BUDGET AND PERFORMANCE PANEL

STOREY CREATIVE INDUSTRIES CENTRE
25 September 2012

Report of the Chief Executive and Head of Resources

PURPOSE OF REPORT

To respond to questions raised by Councillor Mace at the 17 July 2012 meeting.

This report is public.

RECOMMENDATIONS OF THE CHIEF EXECUTIVE AND THE HEAD OF RESOURCES

(1) That the report be noted.

1.0 Introduction

1.1 At its meeting on the 17 July 2012, the Panel was requested to consider a number of questions from Councillor Mace regarding the Storey Creative Industries Centre (SCIC). It was agreed that a report be requested to be submitted to the Panel in relation to these questions.

1.2 Councillor Mace has submitted five questions: question numbers 1-3 have been answered by the Chief Executive and question numbers 4 and 5 by the Head of Resources.

2.0 Questions

2.1 The questions answered by the Chief Executive are set out below:

Q 1: Has any contact taken place between representatives from sub-tenants of the building and the City Council as ultimate landlord (owner of the building)?

A 1: A meeting took place with the tenants of the building on Wednesday, 11 July. The purpose of the meeting was to gather information from the tenants in terms of the detail of their leases with SCIC Limited. At the time the meeting was organised, the Council was planning to have a smooth transition from SCIC Limited to the Council. However, by the day of the meeting it was necessary to update tenants that as a result of the call in, the Council was yet to resolve its position.

A second meeting took place with tenants on Friday, 17 August, following SCIC Limited ceasing trading on 15 August. This was to share information on the current position, particularly the interim arrangements put in hand by the sub-tenants to keep the building open. Sub-tenants were keen to know the Council's future plans for the building, pending the outcome of the liquidation process. It was necessary to explain to tenants the Council's position in advance of Council reaching a decision on its intentions for the Storey Institute, which would not be made before the 12 September.

A further meeting with tenants was held on 05 September. This was arranged to outline the Council report and highlight the opportunity for sub-tenants to make statements to Council, as well as share the limited information available regarding the liquidation and any updates on the interim arrangements.

There have been various email communications in response to the Council report.

Further meetings and updates will now be held with tenants in view of Council's decision.

Q 2: Did the City Council pay the insurance bills and a utility bill for SCIC in mid 2011 and if so, why and on what authority? Why did the City Council not take further action to protect its interests at that time?

A 2: The insurance bills are always paid by the Council as it is the policyholder. The policy covers all relevant council buildings for the full year - there isn't a separately policy or bill for each building. For 2011, the Council then recharged the apportioned insurance costs in the normal way, by raising an invoice to the company. Insurance arrangements are the responsibility of the Head of Resources. Recharging arrangements back in 2011 were the responsibility of the Head of Property Services (who now form part of Resources).

With regard to energy, the Storey was always included on the Council's energy contract; this had allowed the company (and, therefore, the sub-tenants) access to cheaper energy rates. The company had paid the energy bills for the building directly, but when the company experienced cashflow difficulties, it entered into a payment plan with its provider. To protect the Council's interests, the building was removed from the Council's contract at the beginning of November. The company could not keep up its repayment plan. Such energy arrangements were the responsibility of the Head of Property Services (again, they now form part of Resources).

The total £38,000 owing to the City Council in respect of insurance and energy was considered and incorporated into the loan agreement. In effect, £12,900 was deducted from the £90,000 loan, resulting in a cash advance of £77,100. The remaining £25,100 owing was consolidated into the loan agreement, repayable over three years with interest.

Q 3: Why was the decision taken in December 2011 to grant the loan to the company without democratic accountability? [Opening it up to scrutiny could have saved at least four more months of losses and inaction.]

A 3: The decision was taken with democratic accountability and in accordance with the City Council's Constitution. The decision was taken in consultation with the Leader of the Council and the Cabinet Portfolio Holder. (In fact, the Leader took the unusual step of discussing the matter informally with Cabinet Members in advance of taking the decision.) The urgent decision was then considered in terms of waiving the call-in by the Chairman of the Overview and Scrutiny Committee and subsequently the urgent decision was reported to Full Council in the Leader's report. It is not correct to say that waiving the call-in led to loss of savings or inaction. The decision preserved the continued running of the building and the costs/risks of making the loan were considered alongside the greater cost/risks of VAT and clawback.

2.2 The questions answered by the Head of Resources are set out below.

Q 4: What processes of due diligence took place before the loan was agreed in principle in December 2011, when was the loan paid over to the company, and what due diligence took place between the agreement in principle, and the payment of the loan to the company?

A 4: The loan was agreed in full in December 2011. Delegated authority was given to agree terms and conditions.

Extensive queries and reviews were undertaken with evidence being sought on the company's position, from a cross-service perspective (Finance, Property, Legal, Regeneration, and to a lesser extent Community Engagement). The implications of not granting the loan were also assessed as far as possible, in particular VAT and clawback. The VAT risks were estimated at around £230K per year, based on the building's VAT status at that time.

The company's previous year accounts and management accounts were assessed. The company had produced a sustainability plan and that was appraised. A meeting was held in December with representatives from the company, to allow questioning. Various communications took place with the Company's Board and its Finance Committee.

The processes are reflected and summarised in the exempt Urgent Business Report and the Panel is advised to refer to this for more background. Essentially, the due diligence and decision to grant the loan came down to balancing the risks either way, and the following extracts summarise the rationale for granting the loan, but acknowledging the risks involved.

"Option 1 is the preferred option as the potential risk of non-recovery of loan repayments is considered more manageable for the Council when compared to the increased likelihood of far more significant operational and financial implications arising should SCIC Ltd cease trading. That said, it is recommended that further work be done to assess VAT options and to clarify (with the aim of avoiding) clawback liabilities, in order to give the Council greater flexibility in managing its interests in the building.

Conclusion

There is an opportunity for the Council to prevent SCIC Ltd failing in at least the short to medium term by providing it financial assistance by way of a loan *on a fully repayable basis over three years. If approved, it is reasonable to assume that provided the SCIC at worst case continues to maintain its current occupancy levels, it can become a self sustainable operation based on its current financial projections. This should in turn protect economic benefits for the district by ongoing support of the development of the creative and cultural industries and visitor economy. There is no guarantee of such an outcome, however."*

Once the loan had been agreed, work focused on seeking details and agreement on creditors repayment plans and the terms and conditions attached to the loan. Details of the monitoring and financial management arrangements required under the loan are attached at ***Appendix A.***

Q 5: In what way and at what date did examination of the annual accounts of the company contribute to due diligence?

A 5: The draft annual accounts were reviewed at various points between August and December 2011. In particular, verification and explanation was sought on apparent discrepancies between the Council's accounts and that of the company. In summary, the accounts were used as a comparator for the company's sustainability plan and to inform the views of its overall financial position and outlook, as well as to gain greater understanding of the company's cash flow. Examples of this are highlighted in the exempt Urgent Business Report and extracts from one of the appendices are included below, to help demonstrate the processes adopted:

- *"Although [overall] forecast expenditure for 2011/12 is less than that outturned at 2010/11, this seems ok as the previous year included some one-off grant funded expenditure as verified by SCIC's draft accounts for this period.*
- *It has been queried whether it is prudent to reduce heat, light and power costs in future years compared to 2010/11 outturn, however SCIC believe they are currently being overcharged for their gas supply and are in dispute with [their provider]...."*

CONCLUSION OF IMPACT ASSESSMENT **(including Diversity, Human Rights, Community Safety, Sustainability and Rural Proofing)** N/A
LEGAL IMPLICATIONS None directly arising as a result of this report.
FINANCIAL IMPLICATIONS None directly arising as a result of this report.

OTHER RESOURCE IMPLICATIONS

Human Resources:
None arising directly as a result of this report.

Information Services:
None arising directly as a result of this report.

Property:
None arising directly as a result of this report.

Open Spaces:
None arising directly as a result of this report.

SECTION 151 OFFICER'S COMMENTS

The s151 Officer (as Head of Resources) as contributed to this report.

DEPUTY MONITORING OFFICER'S COMMENTS

The Deputy Monitoring Officer has been consulted and has no observations to make on the contents of this report.

BACKGROUND PAPERS Urgent Business Report 20 December 2011 (Exempt from publication)	**Contact Officer:** Mark Cullinan **Telephone:** 01524 582011 **E-mail:** chiefexecutive@lancaster.gov.uk **Ref:** CE/ES/Committees/B&PP/25.09.12

APPENDIX A

MONITORING AND FINANCIAL MANAGEMENT ARRANGEMENTS (AS REQUIRED UNDER LOAN AGREEMENT)

Immediately following acceptance of the loan agreement, the Borrower takes any actions necessary to ensure its financial management, monitoring and administration arrangements are robust and adequately resourced. This includes (but is not limited to) ensuring the timely setting and full recovery of all relevant rents and service charges, so as to assist the Borrower in discharging its financial liabilities to the Council under this agreement .

On request and at appropriate and timely intervals the Borrower will provide information as reasonably required by the Council's Head of Financial Services or their nominated representative, including but not restricted to:

- Creditor invoices, payment receipts and copies of bank statements to evidence both the need for advance of loan and also the subsequent application of loan and discharge of creditor liabilities
- Monthly management accounts including aged debtor and creditor lists
- Monthly cashflow statements
- Annual Business Plan
- Annual Financial Statements
- Reports produced by the Borrower's Accountants or Auditors.

The Borrower will continue to provide the Council's Head of Financial Services or her nominated representative an invitation to attend its Finance Sub-Committee meetings for the duration of the loan agreement as an observer.

The Borrower will continue to provide the Council copies of Board papers and the annual report to the Council and an invitation for the Council's contact officer to attend Board meetings as an observer.

In addition, insofar as it relates to this loan agreement or the Borrower's ability to discharge its obligations therein, the Head of Financial Services or their nominated representative may report directly to the Finance Sub-Committee or the SCIC Board.

The Borrower will allow access to the building and keep suitable records including a record of all expenditure and all other invoices, receipts and other relevant documents to support the information required by the Council's Head of Financial Services, or her nominated representative, for the duration of the loan agreement.