand what are strengths are and what we are less good at compared to the market place?*
- *How does each department and service compare on net income and cost recovery against neighbours and peers?*
- *Are adequate gateway processes established to identify and select new opportunities, and stretch or stop existing ones?*
- *Is it clear how generating income delivers both a financial and social return that is aligned to your local political priorities?*
- *Are you aware of the latest examples on innovative financing to fund your new income generation proposals?*
- *Are governance processes robust enough to scrutinise business case proposals for new income generation?*
- *Do you understand the pros and cons of different alternative development models for the establishment of trading companies, including tax, legal and HR aspects?*

Figure 9 Opportunity matrix to appraise potential new income initiatives – illustrative sample



Forward plan to overcome anticipated barriers to change.

According to a talent survey of 144 HR directors in local government, most believe that commercialisation (70%) and the ability to manage change (60%) are among the top issues that leaders need to work on as their operating environments change. Now and in the immediate future, successful leadership teams need to demonstrate new acumen related to income generation, both in terms of entrepreneurship and collaboration.

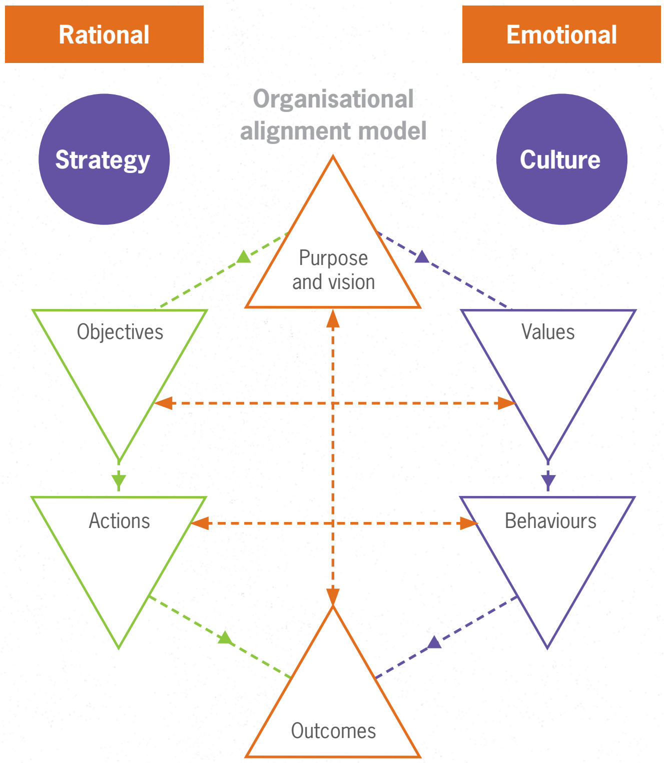
Yet councils are continually challenged with investing in the present to accrue benefits further down the line. This is particularly true of committing budget, people and time to develop the leadership culture, technical skills and capacity to commercialise. It is imperative then that a council's income generation strategy and action plan factors in organisational and personnel development needs so a council is best equipped to realign its operating model to any new vision.

While culture and behaviours are just one part of a complex system that makes up a modern council, the right culture is as central to sustainable organisational success as the right strategy. The Organisational Alignment model in Figure 10 describes the two interdependent paths required to move from the organisational vision (higher purpose) to the desired outcomes and results.

An organisation with a great strategy and a poor culture will continue to find ways to work against itself and not meet its potential. An organisation with poor strategy and a great culture, will be a fun place to work in and deliver good, yet not great results; unable to consistently replicate performance. Only when both strategy and culture are aligned beneath an aspirational and ambitious vision, can sustained success be generated.

Consequently, progressive councils are increasingly investing in leadership development with due consideration for both culture and strategy. Specifically with regards to income generation, forward planning for change should include the time and space for officers and members to breakdown silos, to network and transfer knowledge, to share insights about what does and does not work in practice and the latest innovations (eg procurement protocols for investment, new tradeable asset classes), but also to identify new commercial opportunities to co-produce solutions – that is, cross-departmental working (to realise overarching financial and socio-economic goals), joint investments (both as an investor or an investee), shared services and other collaborative ventures (locally, nationally or internationally, as appropriate). Such a platform will help to overcome the chance and binary nature of discovering new viable commercial options. More than this, it can provide a vital route to identify like-minded partners that can form a collective voice to lobby central government (if and when needed) on the policy reforms required to accelerate council income generation even further.

Figure 10 Culture change



How we can help

These are challenging financial times for local government, but income generation can be the key to doing more with less.

Your ability to take-up new income opportunities is framed by the external and internal factors that are unique to your authority, ranging from in-house capacity to respond, through to risk appetite.

Grant Thornton has significant experience of working with councils and the wider public sector to review and develop income generation strategies and implementation plans. We deliver our services in a way that meets your needs and situation in the three areas as depicted in the diagram below. This covers all technical aspects related to visioning, finance, governance, tax, HR and legal aspects.

We can either act as critical friend and provide an independent view, or join forces with you as a delivery partner to transfer knowledge and build your capacity to become self-sustaining.

Three step process to supporting your strategic approach to income generation

1

Understanding your current performance
Diagnostics to baseline current fees, charges and assets across departments/services and benchmark performance with comparators (eg application of the Grant Thornton/CIPFACFO Insights tool, depicted below).

Evaluating the efficiency and effectiveness of your current procedures for income generation to understand good practice, gaps and areas for improvement.

2

Identifying your new opportunities
Workshops to raise stakeholders' awareness of policy context (legal powers, market reforms) and new options for income, and to understand your risk appetite.

A bespoke framework with criteria and a decision-making tree to identify a short list of new income opportunities for you to exploit (eg rate of return, payback period, ease of implementation, risk, social value).

Acting as a critical friend to develop the outline business cases for different delivery models and corporate financing (eg wholly owned trading companies and JVs, loans and equity, etc).

3

Developing your governance and programme management processes
Due diligence to ensure income and efficiency plans are aligned and integrated (synergies, risks).

Guidance on appropriate governance arrangements and programme delivery processes (eg OGC, Agile and Prince 2).

Outline and full business case development (ie financial modelling, tax, HR and legal aspects).

Supporting you with the drafting and finalisation of a revised/new corporate commercial strategy and implementation plan that is the culmination of this three step process.

Glossary of financial terms

	Instrument	Description
Facilitate or regulate	Advertising or place-based Corporate Social Responsibility (CSR)	Releasing the asset value of the council brand and/or prime marketing space, purely for financial purposes or also associated with wider social goals for local private employers.
	Crowdfunding and open-source	The practice of funding a civic project or venture by raising many small amounts of money from a large number of people, typically via the internet.
	Land Value Capture or developer tariffs	Strategic taxes or charges on key sites to recoup capital costs in recognition of how their rental or sales price will rise upon development completion, such as a Community Infrastructure Levy or Section 106 Agreement. May involve selling developer rights as opposed to the land itself.
	Local taxes	Statutory and discretionary taxes (eg Council Tax, Precept, Business Rates)
	Pollution charges	Cost recovery to pay for public services to clean up the impact of emissions and to invest in cleaner alternatives (eg congestion charging for private fossil fuelled cars to fund public electric vehicles) .
	Local Plans and Sustainability Supplementary Planning Documents (SPD)	Provide further guidance on compulsory or voluntary measures included within spatial frameworks. For a Sustainability SPD this utilises local plans to set policy requirements related to the integration of climate change adaptation measures into new developments (eg sustainable drainage systems, measures to reduce water consumption in areas of water stress, green infrastructure, passive cooling strategies).
Public funds	Joint purchasing agreements	Councils coming together to bulk buy green goods/services at reduced cost.
	Pooled financing agreements	Councils coming together to co-invest in infrastructure at a reduced cost or lend to each other at soft rates.
	Local development banks / funds from municipal pensions	Local, regional or national agencies which have facilities to support general development financing, comprising non-reimbursable and reimbursable funds (eg the European Investment Bank has facilities to finance infrastructure projects such as water management, energy or roads).
	Enterprise Zones (EZs) or Accelerated Development Zones	A geographically defined area offering certain incentives (eg tax breaks or grants) to businesses that choose to physically locate within the zone. Often one component of an overall economic growth strategy, aimed at enhancing the competitiveness of manufacturers and service providers, and also intended to realise agglomeration benefits from clustering industries in one area.
	Revolving funds	Internal or soft loan scheme whereby the council spends or loans money at zero or low interest to fund, for example, new homes building or eco-efficiency technologies in municipal buildings, which is then repaid from the respective property sales/rental receipts or utility savings made as a result.

	Instrument	Description
Equity stake	Financial contribution to PPPs or Special Purpose Vehicles (SPVs) delivering infrastructure, delivering services or developing land	Often a dedicated business that provides a range of services such as a Housing Company or Energy Services Company (ESCo) that designs and implements homes development or utility saving/power generation respectively.
	In-kind contribution to PPPs or SPVs delivering infrastructure, delivering services or developing land	Similar to above but with non-financial contributions such as through a gainshare model (whereby the private sector provides the upfront capital for a council's revolving fund) or the redirection of local municipal pension funds.
	Enterprise Zones (EZs) or Accelerated Development Zones	A geographically defined area offering certain incentives (eg tax breaks or grants) to businesses that choose to physically locate within the zone. Often one component of an overall economic growth strategy, aimed at enhancing the competitiveness of manufacturers and service providers, and also intended to realise agglomeration benefits from clustering industries in one area.
Debt finance	Climate derivatives	Carbon trading or credits such as the EU Emissions Trading Systems (EU ETS) and the Clean Development Mechanism (CDM), whereby finance is provided by companies seeking to reduce their emissions liabilities.
	Municipal bonds	A bond is a promise to pay a loan with interest and issued by a council or government to fund capital expenditure projects. Some municipalities market the bond to the market as sustainable to attract new types of investors.
	Social impact investors or micro-creditors	Responsible investors or lenders who offer finance because of wider sustainability returns and/at lower rates. Usually targeted at small or social enterprises during start-up phase or next-phase growth.
	Sukuk	A special form of bond that complies with Islamic law and investment principles which prohibit lenders from charging interest. The certificate constitutes partial ownership in a debt. Capital protection is provided by a binding promise to repurchase certain assets.
	Tax Increment Financing	A special form of bond which exacts current value from future tax receipts arising from a boost to GDP associated with a particular major development (eg housing, public transport)
	Public or private loans	State-subsidised or market rate borrowing (eg PWLB).

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About us

Dynamic organisations know they need to apply both reason and instinct to decision making. At Grant Thornton, this is how we advise our clients every day. We combine award-winning technical expertise with the intuition, insight and confidence gained from our extensive sector experience and a deep understanding of our clients.

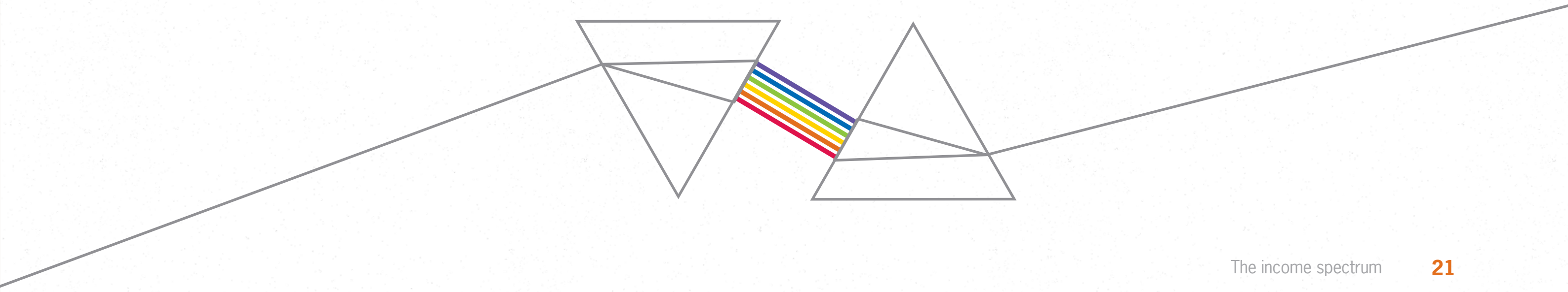
Grant Thornton UK LLP is a leading business and financial adviser with client-facing offices in 24 locations nationwide. We understand regional differences and can respond to needs of local authorities. But our clients can also have confidence that our team of local government specialists is part of a firm led by more than 185 partners and employing over 4,500 professionals, providing personalised audit, tax and specialist advisory services to over 40,000 clients.

Grant Thornton has a well-established market in the public sector and has been working with local authorities for over 30 years. We are the largest employer of CIPFA members and students in the UK. Our national team of experienced local government specialists, including those who have held senior positions within the sector, provide the growing range of assurance, tax and advisory services that our clients require.

We are the leading firm in the local government audit market. We are the largest supplier of audit and related services to the Audit Commission, and count 35% of local authorities in England as external audit clients. We also audit local authorities in Wales and Scotland via framework contracts with Audit Scotland and the Wales Audit Office. We have over 180 local government and related body audit clients in the UK and over 75 local authority advisory clients. This includes London boroughs, county councils, district councils, city councils, unitary councils and metropolitan authorities, as well as fire and police authorities. This depth of experience ensures that our solutions are grounded in reality and draw on best practice. Through proactive, client-focused relationships, our teams deliver solutions in a distinctive and personal way, not pre-packaged products and services.

Our approach draws on a deep knowledge of local government combined with an understanding of wider public sector issues. This comes from working with associated delivery bodies, relevant central government departments and with private-sector organisations working in the sector. We take an active role in influencing and interpreting policy developments affecting local government and in responding to government consultation documents and their agencies.

We regularly produce sector-related thought leadership reports, typically based on national studies, and client briefings on key issues. We also run seminars and events to share our thinking on local government and, more importantly, understand the challenges and issues facing our clients.



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