5 October 2023	ITEM: 6
Corporate Overview and Scrutiny Committee	
Report of the Cabinet Member for Finance, HR and Payroll/Financial Strategy Update	
Wards and communities affected: All	**Key Decision:** None
Report of: Cllr Graham Snell, Portfolio Holder for Finance, HR and Payroll	
Accountable Assistant Director: N/A	
Accountable Director: Steven Mair, Interim Chief Finance Officer	

1 EXECUTIVE SUMMARY

1.1 This annual report from the Cabinet Member for Finance, HR and Payroll focuses on providing the Committee with a detailed update on the work being undertaken to address the Council's financial challenges. This deviates from the traditional annual cabinet member report formats to enable the focus to remain on the financial sustainability of the Council, Furthermore, it provides the committee the opportunity to provide critical feedback as the wider financial strategy develops. This will inform future updates to Council members and the ongoing delivery of the strategy itself.

The report focuses on three areas:

- financial strategy
- divestment of the previous investments
- other financial management initiatives

1.2 The financial strategy aims to:

- sell £1.035bn of **investments** to the fullest extent possible and pay down debt and in doing so ensure the governance, project management, budgetary control etc of this programme of work is properly undertaken
- generate at least £150m of **capital receipts** and pay down debt. This is under review and will be updated in subsequent reports
- reduce reliance on borrowing to fund GF **capital programme** to avoid increasing debt and improve its capital strategy.
- save a further £1m in the 2023/4 **revenue budget** to comply with the Commissioners comment in the 2023/24 budget report.
- save **£18.2m from the revenue budget** for next 2 years and a further £13.65m 7.5%, for each of the following 3 years. This may change over time
- review and improve its **treasury management strategy and MRP policy** and currently assumed budget for MRP.

- review and revise the Council's **finance structure, culture and improvement plans** addressing capacity and skills assessment and development which will develop the service.
- review the Council's **risk management** processes and improve them.
- design and implement a range of improvements to deal with **compliance** with all necessary rules, regulations, delegations, governance of the commercial portfolio and
- a number of further **financial management improvements**

1.3 The divestments workstreams encompass 14 investments covering £1.035bn of original investments of which the 5 major ones are currently in progress and the Council aims to have divested or have underway the divestment of 93% of the Council's investment portfolio by 31 March 2024. The balance of 7% is currently being planned.

1.4 The work involved in this is very complex and is dealing with a number of issues:

- two of the divestments are effectively outside of the Council's control – Toucan and JLG/JCF as these are companies in administration with court appointed administrators
- the others are and will be actioned by the Council
- governance of the work is developing as is project management
- performance monitoring of investments is identified and will improve
- likewise budget management of the related fees and costs
- litigation options are being explored and appropriately actioned

1.5 The other financial management initiatives encompass:

- disposing of capital assets to generate capital receipts – currently estimated at £150m over 5 years. This is under review and will be updated in subsequent reports
- very significantly reducing the general fund financed capital programme focussing on essential and statutory requirements – underway
- strengthening of governance over the capital programme with strengthened reporting of the financial position, forecasting and risk
- £18.2m of revenue savings in 2024/25 and beyond along with improvements to the revenue budget process, timing, consultation, rigour etc
- changes to related budget preparation ie DSG, HRA, treasury management
- a review of MRP
- a restructure of the finance service including change and culture as well as technical, capacity and skills assessment and development
- planned improvements in risk management and compliance
- a range of further enhancements in revenues and benefits
- likewise in preparation of accounts beyond 2021/22
- a review of the Council's financial modelling, financial implications, business partnering, internal audit among others

2 RECOMMENDATIONS

2.1 It is recommended that the Committee:

i) notes the progress on the investment recovery and divestment strategy

ii) notes the progress being made on the other financial actions

iii) notes the urgent ED2 decisions made to date

iv) notes the continued use of necessary advisors as required until completion of work associated with divestment of and recovery of value of investments including the conduct of litigation, subject to the review of the programme currently being undertaken by the Council's officers to be reported to Cabinet in November 2023 and the Leader, Finance PFH, Chief Executive and Commissioners being consulted before advisors are instructed on new work streams

v) notes that the each council Director involved in delivering the strategy is in consultation with the Leader, Finance Portfolio Holder the Section 151 officer, the Monitoring Officer (where the Director does not fulfil one of those roles) and Commissioners is authorised within their professional area to:

(a) subject to recommendation 2.1 iv), to procure and appoint the advisors using the most expeditious and efficient procurement process which is lawfully available under the Public Contract Regulations 2015 and that the financial thresholds in the Council`s Contract Procedure Rules are waived for this purpose; and

(b) to take all action necessary (within appropriate budgets) to ensure the implementation of the Council`s recovery strategy if timescales do not allow for a report to Cabinet as long as a full update is provided at the next available Cabinet meeting.

vi) notes the Director of Law and Governance is authorised to the commence legal proceedings for potential claims where there is a supportive advice from a King`s Counsel together with any associated action after consultation with the Leader Chief Executive, Section 151 Officer and Commissioner subject to reports on progress being brought to Cabinet.

vii) notes the Section 151 Officer in consultation with the Leader and Portfolio Holder, the Monitoring Officer and Commissioners is given delegated authority to take all action necessary to implement the divestment strategy where a divestment meets the criteria set out in the Direction subject to reports on progress being made to members.

viii) notes that the main objective is to reduce the Council's exposure to financial risk by delivering a divestment strategy that optimises (sums and timing) receipts to repay the borrowings as long as doing so .secures best value using its criteria set out in this report

ix) notes an indicative hurdle rate of 12% (i.e., 7% PWLB rate and 5% MRP) is set for investment yield / return, with anything yielding less being put forward for sale, subject to the detail of the individual investment, the Council's contractual obligations and the ability to deliver value for money

x) notes and agrees the review of the programme as set out in paragraph 4.70 and requests regular reports back to Cabinet on progress on the financial strategy

COMMISSIONER COMMENTS

The report sets out the financial strategy, as overseen by the Financial Recovery Board put in place as a result of the directions. On 2 September 2022 the former Secretary of State announced that after due consideration he was using his powers under the Local Government Act 1999 to intervene at the council, given the great concerns about the scale of the financial and commercial risks potentially facing Thurrock Council. This included directions requiring a strict debt reduction plan and action to ensure that the investment and treasury strategies are sustainable and affordable.

As laid out in the report, Thurrock has made good progress made on the divestment strategy, supported by appropriately skilled advisors, with a clear action plan to divest of £1.035Bn of investments. There is also a clear plan for property asset disposal with a £150m disposal programme set out, noting that this figure is under review. These divestments will in turn will reduce the borrowing costs and support pay down of the debt – in accordance with the directions from the Secretary of State. The actual investment sales will proceed through 2023/4 and into future financial years. Commissioners will maintain a close overview on the delivery of the action plan through the Financial Recovery Board.

The broader financial strategy as set out from section 4 outlines the key components of the financial strategy. There are two important considerations that commissioners want to emphasise:

First, is that considerable savings are required. Looking ahead there are planned savings of £18.2m from the revenue budget for next 2 years (to 2024/25) and a further £13.65m 7.5% for the following 3 financial years. The most significant decisions lie ahead, whereby difficult choices around prioritisation and transformation will be required. Further reports will be coming to Cabinet later in 2023 to outline the choices as a precursor to the 2024/25 budget setting.

Secondly, as laid out in 3.10 and 4.139, the audit of accounts from 2020/21 remain outstanding; that is there are 3 years of open historic accounts. Until such a time as those accounts are finalised and opinions provided, there remains a risk around the full and accurate determination of the financial gap. The financial strategy is based on recovery of the financial position as understood and reported (most recently in the Quarter 1 report to the September Cabinet). There is an inherent risk that that position could change subject to finalisation and potentially any restatements arising

3 INTRODUCTION AND BACKGROUND

3.1 The purpose of this report is to provide Cabinet and Council with the first of a planned series of updates covering the financial work being undertaken in response to the very serious financial challenges the Council is facing. This includes responses to the recommendations from the Secretary of State and other improvement work generated by the Council.

3.2 The financial position of the Council is extremely challenging in terms of the scale of the financial impact, the time it will take the Council to recover from this and the range of issues to be dealt with. The position will undoubtedly regularly change and resolving all the known matters will take at least 5 years. A great deal of work has been undertaken and is planned to continue and develop further to improve the Council's financial position.

3.3 As part of this improvement journey the opportunity is being taken to develop a comprehensive update for Members, and other stakeholders as appropriate, on the Council's finances, processes etc. This report is intended to start the journey of providing holistic updates on the various financial issues the Council faces and how it is addressing these. It will be continually refined in the coming months as information is brought together, analysed, and assessed. This report is therefore a work in progress with some information currently being more developed than others. As this is the initial report this contains background information which will not be necessary in the future when the reports will focus more on updates on progress.

3.4 It should also be noted that the embedding of all of the work now being undertaken and developed will take some considerable time to fully implement. This combined with the related culture change and continuous improvement will continue to evolve.

3.5 This and future reports will enable the Council to demonstrate appropriate levels of transparency and information on progress towards financial recovery.

3.6 The report provides an update on the following specific issues:

- **financial strategy**
- **divestments** including financial recoveries and potential litigation
- **financial management actions/improvements**
  - capital receipts
  - capital programme
  - revenue budget
  - treasury management and MRP
  - finance structure
  - risk management
  - compliance
  - revenues and benefits
  - accounts
  - other financial improvements
  - the current forecast financial position of the Council in 2028/29.

3.7 Members will be aware of the Directions received from the Secretary of State which are set out in Appendix A and are elements of Part 1 of the Local Government Act 1999, combined with five specific actions. The Council is however also addressing other issues that will support the financial changes needed in the Council.

3.8 Members will also be aware of the current key financial challenges facing Thurrock which arose from:

- over-reliance on investment income to support revenue budgets - proportionality risk;
- over investment in one solar/windfarm basket - investment concentration risk;
- long-term investments funded by borrowing on temporary markets from other local authorities - interest risk;
- very significantly inadequate budgeting for MRP - legality risk.

3.9 These issues crystalised adversely for the Council and resulted in the Secretary of State announcing intervention on the 2 September 2022 and the acting s151 officer issuing a s114 notice in December 2022 with the Council facing, as identified as of December 2022:

- a deficit in annual revenue investment income of £41.5m;
- a collapse in asset values of investments;
- inaccessibility to the short-term local authority borrowing market and rising interest rates resulting in the need to transfer £1.043bn to PWLB and interest rates rising from 0.5% to 5% at an increased annual cost of £28.3m in 2023/24;
- a then estimated budget pressure of £116m to budget for MRP;
- a potential long term capitalisation direction of £802m;
- continual revenue budget deficits for the long-term duration of the MTFS.

3.10 The Council also received on 15 June 2023 the Best Value Inspection report which has been separately reported to Council and is not repeated here for that reason. Without pre-empting what the Council’s external auditors may report in the future it is reasonable to assume they will make recommendations in respect of the accounts and possibly other matters. Regarding the former the current focus of work is finalising the 2020/21 accounts, while progressing preparation of the 2021/22 and 2022/23 accounts. Likely areas of comment arising from this will be identified and addressed by the Council from September 2023. Regarding these the ongoing work by the Council will assist with what the auditors may, or may not, also raise.

4 ISSUES, OPTIONS AND ANALYSIS

4.1 The issues are categorised within the report into the financial strategy, the main area of work which is the divestments and the improving financial management practices being undertaken.

Financial Strategy

4.2 The Council has a developing **financial strategy** designed to address the Secretary of State Directions and its underlying financial challenges. The fundamentals of this strategy are to:

Divestments

- sell £1.035bn of **investments** to the fullest extent possible and pay down debt and in doing so ensure the governance, project management, budgetary control etc of this programme of work is properly undertaken

Financial Management

- generate at least £150m of **capital receipts** and pay down debt. This is under review and will be updated in subsequent reports
- reduce reliance on borrowing to fund GF **capital programme** to avoid increasing debt and improve its capital strategy.
- save a further £1m in the 2023/4 **revenue budget** to comply with the Commissioners comment in the 2023/24 budget report.
- save **£18.2m from the revenue budget** for next 2 years and a further £13.65m 7.5% for the following 3 years. This may change over time
- review and improve its **treasury management strategy and MRP policy** and currently assumed budget for MRP.
- review and revise the Council's **finance structure, culture and improvement plans** addressing capacity and skills assessment and development which will develop the service.
- review the Council's **risk management** processes and improve them.
- design and implement a range of improvements to deal with **compliance** with all necessary rules, regulations, delegations, governance of the commercial portfolio and
- a number of further **financial management improvements**

Divestments

4.3 In recent years, the Council had built up a substantial investment portfolio, all funded by borrowing temporary loans from other local authorities. Not only is it necessary to divest from the investments to satisfy the Government Directions, but also because the costs of funding the portfolio have risen significantly in the past 18-24 months which combined with proper accounting for MRP means that most of the investments are no longer generating a positive yield for the Council. Furthermore, the medium-term interest rate forecasts indicate that rates are unlikely to reduce markedly in the medium-term. Consequently, it is logical to divest to reduce the financial risk associated with the portfolio. Notwithstanding this, the Council also needs to ensure that best value judgements are taken in respect of the disposal of each investment.

4.4 The Council's investment portfolio comprises 14 investments totalling £1.035 billion. To date the focus has been on disposing of the largest investments – Toucan and JLG, which collectively represent circa 75% of the Council's portfolio and therefore, the largest part of its exposure. These companies have been restructured and are currently in administration. Consequently, the divestment of these assets is following a predetermined process supported by the Council. In addition, the Council has commenced divesting from the CCLA Property Fund. The decision has been approved by ED2 but will take 6 months to crystallise following the call notice being issued to the fund – proceeds are expected end of January 2024. The £0.9m in the CCLA diversified fund has been received.

4.5 In addition, with Toucan and JLG, there are litigation routes available to the Council and the report includes updates below.

4.6 A further 7% of the investments are currently under active review with divestment analysis and options planning underway. Therefore, the Council aims to have divested or have underway the divestment for 93% of the Council's investment portfolio by 31 March 2024.

4.7 That will then leave a small proportion of smaller investments, totalling circa 7% or £67.6m where assessments will need to be undertaken and the Council's options as well as strategy planned out.

4.8 The recoveries shown below do not include any monies that could be claimed via litigation. Workstreams are ongoing and claims need to be fully assessed, along with the costs of litigation.

4.9 There are a number of **overarching issues** with the divestments programme:

- firstly, while highly implicit in Council reports and under Government Direction the Council should take a formal explicit decision on the overall aims/intention of the divestment programme.

- secondly to seek to make progress on the divestments there have been 4 confidential urgent decisions made since September 2022. These currently remain confidential. The aim from this and subsequent Cabinet meetings is to make Cabinet aware of the progress on the divestments and “regularise” i.e., seek Cabinet approval for the four divestment decisions to date, along with current advisor appointments. As far as possible future decisions will either be made formally under delegated powers, if agreed by Cabinet under this report, and then with retrospective updates to the next Cabinet meeting or at Cabinet if time allows. The confidential urgent decisions will be released publicly as soon as possible

- thirdly as reflected in the Best Value Inspectors Report (BVIR) the governance processes generally at Thurrock were not always well developed. It has taken time to put in place the full governance required for the major programme of divestments which has been developed to date with Commissioners, but as set out in this report that governance process is now developing further. Likewise, there is an emerging focus on project management which is similarly being developed

- fourthly any future investments and those still operating during the current sales process must have regular performance reporting which is to be developed in the Autumn and will include reporting to the Member Panel as well as Cabinet

- fifthly the recovery of funds is clearly fundamental to the Council’s financial recovery and where funds have been so far recovered, they are set out in paragraph 4.26, and Cabinet will be updated as and when matters are developed further

- sixthly, given the material quantum of the advisors fees, work is ongoing to provide additional assurance about the original procurements and to improve budget management and cost control

- finally, it is important that the Council begins to develop good and commercially sensitive visibility of upcoming divestment decisions to the end of the 2023/24 financial year, which should see a significant proportion of the financial investment portfolio realised and used to repay Council borrowing. Future work is being planned and will be reported in more detail to subsequent meetings

Decision to Divest

4.10 The Government Direction states that there should be a “strict debt reduction plan” and various reports of the Council refer to this matter and it is clear that in considering matters related to **divestment**, there is an implicit acknowledgement that the Council is pursuing a divestment strategy. However, the decisions taken by the Full Council, the Cabinet and the Corporate Overview and Scrutiny Committee were “passive” decisions. For example, in relation to the Treasury Management Strategy 2023/24 to “Note the divestment of investments and the sale of property assets are required to repay the Exceptional Financial Support from DLUHC and this is a key assumption supporting the strategy.

4.11 Regarding the way divestment decisions should be taken it is imperative that these decisions achieve best value and the Council likewise agree to this. Best value is assessed by comparing the gross return (i.e. distributions/interest and changes in market value) from the investment against the cost of financing the investment (i.e. interest plus MRP where applicable).

4.12 The majority of the investment portfolio meets the statutory definition of capital expenditure and should have had MRP charged. The CCLA Property Fund and some of the solar farm investments do not meet the statutory definition of capital expenditure, but were nonetheless financed from borrowing, and therefore require the accounts to be restated:

- in the case of the CCLA Property Fund this is being redeemed in 2023/24 and the proceeds applied to reduce borrowing.
- in the case of expenditure on the solar farms where the expenditure does not meet the statutory definition of capital expenditure, the investment will be reclassified but also because there is no asset to support the “investment”, this will have to be impaired as it is irrecoverable. This will result in an unbudgeted revenue expense which is currently being reviewed and assessed.

4.13 The MRP on both the capital investments and the Capitalisation Direction is at least 5%. Interest rate costs are now running at c. 7%. Consequently, the overall cost of holding the investments is at least 12%. In all cases investment returns are below 12% or expected to be so given current known information. Therefore, even where there were regular Local Government Treasury Management operations an authority would look to divest of those “loss making” investments providing that there is no significant financial downside to the divestments or repaying the borrowings.

4.14 The actual interest and MRP percentages may vary depending on the useful life of the asset and the actual interest rate at a point in time, however as a guide 12% is a reasonable indicator which will be refined for each specific instance.

4.15 Thus it is recommended that an indicative hurdle rate of 12% (i.e., 7% PWLB rate and 5% MRP) is set for investment yield / return, with anything yielding less being put forward for sale, subject to the detail of the individual investment, the Council’s contractual obligations and the ability to manage any associated risk.

4.16 In addition, the Council did not have the skills or capacity to manage these investments when it first entered into them, which is contrary to the Statutory Guidance on Local Government Investments and its status as a MiFID II professional investor. Furthermore, it is only currently able to manage the current portfolio with substantial external advisory support.

4.17 To recognise and address this it is recommended that the Council confirms the following objective.

The main objective is to optimise (sums and timing) of the receipts and recover as much of the investment amounts the Council have made, to repay the borrowings as long as doing so secures best value using and demonstrating its criteria set out in this report.

Decisions to Date

4.18 The **4 decisions** taken to date which are consistent with the action required under the Direction are summarised below with the original ED2 reports attached as Appendices E to H:

- entering into a restructuring transaction in relation to Pure World Energy was agreed with the Council taking ownership of the company. Cabinet agreed the appointment of independent Non-Executive Directors

- support was given for Toucan Energy Holdings 1 (the1) Limited to place the company into administration with an administrator being appointed. Support was not given to signing a term sheet confirming its position in respect of the bond documents, and agreeing to the terms of restructuring provided by TEH1's lawyers.

- a decision was taken to serve notice on Shard Capital and Shard Credit to terminate the Relationship Agreement and request the return of the monies on account as soon as possible

- a decision was taken to divest of the £103m investment in the CCLA Property Fund and divest of the investment of £1m in the CCLA Diversified Income Fund

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4.19 The intention should be to publish these papers as soon as circumstances allow is as public documents once commercial considerations are past or using the Council's "pink papers" process in the meantime. This starts to be addressed through this report

Governance

4.20 The emerging governance of the divestment programme is as follows:

- Officer Investment Meeting (OIM), Investment Advisory Panel (IAP), Financial Recovery Board (FRB) and Improvement and Recovery Board (IRB). These in turn feed into Cabinet, Council, Commissioners. Both the OIM and IAP replaces the previous Strategic Investment Advisory Group (SIAG)

- The OIM (which first met in May 2023) is required to oversee the recovery work on the Council`s Investment Strategy and to report as necessary

- the IAP (which will first meet in September 2023) will monitor the financial position of the Council`s investments (both financial and property) and borrowings and make recommendations to the Leader /Council. In addition, it should receive regular reports on the performance of the Council`s investments, review the Council`s Treasury Management and investment strategies, review new investment decisions, receive regular reports and review the performance, effectiveness and efficiency of the Council`s income generating and sold services, receive reports on and review the Councils disposal programme and make and review the performance of the Council's property assets, making recommendations. This work is being developed and will progress from September

- note, neither the OIM nor the IAP are decision making settings. Instead, OIM can make recommendations to IAP and then IAP can make recommendations to officers as well as the Leader and Cabinet. Meanwhile, certain actions can be progressed under delegated powers, but it will be important to communicate what actions have been progressed through these governance arrangements

4.21 Governance will continue to be developed as is seen through this report.

Performance Monitoring

4.22 There was very limited investment portfolio monitoring and reporting back to Members, despite the size of the Council's investment portfolio (just over £1billion) being equivalent to a London borough pension fund for which regular (i.e. quarterly) investment performance monitoring against benchmark performance measures is a requirement together with independent investment advice. In contrast there was no such detailed performance monitoring or independent investment advice sought or provided. This is now being addressed

4.23 CIPFA's Prudential Code 2021 edition introduced the requirement for performance against the prudential indicators to be reported to Members quarterly with effect from 1 April 2023. However, because of the size of the portfolio, this should have been happening in any case just as a matter of good practice. To comply with the Prudential Code 2021 edition, quarterly monitoring of both treasury (including the debt reduction strategy) and investment activities (including divestment) will commence with the quarterly position as at 30 June 2023

Progress in Divestments

Summary

4.24 The current work in progress on recovery of funds is show below, at an overall level the Council is progressing as shown.

In process of divestment	86% of portfolio (4 investments)
Under divestment review	7% of portfolio (2 investments)
Options/divestment analysis underway	3% of portfolio (2 investments)
Preliminary reviews underway	4% of portfolio (5 investments)
Restructured / recovered to date	one investment / circa £30 million.

4.25 It is important to note that the Council has some tail positions where there is no ability within the existing terms to divest till the maturity of the investment, which may be several years out. In the context of the Council's portfolio, they also represent a much smaller residual exposure once the above key positions have all been worked through. Analysis and divestment options will be prepared for each of the remaining tail investments in order of materiality over September and October 2023

4.26 The potential long term estimated financial recoveries remain under review. In the shorter term the following funds have been or should be received by 30 September 2023:

Table 1

Investment	Expected funds £m	Explanation
Toucan	38.0	Cash distributions from TEH1 (estimated)
Pure World Energy (PWE)	11.0	Repayment of funds and distribution
Shard	10.0	Cash returned following end of relationship agreement
Just Loans Group (JLG) / Just Cash Flow (JCF)	5.8	Cash from ongoing distributions
CCLA	0.9	Cash from redemption of Diversified Income Fund
Total	**65.7**	

Toucan Energy Holdings 1 Ltd (TEH1)

4.27 Regarding the specific divestments the administration of the Toucan Energy Holdings 1 (TEH1) investment is the most significant divestment and background; process and estimated timescales are set out below.

4.28 TEH1's director, Nicholas Pike, resolved to appoint administrators to the Company, having previously received a valuation of Toucan's solar portfolio which demonstrated that TEH1's liabilities exceeded its assets. Interpath Advisory were appointed administrators on 10 November 2022. An administrator is an officer of the UK High Court.

4.29 In an administration, the running of an insolvent company's affairs, business and property are managed by an administrator, who is a licensed insolvency practitioner. The powers and duties of administrators are set out in the Insolvency Act 1986.

4.30 The administrators' main objective is to realise assets and distribute net realisations to creditors – in this case this is currently understood to be the Council and HMRC.

4.31 In TEH1's case, the Joint Administrators have developed a strategy, on which they have consulted with Thurrock as TEH1's main creditor and worked with the Council's advisors, which involves creating a stable platform to seek to ensure the underlying subsidiaries and assets continue their day-to-day operations on a "business as usual" basis.

4.32 This has included:

- complying with the statutory and regulatory requirements of an administration, including establishing the claims of creditors, in particular Thurrock in its position as bondholder;

- preparing the Company's solar portfolio for sale and bringing the assets to market in a full suite Mergers and Acquisitions (M&A) process. Given the sale values envisaged and discussions with the top tier of UK and international renewables investors, this has included a full suite of technical due diligence, commercial diligence, legal diligence, financial and tax diligence, and obtaining indicative new debt funding at asset level. All this work is aimed at enabling buyers to bid full value with confidence concerning the underlying assets;

- undertaking a group reorganisation to create a clean, clear transaction perimeter to support value maximisation in the mergers and acquisitions process;

- investigating certain historic transactions to establish whether any claims can be brought by either TEH1, or associated Toucan companies. The Council and Interpath will, as this work develops, agree on the priority and relative merits and strength of each parties claims.

4.33 Interpath are assisted in this by:

- the financial advisor on the M&A process - KPMG LLP.
- the legal advisors are Herbert Smith Freehills LLP and Linklaters LLP.
- the other advisors to the M&A process are:
  - ✓ the Natural Power Consultants Ltd – technical due diligence on the solar assets.
  - ✓ Cornwall Insight Limited – commercial due diligence on the solar assets.
  - ✓ Interpath Limited – financial vendor assist, tax vendor assist and debt advisory.
  - ✓ Aon plc – insurance due diligence and Warranty & Indemnity broker support.

4.34 The current actual and planned timetable to completion, which is subject to change is:

- appointment of Interpath and advisors – November/December 2022
- preparation of sales process and materials – November 2022 to May 2023
- Toucan marketed 31 May 2023
- round one offers – July 2023
- phase 2 launch and phase 2 due diligence and bids – August 2023 to October 2023
- completion – estimated – by end of November 2023

4.35 The sales process currently remains on track per the timetable above.

4.36 Phase 1 non-binding offers were due in July and have been received.

4.37 The Council's advisors and the administrators are currently working with bidders to understand the details of the bids, gain an understanding of proof of funding from the leading bidders, as well as evaluating the structure of the bids from a financial and timing perspective.

4.38 The preferred bidders will be taken to phase 2, with a targeted transaction date of mid-November 2023. Careful risk management of the process and the second round of detailed due diligence will support delivery against the timetable above.

4.39 Alongside this, Interpath, in conjunction with the Council's advisors, have agreed the status of the Council's bonds to ensure net sales proceeds will flow to the Council with minimal complications.

4.40 The Council's advisors have also been consulting with the administrators to implement frameworks to receive distributions swiftly. The administrators have now confirmed that the Council can expect to receive circa £15m in the coming weeks, with a further £23m to follow shortly thereafter, less administration costs. The administrators have also acknowledged the significant help of the Council's previous work and advisors in speeding up the administration and sales of the assets.

4.41 Assuming a smooth sales process, the Council is expected to receive the vast majority of the net sales proceeds before the end of 2023.

4.42 Another source of recoveries is the litigation workstream. It is expected that any recovery from claims will take some time. The Council will also need to decide which claims it wishes to pursue in the first instance, given the common pool of assets being targeted. The Council will therefore undertake cost-benefit analysis to determine those claims with the strongest chances of success and ensure that these are pursued in the first instance. In the interim, steps have been taken to limit the dissipation of assets while the Council evaluates its claims.

CCLA Property Fund and Diversified Income Fund

4.43 The Council has exposure to two pooled funds run by **CCLA** (Churches, Charities and Local Authorities) Investment Management Limited, a well-known investment manager for local authorities. The majority of the exposure – an original investment of £103m – is to the CCLA Local Authorities' Property Fund (LAPF), which invests into a long-term, actively managed, and diversified portfolio of UK commercial property. There is also a small exposure of £1m (original investment) to the Diversified Income Fund, which looks to generate an income-focused return through a diversified actively managed portfolio of stocks, bonds, cash, and infrastructure assets in the main.

4.44 As of July 2023, the £103m is now valued at £96.3m, representing a loss of £6.7m. Disposal of this investment is a simple notification by the Council to the fund which has now been approved via an ED2 agreed but will take 6 months from end August in line with the Fund's redemption terms.

4.45 CCLA have confirmed that they have maintained significant cash in the fund, giving comfort that the redemption notice period should be met.

4.46 The Council has prepared the forms and submitted them on 28th July.

4.47 Regarding the Diversified Income Fund, redemption terms and process have been collated, with the redemption due to be submitted in August. The proceeds have been received.

Shard Credit Fund

4.48 **Shard** is a private credit fund, which makes loans to medium-sized companies. The Council invested in both the fund as well as co-invested alongside Shard to make loans to specific companies. £10m has been divested to date from the original exposure of £24.3m. Further analysis is underway on the remaining positions and will be complete by end of September 2023. This is a more complex position comprising loans to private companies, so the Council will need to examine the positions and potentially negotiate these individually to exit the arrangements in place.

Pure World Energy Ltd (PWE)

4.49 **PWE** is a company supplying heat pumps to council-owned leisure centres in the main which the Council invested £30m in. It has since been restructured after an options-based appraisal by Council. The majority of debt was converted to equity and £2m of senior debt retained currently. £10m has been recovered in cash and £1m of debt repaid to date. The Council's intention is to retain its exposure in the restructured company, as it develops its business further, subject to an ongoing and regular prudent assessment of risks. Under recommendation from the Council, to meet governance objectives, PWE are in the process of appointing two non-executive directors ("NEDs") to the board of PWE.

Just Loans Group (JLG) and Just Cash Flow (JCF)

4.50 The Council has several bond investments totalling £93.6m in **Just Loans Group (JLG) and Just Cash Flow (JCF)**, affiliated companies which make loans to UK SMEs. Most of the loans are small, with the average loan size being circa £60,000, but there are also a number of larger loans above £1m. JLG defaulted on one bond tranche in May 2021 and subsequent investigation revealed wider issues within the group and concerns for the Council's investments. Given the fundamental nature of the risks, significant work was undertaken by the Council and its advisors to stabilise the Group and prevent a disorderly collapse, which would have been more financially damaging for the Council. A restructuring and insolvency process was undertaken and the loans are currently being serviced and recovered by the administrator and an external servicer.

4.51 Assuming a smooth runoff process, the Council is expected to receive net recoveries of £31.5m over the next two years. Part of this has already begun to come through, with the Council having received £5.8m to date, with work underway to release up to a further £1.5m

4.52 Another source of recoveries is the litigation workstream. It is expected that any recovery from claims will take at least 1-2 years.

Wind Farms.

4.53 The Council has invested in two **wind farms** which are both illiquid private investments. If the Council wishes to exit these, it would need to sell the positions to a third party.

4.54 The Council's advisors have been analysing the assets as well as mapping out options for the Council and key dependencies.

4.55 Currently, both wind farms appear to be performing well. Following assessment, the Council will complete its best value assessment and then instruct appropriate parties to run a sales process.

4.56 Following this, a detailed options appraisal will be prepared, evaluating the offers received against the Council's reserve exit price and against holding the position longer-term.

Safe as Houses (SAH)

4.57 The Council has a loan to **Safe as Houses (SAH)**, a provider of care homes, assisted living accommodation and sheltered housing to local authorities. The Council's advisors have been in correspondence with SAH to gather information on the financial state of the business. A Non-Disclosure Agreement (NDA) has been agreed to gain further information.

4.58 The bond is due to be repaid at the end of 2023, so the aim is to ensure everything is in place and to also understand the redemption process.

4.59 For the remaining tail investments, preliminary analysis, and information gathering is underway. The goal is to undertake preliminary analysis in the next 2-3 months with full options analysis being completed by the end of the year. A process has been agreed for all positions, which will comprise the following:

- preliminary review: initial assessment, views on liquidity availability and options being explored. Interim updates will be provided, with positions worked through in an orderly fashion in order of materiality

- post initial assessment, officers will decide on priorities and areas of focus, and authorise work to be progressed on options. They will also identify any decisions and map out timelines, governance, and review requirements. Lastly, they will ascertain any impacts on divestment timelines and wider considerations, e.g., borrowings / MRP

- in advance of decisions, a detailed analysis will be prepared examining options; assessment of position value; contractual obligations / limitations; any early divestment options; and recommendations for next steps

- decision options will then be presented to members and the chosen options will then be implemented.

Procurement and Financial Costs/Budgets/Project Management and Financial Implications

4.60 The divestment strategy being pursued by the Council involves complex financial and legal issues and it has been vital that the Council is in receipt of high-quality and relevant financial and legal advice to support decision-making. The complexity of the investments and remediation work undertaken has been significant and is both a function of the size of the assets as well as deeper underlying issues that were uncovered, which required significant resources to remedy. For example, in the case of Toucan, legal uncertainties as well as the opacity of cashflows and the use of the Council's proceeds necessitated significant work on valuations, forensic investigations, tracing of assets, resolution of complex financial structures and deep dive due diligence. Similarly, in the case of JLG, the complexity of the loan book coupled with multiple creditors and poor management required significant analysis, restructuring of the company, resolution of identified security issues and implementation of controls.

4.61 In addition, the administration of Toucan and JLG/JCF means significant administrator and external advisor costs are being incurred in progressing these administrations to satisfactory completion.

4.62 The total advisor costs including the administrators' direct costs, administrators' advisor costs and the Council's own advisor costs as at July 2023 are estimated at £17.4m to date with forecast additional costs of £29.1m as set out in Table 2. These costs are under review and may change. Depending on the specifics of the investigations and legal actions undertaken by the Council and the administrators, these costs may be smaller or larger, though the Council will conduct cost-benefit analysis to understand all costs and limit extraneous costs.

4.63 As summarised in Table 2 below, the current estimated total costs of disposing of the Council's investment portfolio is currently estimated to be c. £46.5m. Regulation 23(h) of the Local Authorities (Capital Finance and Accounting)(England) Regulations 2003 permits the directly attributable costs of the disposal of General Fund assets to be met from capital receipts to a maximum of 4% of the capital receipt. The estimated maximum fees which could be offset against capital receipts would be circa £36m, which would mean that circa £10m would be chargeable to the General Fund. Funding of this will be finalised once the actual receipts in this financial year are known.

4.64 Since the commencement of the recovery programme work has been ongoing in various areas as advised by the Council's advisors:

- ➢ there have been cost savings to date vs original quotes and budgets, particularly on the Toucan administration, which is the largest part of the portfolio. Efforts to understand and manage costs are ongoing with all positions, as they move into recovery or divestment;

- ➢ the work noted in paragraphs 4.60 has resulted in an improvement in the recovery positions. For example, without the work undertaken on Toucan, the Council's losses at maturity of the position in a few years could have been much higher, while the recoveries on JLG might have been *de minimis*. In contrast, today the loss on Toucan has been reduced while recoveries on JLG are now £31.5m, both net of costs, representing a much better outcome for the Council, notwithstanding the absolute losses;

- the Council's advisors have undertaken cost measures on its largest exposure, Toucan, such as negotiating the administrators' fee rates down, negotiating down the base M&A advisor fee and capping it, and capping the debt advisory fees. These savings in total amount to £4.4m (excluding VAT) vs the original proposals for the Toucan administration and represent a direct cost avoidance to the Council;

- additionally, where possible, the Council has made available the work undertaken by its own advisors to the companies and administrators. This has prevented duplication of efforts, removed costs that might have otherwise been charged and critically, aided the efficiency of resolution and distribution;

- following the service of the Section 114 notice business cases were prepared to justify continuing expenditure.

4.65 Lastly, it is important to differentiate between the relative cost profiles of Toucan and JLG. The complexities of JLG are that there are multiple creditors with a multiplicity of vehicles that provided funding to the group, necessitating more complex negotiations and structuring; has severe gaps in security, systems and documentation that have needed to be rectified; makes SME loans and has a large portfolio of over 1500 loans with significant delinquency and default issues within the portfolio. The size of the portfolio and the need to have adequate monitoring as well as servicing in place means that the resources required to run the company, its embedded costs such as credit agencies, and to recover delinquent loans are significant.

4.66 Totals are shown in Table 2 below:

Table 2

		Cumulative spend £m	Forecast £m	Total £m
Toucan disposal				
Cost of Toucan Administration		13.4	11.3	24.7
Council advisors		1.2	1.7	2.9
Total	**A**	**14.6**	**13.0**	**27.6**
JLG disposal				
Cost of JLG Administration		0.0	11.8	11.8
Council advisors		2.3	3.4	5.7
Total	**B**	**2.3**	**15.2**	**17.5**
Remaining investments	**C**	**0.5**	**0.9**	**1.4**
Total forecast fees	**C= A+B+C**	**17.4**	**29.1**	**46.5**

4.67 The fees to date have recently increased by £5.7m, due to additional administration costs incurred on Toucan. In addition, the administrator of Toucan has indicated that following an analysis of the VAT position for the company, a greater overall economic benefit position has been calculated and notified to HMRC.

4.68 The forecast fees have increased (they were previously £24.2m - £27.7m). This is due to the Council now having received forecasts for the Toucan administration through to the end of 2024, compared with through to the end September 2023 only previously. In addition, the final costs are dependent on the legal options explored by the Council.

4.69 In order to ensure enhanced management of the programme council officers are undertaking a review of processes now in place which will cover:

- a recurring process to record and verify advisor fees. This is a developing piece of work and will be reported to Cabinet in future;

- the scope of advisor work will be kept under close review going forward, as there is potential for duplication, and will likewise be reported to Cabinet in future;

- budget monitoring is being enhanced utilising the recording noted above and regular checking, processing and reporting of these costs;

- cost challenging is being reviewed and also further developed for the future;

- project management of a programme of this size is absolutely essential and the Council, is beginning to develop this which includes ownership of the programme by the Council fully supported by advisors, forward planning, the use of action trackers to monitor and review progress, proactive determination and promotion of the Council's requirements, minuted progress meetings etc. Work on this has been developing and is now being further developed to become fully functional with a comprehensive audit trail supported by underlying records;

- as noted in paragraphs 4.11 to 4.15 best value decisions are essential and they are being reviewed in light of the hurdle rate now established along with the review of MRP.

Potential Litigation

4.70 The Council is very mindful of the responsibilities of those outside of the Council for the situation the Council finds itself in and proactive work is being instigated in respect of individuals and organisations who may not have met the standards expected of them.

4.71 Fuller details are shown in Appendix B.

4.72 Where opportunities present themselves to make additional recoveries through litigation all necessary action will be taken subject to securing the necessary legal advice on the merits of a potential claim and the undertaking of a cost benefit analysis.

Financial Management

Capital Receipts

4.73 As part of the improvement and recovery plan there is a strategy to dispose of £150m of Real Estate Assets to provide capital receipts over a 5-year period to assist to reduce debt. This is under review and will be updated in subsequent reports.

4.74 This strategy was set out initially in a Commissioners and Directors Board Report of 22/11/2022 and has subsequently been implemented. The proposed approach to disposals was also noted as part of the Treasury Management Strategy approved in March 2023.

4.75 This strategy involved setting up a dedicated interim team of surveyors and lawyers in February 2023 to focus exclusively on this, and to engage commercial agents, auctioneers, and property consultants as appropriate to market and sell the properties. The report estimated in addition to the interim resource, a range of 3% -5% of the proceeds should be assumed for legal, agents, and valuation fees, being external support through frameworks.

4.76 The Asset Disposals Team was set up in February and March 2023 and continues the ongoing work, of reviewing and appraising properties within the team, and consulting the legal team, other service areas, and commercial agents. This includes both legal and property due diligence that is essential for effective disposals.

4.77 The initial target of £30m of capital receipts for 2023/24 has been increased to £42m following work by the Asset Disposals Team.

4.78 The separate Asset Disposals Paper elsewhere on this agenda sets out a tranche of properties for disposal for approval in Cabinet of 13th September, this totals c. £23 million of additional forecast receipts giving a current potential 2023/24 total of £53 million (see below), which allows a buffer for delayed real estate transactions whilst still meeting the £42m target.

4.79 This includes 15 properties with prior Cabinet disposal approvals that are currently in the hands of agents with estimated anticipated sale receipts of around £30 million in the current financial year. There are offers and negotiations in hand on around £9.5 million of these at present. Exchange of contracts is expected in September on these transactions with completions in October.

4.80 The team has commenced due diligence on the next tranche of properties for November Cabinet approval. The focus again is on properties that can be quickly sold on a straightforward basis for good capital receipts.

4.81 The Avison Young (AY) Market Review of 250 properties was received in two phases in June and July 2023. This provides independent advice on forecast sales receipts for the properties and underpins the targets for 2023/24 both in terms of the likely capital receipts to be generated and deliverability.

4.82 The AY Report will inform a more accurate overall figure of the possible magnitude over 2024/25 and for the subsequent three financial years. The Asset Disposals Team is now conducting essential work analysing this to provide an up-to-date detailed programme of capital receipts forecasts for the future financial years and we will report further on this in October 2023.

4.83 In order to continue to deliver the agreed programme effectively it will become necessary to appoint a single firm of commercial agents and a firm of auctioneers to handle all future disposals (in addition to the agents working on current disposals) so they can do work immediately on due diligence and preparation of marketing materials ahead of specific property disposal approvals.

4.84 This is essential, in order to allow the process of marketing, property negotiations through to completed sales to proceed at pace, to achieve forecasts for both the remainder of the current financial year and for the first two quarters of 24/25

Capital Programme

4.85 The capital programme which will be set out in the Capital Strategy forms a key part of the Council's budget setting process.

4.86 The aim for the **capital strategy** is to meet the requirements of the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code which requires local authorities to produce a Capital Strategy to demonstrate how capital expenditure, capital financing and treasury management activity contribute to the provision of planned outcomes and take account of stewardship, value for money, prudence, sustainability and affordability.

4.87 This Capital Strategy 2023/24 – 2027/28 will form part of the framework for financial planning and is integral to the Medium-Term Financial Strategy (MTFS) and the Treasury Management Strategy. It will set out how capital investment will play its part in delivering the long term strategic objectives of the Council, how associated risk is managed and the implications for future financial sustainability.

4.88 All capital expenditure and capital investment decisions will be covered by this strategy, not only as an individual local authority, but also those entered into by the authority under group arrangements. It will be refreshed annually in line with the MTFS to ensure it remains fit for purpose and enables the Council to make the investments necessary to deliver its strategic aims and objectives.

4.89 The process will be the development of a capital strategy that is compiled using some key principles, including meeting statutory requirements, such as health and safety. Significantly the capital investments will be focussed on essential outcomes for citizens and absolutely minimal new expenditure.

4.90 Rigorous review is being undertaken and involves the relevant Directors, project leads and finance to focus on essential outcomes and borrowing for refinancing where essential.

4.91 The benefits will be a Capital Strategy that delivers a financially sustainable position over the medium and long-term that delivers essential outcomes and outputs for citizens.

4.92 The aim for the **capital programme** is to provide Members with an updated capital programme for 2024- 2029, detailing forecast resources for that period.

4.93 The capital programme is a key element of the budget papers and must comply with the requirements of the Capital and Treasury Management Strategies. Capital expenditure is defined in legislation and is expenditure that is incurred on buying, constructing or improving physical assets such as land, buildings, infrastructure and equipment.

4.94 This update of the capital programme will be prepared in the context of the overall resources available to the Council. This capital programme will therefore set in line with the level of resources as set out in the Medium-Term Financial Strategy.

4.95 In preparing the capital programme, ongoing reviews of the projects as well as phasing of expenditure on existing capital schemes are being undertaken together with an updated projection of capital resources. The focus of the capital programme has been on undertaking mandatory duties keeping the public safe.

4.96 Where appropriate, scheme estimates have been revised and projects removed.

4.97 Previous year’s capital programmes have been ambitious involving several major projects in any one year and were heavily dependent on borrowing. There has been insufficient capacity and capability to deliver major capital schemes which have resulted in very significant overspends, for example as reported on the A13.

4.98 The cost of servicing prudential borrowing is a major pressure on the Council’s revenue budget.

4.99 The capital programme is thus being reviewed to:

- reduce capital expenditure to focus on contractual commitments and health and safety requirements in line with the s.114 Notice – this will reduce the capital programme;

- extend the capital programme from three years to a five year forward look in line with best practice.

4.100 As with the strategy, the process will be a rigorous review of the existing capital programme, collaborating with Directors and relevant project leads, reviewing all expenditure, funding, and borrowing and focussing on mandatory duties given the financial context within which we are operating.

4.101 It is essential that borrowing costs are significantly reduced supporting the council’s overarching aim to live within its means.

4.102 The benefits will be a Capital Programme that supports the Capital Strategy to deliver a financially sustainable position over the medium and long term that secures essential outcomes and outputs for citizens.

Revenue Budget

4.103 The Council’s 2023/24 revenue budget process was completed in a very shortened timescale and proposed savings of £8.3m.

4.104 Part of the work in this financial year has been to review the proposals to ensure that there is evidence to support the original proposals – this has now largely been completed.

4.105 For 2024/25 the budget process has been revised within regular timescales to improve the process and will now include:

- a target of £18.2m of savings in 2023/24
- each proposal having an EQIA, business case and action plan to support it.
- EQIAs that will be published.
- an improved timeline that is planning:

    - Savings being worked up in full by 30/9/23;
    - Scrutiny meetings in October/November 2023;
    - Cabinet in December 2023 to agree the proposed savings;
    - any slippage in the above being accommodated early in the New Year.

4.106 The above will be followed by the normal round of budget papers. This will allow earlier scrutiny of proposals that have been fully developed and assessed within a regular timeline.

4.107 Within the Council the Change Team is leading on bringing together all the £18.2m of savings working closely with Directorates while PWC have been engaged to do likewise bringing their wider experience to ensure savings can be generated.

4.108 In order to further develop the revenue budget process the following improvements in practise are also being undertaken:

Salary workings

4.109 Centralised staffing template has been developed and shared. Confirmation of the establishment and reconciliation to the general ledger was completed on the 31st of July 2023.

4.110 This allowed the overall calculation for pay award and increments to take place in early August which will support the growth requirement figure in the MTFS. The file will also allow for modelling of different pay policy options.

Service Reviews

4.111 These are targeted reviews of services areas which have historic/current budget pressures and growth requirements in the MTFS. They will provide standardised documents to sit behind the growth allocations in the MTFS, for example, inflation & demographic growth assumptions in Children's Social Care, changes to the Waste strategy, proposed staffing restructures in the central core. The documents will set out the key issues, actions that can be taken within the service to mitigate and any formal growth requirements. These are taking place alongside in-year budget monitoring and intended to be completed by 31st August with review and potential MTFS adjustments taking place early in September.

Income Review

4.112 A central template has been produced to show all income lines at a code combination level and allow for detailed analysis to take place. All income will be categorised and identify the source of the income, corresponding expenditure, availably of volume/performance data etc. This exercise will allow for re-alignment of targets to match activity, correct classification of income and will support the fees and charges process in assessing potential additional income opportunities. This exercise has not been conducted at this detailed level before, the final document will allow finance and the relevant service areas to gain a greater understanding of the revenue streams the council currently has. Income is often looked at in isolation without consideration to associated costs which this exercise intends to rectify.

4.113 The income review is intended to be completed by 30th September but is likely to continue throughout October and will link closely in with the Fees and Charges work previously reported to Cabinet.

Review of Contracts

4.114 The current contract register is being assessed to determine the value of contracts due to end in the current financial year and 2024/25 to be able to model the potential inflation uplift requirements which will need to be reflected in the MTFS. Contract inflation as historically been absorbed within operational budgets but with increased inflation and tighter budgets this is unlikely to be achievable.

4.115 This will be completed at a high level by 31st August but will require further support from contract managers and service leads to understand specific plans in some key areas and which contracts have the potential to be consolidated etc.

Dedicated Schools Grant

4.116 Thurrock with a DSG deficit of £0.534m, is part of the Delivering Better Value in SEND programme that aims to support LAs to improve delivery of SEND services for children and young people while ensuring services are sustainable. The programme will provide dedicated support and funding to 55 local authorities.

4.117 Thurrock is part of Wave 3 and started engagement and data exchange with the team from Newton and CIPFA in June. Pupil level data and costs have been returned. Analysis and discussions have started to ensure accuracy and understanding of information.

4.118 A fundamental characteristic of the DBV diagnostic approach is the whole system engagement with partners and stakeholders. This includes the Schools Forum; Children and young people; Parent Carer Forums and wider parent carers; Education colleagues (Headteachers, Setting Leads, SENCO's, teachers, and governors) and Health and Social Care partners.

4.119 Workshops are to be held in September and October with partners and stakeholders. This will include seeking views on the current system and inclusive practice, what works well or less well at present, and which areas for improvement would make the greatest difference.

4.120 Officers from the Local Authority will attend two separate residential sessions to discuss current practice and outcomes with other Local Authorities. These are to be held in August and October.

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4.121 The emerging insights from DBV in SEND Tranche 1 programme is to provide better support and outcomes for children and young people with SEND. The greatest opportunity exists in increasing the ability of local systems to support children in a mainstream setting.

4.122 The expected outcome from the programme will be a grant application to the Department for Education, backed up with data, which will allow investment to improve outcomes for young people through invest to save initiatives.

HRA

4.123 Whilst the HRA is ringfenced, a similar approach has been taken with a rigorous review being undertaken involves the relevant Directors, project leads and finance to focus on essential outcomes and meeting statutory requirements and minimising borrowing wherever possible.

4.124 It is essential that capital expenditure is focussed upon keeping our citizens safe by ensuring that all regulations are met including fire safety. There are a number of properties in the Borough that currently need improvements to meet these regulations. This will involve some capital projects being refocussed to include essential spend removing the aspirational discretionary spend currently within those projects.

4.125 The review includes analysis of contractual commitments currently in the programme that the Council will need to honour.

4.126 A 30 year business plan will be developed over the next 3 months that will ensure that the HRA remains financially sustainable, this review will deliver an improved financial position based upon delivering statutory duties as the baseline for the development of the business plan.

4.127 The updated HRA Capital Programme will be reported to Members alongside the General Fund Capital Programme and the Medium-Term Financial Strategy in accordance with the budget timetable.

Treasury Management

4.128 A detailed treasury management model has been established to ensure that the charges to revenue for capital and debt, which comply with all relevant regulations, are correctly reflected. This can be updated on a regular basis as circumstances change and can also be used to model various scenarios should this be necessary. As well as being updated for economic changes (revised interest rates etc.), any changes to specific elements (e.g., unfunded capital expenditure, timing, and value of asset disposals etc.) can be included and reflected in the capital costs and debt levels for the Council going forwards. This remains a significant cost area for the Council and therefore accurate inclusion of these in the wider budget process is vital.

MRP

4.129 Minimum Revenue Provision (MRP) is a legal requirement, specific to local authorities, which arises where General Fund capital expenditure has not been funded from either capital receipts, government grants, developer contributions or revenue budgets. This is sometimes referred to as "unfinanced" capital expenditure.

4.130 Regulation 27 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 requires that in these circumstances an annual amount is charged against General Fund balances, effectively representing future repayments of assumed new borrowing. The overall objective of MRP is to ensure that local authorities charge to the revenue account "a prudent amount" which recognises the cost of acquiring such assets, over a period commensurate with the benefit provided by the asset which has been obtained.

4.131 A review of the Council's current approach to setting and calculating MRP is underway. This will report and set out its findings and, if appropriate, make recommendations.

Finance Structure and Service Development

4.132 A fundamental part of a financially sustainable Council is a finance service of the highest quality. To assist with the development of the current team it is planned to undertake and develop:

- a review of the finance structure
- an assessment of capacity and skills needs and development
- productivity plans
- process efficiencies
- refocussing of resources
- succession planning
- communications
- training and development
- trainee accountants
- continuous improvement
- cultural changes

4.133 This is planned to conclude by December 2023 with any external appointments being in place by 31 March 2024 subject to a successful recruitment process.

Risk Management

4.134 The Risk and Opportunity Management Strategy, Policy & Framework (ROM S, P&F) has been strengthened and drafted to address the recommendations in the BVI report. The draft is being considered by SLT in August for consultation/feedback and then onward reported to Standards and Audit Committee. The feedback from this committee will then be reported to SLT and the ROM S, P&F further refined as appropriate and the final draft presented to December Cabinet for approval.

4.135 Work has been undertaken with consultants (Zurich Management Services) to develop a ROM workshop for SLT in August 2023. The workshop is to go through some key elements of ROM, consider/set risk appetite and undertake a facilitated session to identify the key strategic items that need to be considered for the refresh of the strategic/corporate risk and opportunity register. A further workshop is planned for early September to be undertaken with Senior Leads (Directors, ADs and Service Managers) to identify any additional items that need to be considered for inclusion in the register (e.g. strategic, corporate/cross cutting or project, partnership items). The outcome of these workshops will then be reported to Members.

Compliance

4.136 A review of the Council's financial regulations is underway and almost complete

Revenues and Benefits

4.137 Exploratory work is underway to examine areas that can be further developed/improved. At this exploration stage these include:

Billing

- Review of remaining discretionary discounts/exemptions – underway;
- Consider business case to introduce Direct Debit for Sundry debt – underway;
- Consider business case to introduce of E billing for Sundry Debt and Business Rates – underway for Sundry debt;
- Use of RPA and workflow to enter Sundry invoice requests to remove duplication of work and risk of error – underway;
- Introduce Direct Debit functionality for Sundry Invoices – underway;

Benefits

- Review of Local Council Tax scheme – underway;
- Expansion of cheaper contact channels for outgoing benefits correspondence – linked to progression of the corporate INS solution

Debt

- Further phases of Single View of Debtor (SVOD) - subject to business case and current xantura review;Introduction of generic recovery stages – linked to SVOD;
- Expansion of multi contact channels – underway but also linked to SVOD;

Accounts Payable

- Use of existing Oracle scanning functionality for Accounts Payable – underway;
- Review to identify duplicate payments – initiative commenced.

Accounts

4.138 As Members will be aware, the audit of the 2020/21 Statement of Accounts is still ongoing. The Accounts will require a substantial re-write to reflect the following issues:

- reduction in the value of infrastructure assets in line with CIPFA's Code Update; This is a sector wide issue.
- restatement of accounting for IT projects some of which have been classified as intangible assets and need to be restated to revenue. This is largely related to cloud-based services.
- restatement of assets previously classified as heritage assets, but which operational assets and revaluation of the remaining assets to cost;
- restatement of investment values arising from the impairment of a number of the Council's investments, principally the solar farms
- restatement of MRP charges arising from the MRP review referred to at para 4.142 above and reflecting the revised approach to MRP in respect of capital investments.
- restatement to reflect the provisional Capitalisation Direction notified to the Council by DLUHC.

4.139 To assist with the above and bring the Council up to speed with the closure of accounts for the years 2019/20 to 2022/23, the Council has made progress in the following areas:

i. **Resources** – The Finance team has onboarded additional interim support with experience of dealing with similar issues at other local authorities, to provide additional capacity to support both the range and complexity of the work arising from the audit overrun and various issues identified;

ii. **Working papers** – A standard suite folders will be introduced for all financial years. Finance staff will then use the standardised working paper templates linked back to the Code for all disclosures to ensure that the accounts comply with the CIPFA Code of Practice;

iii. **Quality Assurance** - The working paper templates will also include a three-stage quality assurance process covering 1) preparation, 2) technical review and 3) sign off review. This is essential for ensuring a right first time approach to accounts preparation and to ensure a smooth audit;

iv. **Accounts plan** – A comprehensive accounts plan linked to the auditors required by client schedule will be developed. This will be communicated to all key stakeholders and includes a responsible officer for each task and separate deadlines for preparation and review;

v. **Whole team approach** – A key element of faster closedown is ensuring that all staff within the Finance Department are engaged on accounts closedown. This reduces the risk of bottlenecks arising from reliance on one or two officers to produce the accounts, and provides resilience in the Finance function;

vi. **Review of accounts** – the Statement of Accounts will be reviewed to simplify and strip out unnecessary disclosures, and ensure that the remaining disclosures meet Code requirements.

Other Financial Management Improvements

4.140 Several financial management improvements have been referenced above, others are being developed and include but are not restricted to a review and improvements to:

- the Council’s financial modelling
- the financial implications in reports
- business partnering
- internal audit
- MRP calculations

<u>Forecast Financial Position of the Council</u>

4.141 The current overall forecast position despite those positive financial implications from the various above actions is that the Council remains financially unsustainable in terms of:

- a level of debt at circa £680m
- the cost of financing this debt at 30% of the budget, considerably more than what could be considered reasonable for a sustainable council.
- a revenue budget that is not in balance by 2028/29 - out of balance by £16m - which means the continued need for exceptional financial support and thereafter potentially increasing deficit.

4.142 This position is under review and will undoubtedly change.

5. **RISKS**

5.1 The key risks are:

- **Crystalised losses on Toucan, JLG / JCF, and PWE investments:** These investments are currently being divested or have recently undergone restructuring to resolve identified issues and recover value. The current analysis shows that the Council's investment will be impaired here (outside of legal recoveries), but the extent of impairment could be worse if market conditions worsen, e.g., if interest rates rise.

- **Borrowings:** The Council's refinancing strategy continues to replace maturing inter-LA loans with PWLB loans. There is a risk as new loans are taken out; the cost of borrowing will grow. A number of the investments are now loss making once the higher cost of borrowing is factored in. In addition, any delays that occur in divestment and associated decision-making will lead to added borrowing costs being incurred, making it critical to manage divestments efficiently. The Council will also be left with some investment associated borrowings at the end of the period, due to the impairments incurred.

- **Illiquid Investments**: Most investments are illiquid by virtue, as they are in private markets. Thurrock has already implemented divestment plans on 75% of its portfolio, with a further 10% to be confirmed shortly. For the remainder, analysis is underway, but the investment terms indicate that for a significant portion, the Council will be locked into these investments until the maturity date (with the latest anticipated maturity date being c. 2032). Therefore, it will be important to negotiate and plan out divestment strategies carefully to access liquidity earlier and recover proceeds sooner where feasible.

- **Inflation and rates:** Inflation has risen significantly and remains elevated, accompanied also by rising interest rates. This has far reaching impacts on the performance of the investments and companies the Council have invested in, as well as on asset valuations, in particular for Toucan, where revenues are linked to inflation but where rising interest rates also increase the discount rate for future cashflows. The portfolio has some protection through index-linked investments, notably the solar and wind investments. The real estate exposure (CCLA) is also a partial mitigant, through the index-linkage is typically capped here and will not fully mitigate current inflation. Alongside, the Bank of England has raised rates aggressively in recent months, which has also raised borrowing costs for the Council.

- **UK Economic Downturn:** An economic downturn could impact investment counterparties and therefore, impact divestment timelines and recoveries. The

Council has significant exposure to many aspects of the UK economy: property, small businesses, energy, etc. Therefore, a downturn and potential recession as growth slows would negatively impact their portfolio. We note there is a growing risk that the UK may enter a recession, which will increase the risk for several positions.

- **Accounts** - inherent risk of further liabilities/revenue costs arising as the audit, accounts preparation and restatement work is in progress.

5.2 In common with other elements of the divestments workstream, many of the risks highlighted above are outside of the Council's contract and there is no way to easily mitigate these risks. Having said that, there are some mitigants being explored:

- the Council is looking to proactively manage its divestments and realise value sooner (instead of taking the risk of further issues down the line or lower proceeds at maturity), as with Toucan and JLG.

- it has implemented cost and governance frameworks within the administrations to allow costs to be managed. This has resulted in significant savings to date. It has also used its own analysis to date to replace at lower cost work that the administrators would have otherwise undertaken and to aid the efficiency of asset disposals and distributions to the Council.

- lastly, scenario analysis is being undertaken on the portfolio to understand the impact of different events and the knock-on potential impact on impairment.

6. Reasons for Recommendations

6.1 The Council's financial position is well known and extremely challenging.

6.2 The various financial workstreams are addressing this situation and the recommendations will allow for this work to continue and for Members to be fully informed.

7. Consultation (including Overview and Scrutiny, if applicable)

7.1 Consultation has taken place with the Commissioners.

8. Impact on corporate policies, priorities, performance, and community

8.1 The successful conclusion of this work will allow other corporate policies to be undertaken in a sustained manner.

9. Implications

9.1	**Financial**	As set out throughout the report.
9.2	**Legal**	**Mark Bowen** **Interim Project Lead - Legal**

The key legal implications are set out in the body of the report.

9.3 **Diversity and Equality** **Rebecca Lee**

Team Manager, Community Development Team

While there are no specific diversity and equality implications associated with this update report, council is committed to completing Community and Equality Impact Assessments (CEIA) for proposals involving savings.

9.4 **Other implications** (where significant) – i.e., Staff, Health Inequalities, Sustainability, Crime and Disorder, and Impact on Looked After Children.

Detailed impacts will be reported through specific reports.

10. **Background papers used in preparing the report**

Various working papers

11. **Appendices to the report**

Appendix A - Recommendations from the Secretary of State

Appendix A

Recommendations from the Secretary of State

To deliver financial sustainability by closing any short- or long-term budget gaps and reducing the Authority's exceptionally high level of external borrowing.

To ensure compliance with all relevant rules and guidelines relating to the financial management of the Authority.

To ensure that a strategic and systematic approach to risk management, with appropriate scrutiny and governance of the decision-making processes and procedures, is adopted and embedded across the Authority.

To address the culture of poor financial management and governance of its commercial portfolio.

To prepare and agree an Improvement Plan to the satisfaction of the Commissioner (which may include or draw upon improvement or action plans prepared before the date of these Directions), within 3 months, with resource allocated accordingly, to include at a minimum:

a. An action plan to achieve financial sustainability and to close any short and long-term budget gaps identified by the Authority across the period of its medium-term financial strategy (MTFS), including a robust multi-year savings plan.

b. An action plan to ensure the Authority's capital, investment and treasury management strategies are sustainable and affordable.

c. A strict debt reduction plan, and an updated minimum revenue provision (MRP) policy in line with all relevant rules and guidelines.

d. An action plan to ensure the Authority is complying with all relevant rules and guidelines relating to the financial management of the Authority; and

e. A suitable scheme of delegations for financial decision-making.