Commercial Strategy Rationale

1 Introduction

- 1.1 The development of a commercial approach for the council is part of our wider response to how council services are funded. Over the period 2019/20 to 2021/22 years we need to save £14.5m. We need to consider how we approach being commercial in order to be able to achieve our corporate priority of future financial sustainability for the council.
- 1.2 The financial challenge faced by the council since 2011 has been described as the single biggest risk to sustainable public services on the Island. Accordingly, the council needs to maximise the deployment of resources that it does have (revenue, capital, property and staff) towards driving additional income/funding and cost savings to secure council services for the future.
- 1.3 The commercial strategy sets out the approach we intend to take, and they are not simply words on a page. In many ways we are already starting to deliver. There is no fixed view on how services should be delivered as we want to tap into the talents and skills in our workforce and through our partners and contractors and with our community.
- 1.4 The commercial strategy will frame how the council does business, from delivering services in an efficient way, through income generation opportunities to understanding how services could be traded; the aim of which will be to secure funding for maintaining essential services for residents.

2 Context and Drivers

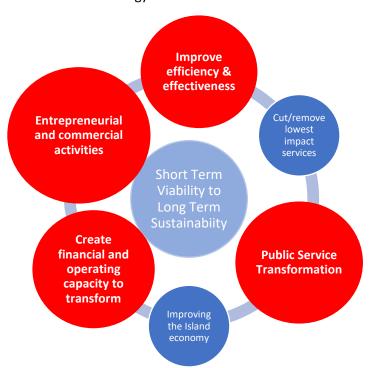
2.1 Reduced public sector funding and increasing demand for services, driven by demographics and long standing social, health and economic pressures mean that the council, like many other authorities across the UK continues to face significant challenges in providing the services local people need and want within available resources. The council's financial position remains its most serious challenge¹; its net controllable expenditure in 2019/20 is £150million. Having already saved in excess of £76million over the eight years from 2011/2012, it must save a further £13.5million over the period 2019/20 to 2021/22.

2.2 Key drivers include:

- Service Pressures
 - Rising population and demographic pressures
 - Increasing demand for services
 - Estimated additional costs of between £6m and £7m per annum
- Reducing Resources
 - Significant savings made (£76m) but an additional £14.5m to find
 - A reduction in net spend per capita
 - Uncertainty about future funding
- External Factors
 - Shrinking public sector at a time of greater reliance and need for the integration of services
 - Advances in technology and changing expectations
 - Rising costs
 - Island factor (the unique costs of providing services on an Island)

¹ Isle of Wight Council, Corporate Plan 2019-2022

- Ambition and Aspiration
 - Desire to transform the way we work
 - A shift from a paternalistic approach to service delivery
 - Ensuring fair cost of services for residents
 - Vision to be an inspirational place to grow up, live, work and visit.
- 2.3 The council has taken robust actions in the development of a new medium-term financial strategy² (MTFS), which has improved the overall resilience of the council and responded to the financial challenge by:
 - Smoothing out savings requirements to avoid "front loading" and buy time
 - Rebuilding reserves and balances to improve our resilience
 - Providing funding to pump prime "invest to save" initiatives
 - Maximising capital resources that can stimulate economic regeneration, jobs and housing
 - Targeting other resources to regeneration and transformational change
 - Embedding a financial framework that promotes longer term planning, encourages more responsible spending, improves decision making and aligns financial accountability and discipline.
- 2.4 The MTFP sets a strategy which identifies short term viability activities which will lead to longer term sustainability for the council, set out within six broad themes and four of these themes set the framework for the commercial strategy.



- 2.5 From a financial perspective the commercial strategy will form part of the MTFS holistic approach to the financial challenge facing the council.
- 2.6 Under each MTFS theme there are a series of broad activities identified and the diagram below sets out those activities as they could relate to and inform the development of the

² Full Council, 19 October 2016 Medium Term Financial Strategy 2016/17 – 2020/21

commercial strategy.

Creating Financial and operating capacity to transform

- Create a £1m Transformation Reserve to fund "spend to save" schemes
- Review existing capital programme and re-prioritise towards invest to save

Increasing efficiency and effectiveness

- Review of cost and income opportunities
- Capital investment targeted towards revenue savings
- Capital investment targeted towards avoiding future costs
- Smart and lean evidenced based commissioning providing for actual need rather than perceived need or want.
- Review of fees and charges to ensure alignment with policy objectives and affordability

Entrepreneurial, Commercial and Collaborative activities (with managed risk)

 £100m commercial property acquisition fund with a portfolio of assets of different size, across sectors and geographies with strong covenants and in strategic growth locations

Public Service Transformation

- Pursue One Public Estate/One Publis Service initiative.
- Use tehnology and digital solutions.

- 2.7 Some of the activity outlined in the table above has been undertaken in advance of the council having a full commercial strategy, the most obvious being property investment.
- 2.8 Alongside the capital financing requirement (CFR) for the existing Highways PFI and Waste contracts the council has a Commercial Property Acquisition Fund which is funded through borrowing. The strategy for borrowing is set out in the MTFS, the council's Treasury management Strategy Statement³ and its Property Investment Strategy⁴, all of which have been approved by council, but clearly form an element of a wider commercial strategy for the council.
- 2.9 The intent of the programme of commercial acquisition is to exploit commercial opportunities and secure a pipeline of income, through use of the council's borrowing capabilities, that will contribute to the council's future financial sustainability. It is important to note that the council's approach to commercial property acquisition is separate from the recently approved regeneration strategy and its asset management strategy.
- 2.10 Income generation is a key mechanism they council can use to reduce the need to cut services. The council does have a history of taking this approach with some services that it currently operates (leisure services; car parking; property acquisition). There are areas however where the council may be able to extend, intensify and strengthen its income generation activities and these will be considered when implementing the commercial strategy.

3 Scrutiny Task and Finish Group and Staff Engagement

- 3.1 In February of 2019 Scrutiny Committee received a report from its Task and Finish Group ⁵ on commercialisation and a follow up report in June 2019. The report included several conclusions which it considered should underpin the IW Council Commercial Strategy, including:
 - Political drive, leadership and a culture of commercial thinking.

³ IW Council <u>Treasury Management Strategy Statement 2019-2020</u>

⁴ IW Council <u>Property Investment Strategy, September 2017</u>

⁵ IW Council Scrutiny Committee – Reap the Harvest – Profit with Social Value, Feb 2019

- An understanding of how council's commercial activity differs from service delivery.
- The need for a commercial strategy.
- The need to build commercial understanding and skills throughout the organisation.
- The need to understand how commercial activity links with social value.
- Commercial activity needs to be based on robust business plans and business planning.
- Consideration should be giving to setting up a trading company(ies), identifying current
 activity that would benefit from being part of traded activity.
- Investment in ICT is needed to support commercial activity.
- 3.2 The issues highlighted by the task and finish group are also reflected in responses and feedback that the council has received through various staff engagement activities. There have been several opportunities for staff to feedback their views on current and potential commercial activity, commencing with the Chief Executive's BIG Conference in November 2018 and including conversations with managers staff groups from across the council as well as staff survey questions.
- 3.3 In response to the question "What do you think we mean when we say commercial?", the response provided clear feedback linked to being more business-like and generating income for the council.



3.4 When asked "How commercial are you now?", the response was more varied response with feedback ranging from not at all, through having constraints to commercial activity to being reasonably commercially minded. Issues with capacity, skills and the need for support to change were evident throughout the responses given.



3.5 Finally we asked, "How could you be more commercial in the future?". Feedback was less about ideas for being commercial and more about the support and skills that individuals and the organisation needed to develop to be more commercial; identifying that there is work to be done to develop the culture of innovation, enabling and empowerment that accompanies commercial activity.



- 3.6 The council currently has a mixed model of provision with services provided in-house and externally through a range of stakeholders including voluntary and community services and commercial organisations.
- 3.7 Exploring ways to enable the delivery of better services for less, working collaboratively with partner agencies, communities and staff and doing more with local people rather than to them will

be critical to the council achieving its corporate plan ambitions and addressing the challenges that lie ahead and this approach has informed the approach set out in the commercial strategy.

- 3.8 Equally, building confidence and capacity and encouraging people to help themselves and be less dependent on public services will be a key thrust in plans moving forward. Streamlining systems and procedures will play a key part in this.
- 3.9 Finally, as identified by the task and finish group and through staff engagement, our staff will need to share the vision and have the skills to support the council in delivering its commercial strategy.
- 3.10 We do have a rich source of assets, attributes and roles that as a council we can use to derive commercial value:

Place shaping role	Using our planning, economic growth, education and skills
Trace shaping role	development roles to shape and create the market for growth and
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C: 55	enterprise.
Staff	Using and developing the knowledge and skills of our workforce to
	create culture of empowerment, innovation and involvement in
	commercial activity
Infrastructure	Using and developing digital and ICT and highway assets for
	commercial gain.
Land and buildings	Using our land and buildings to promote and deliver housing and
	economic growth; co-locate with partner public sector agencies
	and generate capital receipts and reduce costs.
Partnerships	Using and selecting the most appropriate private, public and third
	sector partner to deliver schemes and projects that derive
	maximum level of income for the council and value for customers,
	residents and communities.
Business Intelligence	Using our business and service data more intelligently to create
_	new commercial opportunities and better service delivery models
	which will generate new income for the council.
Customer intelligence	Using the information and contacts we have to help design and
-	develop new commercial activities.
Brand and web presence	Use the value of our web presence, search engine optimisation
	and brand value to promote our trading and commercial activities
	and those which we can partner with others.
Liquid Assets	Access to borrowing to enable investment.

4 Commercial Decision Making, Procurement and Risk

- 4.1 The expectation that commercial decisions and investment opportunities are informed by sound financial decisions as set out within the councils MTFS and its Property Investment Strategy. Equally, to ensure that the council makes decisions around traded activity which are properly informed a corporate approach to the business model is needed and good practice provides that this should include the following:
 - Strategic fit fit with the council's objectives and values (including social value and environmental objectives);
 - Legal ensure that proposals are lawful;
 - Financial consideration of cash flow and understanding of cost and financial benefit;

- Commercial market knowledge of customers and competitors;
- Operational and technical staff and other resources requirements and how they can be met; and
- Risk assessment and management plans.
- 4.2 Income generation activity should be designed to both increase income to the council as well as increase funding from council tax, business rates and government grants.
- 4.3 Procurement has a role to play in transforming service delivery, providing a route to encouraging innovation, as well as ensuring value for money and making a positive impact on local businesses and jobs.
- 4.4 The council has a procurement strategy, the purpose of which is to set the overall context for the council's procurement and contract management activity. It provides a framework to support all areas of the council in adopting a consistent, comprehensive and robust approach to spend with third parties. Those who are involved in carrying out procurements and/or managing contracts or commissioning for the council need to have the right commercial skills to enable them to do so in order that the council can maximise commercial opportunities.
- 4.5 When commissioning or procuring the council should respond to the Public Services (Social Value) Act 2012 which requires all service contracts to be subject to appropriate social value criteria and this can range from community benefits such as targeted recruitment or training initiatives or supplier engagement with schools and colleges through to vocational training opportunities or voluntary initiatives. Equally procurement decisions should aim to minimise harm to the environment and to promote conservation of natural resources.
- The council has in place both strategic and service level risk registers and these are regularly reviewed, but in the main are primarily used to reduce exposure rather than improve risk management. We have well defined fiduciary duties that effectively disallow recklessness, but this does not preclude taking commercial risks. In making commercial decisions the council must properly consider and put in place proportionate measures to manage risks.
- 4.7 This means that officers involved in commercial or traded activity will need a clear understanding of the corporate approach to risk and commercial failure. Commercial trading is inherently risky, and it is inevitable that some initiatives will fail (just as they do in the private sector). In undertaking commercial activity, the council will need to ensure that the risks taken are proportionate and demonstrably reasonable. Equally the council needs to ensure that in implementing its commercial strategy, seeing commercial failure as unacceptable is likely to stifle taking risks that may be necessary for the council to succeed in a competitive market.
- 4.8 The business case model set out in the draft commercial strategy should ensure that risks are understood and identified early and that all risks (financial, legal, commercial, operational etc.) identified indicate likelihood, impact and overall severity and be accompanied by preventative and mitigation measure to be taken.

4.9 The following table provides further information in relation to risks associated with the commercial/traded business case approach.

Business case element	Generic Risk	Comment
Strategic	Trading activity not consistent with political ethos of the council.	Business cases should actively demonstrate how a proposed initiative will contribute to corporate priorities and strategies. Where no such contribution is identifiable there is no case for proceeding.
	Trading activity results in backlash from private competitors. Negative press or public feedback.	It is the nature of competition that there are winners and losers. It is however important to be able to demonstrate that the council is not operating unfairly and that any adverse impact on local business is fully understood and acceptable before trading commences.
		Where risks of negative public perception are identified these can be mitigated through an effective communication strategy to ensure there is wide-spread understanding of the benefits that will flow from the trading initiative.
	Trading failure results in reputational damage	Careful consideration of the risk/reward ratio and a robust balanced business case are required.
		Clear communication strategy and well thought through risk mitigation strategy essential for high profile initiatives.
Legal	Trading activity deemed unlawful. Challenge from competitors.	Most trading activity is low risk in this respect but where there is doubt it is essential to ensure that appropriate advice is taken.
		Councils should always act reasonably and demonstrate that they have taken account of the impact of any trading activity on local businesses etc.
		When trading through a separate corporate identity advice should be taken on procurement and state aid implications.
Commercial	Demand failure Supply failure	Understanding of the market is a crucial element of a robust business case. Deep knowledge of the customer is a prerequisite of any successful trading company.
Financial	Trading fails to generate a profit. Trading failure leads to loss of sunk expenditure.	The business case should set out profit and loss projections on a basis that is acceptable to the council's finance team. Trading should not continue where it is unable to operate on a financially sustainable basis.

		Risks such as non-payment should be assessed and mitigated.
		Clarity over the extent of sunk cost exposure should be included.
		Spreading financial risk across a range of different initiatives will help to off-set the impact of potential failures.
Operational	Inability to provide service because of staff shortage or lack of suitable equipment. Diversion of resources impacts on delivery of core services.	Business case should clearly demonstrate what resources are required and where they will come from. Good business planning is essential – including contingency planning.
	delivery of core services.	Core service delivery should be protected, and, in most cases, it will not be acceptable to rely upon existing capacity to delivery commercial activity.

5 Conclusion

Taking into account all the considerations set out in sections 1-4, the draft commercial strategy sets out a model framework which seeks to facilitate and enable operational teams to take action and creating a whole authority approach to commercialisation. The aim is to foster a culture of entrepreneurialism where pursuit of commercial activity is expected of all staff throughout the organisation and provide a route to secure financial sustainability for the council.