



*Draft guidance on the power  
for Fire and Rescue  
Authorities to trade in  
function related activities*

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On 5th May 2006 the responsibilities of the Office of the Deputy Prime Minister (ODPM) transferred to the Department for Communities and Local Government.

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## Introduction

1. The *Local Government Act 2003* ('the Act') received Royal Assent on 18 September 2003. Section 95(1) of the Act provides power for the Secretary of State, or (in relation to authorities in Wales) the National Assembly for Wales, to make an order enabling best value authorities (with certain exceptions) to trade in any of their ordinary functions. This guidance relates **only** to Fire and Rescue Authorities. The exercise of section 95 powers by any other best value authority (including counties when not acting as a FRA) are governed by separate guidance issued in July 2004.

## Scope of the Guidance

2. The purpose of this guidance is to provide assistance to Fire and Rescue Authorities (FRAs) in England on trading through a company in anything that they are authorised to do for the purpose of carrying on their ordinary functions. Now that the relevant order has been made under sections 95 and 96 of the Act – the *Local Government (Best Value Authorities) (Power to Trade) (England) (Amendment) Order 2004* (S.I. 2004/2307), ('the 2004 Order') this guidance explains how, in the view of the Secretary of State, issues in relation to trading may be handled. This is statutory guidance issued under section 96(2) of the Act, to which authorities are required to have regard.
3. This guidance should not be taken to constitute legal advice or to provide a comprehensive view of the law.

## Sections 95 & 96 of the Local Government Act 2003

4. The Act contains powers for best value authorities to trade in function-related activities through a company and also provides for the regulation of these trading powers. Section 95 provides power for the Secretary of State, to make an order enabling best value authorities (with certain exceptions<sup>1</sup>) to trade in any of their ordinary functions through a company. Orders made under the power may relate to all best value authorities or to particular best value authorities, or descriptions of best value authority. Future trading Orders may be framed by reference to descriptions of authority which, by virtue of an order made from time to time under section 99(4), of the Act are of a particular category though the option remains to specify authorities by name
5. Section 96(1) provides an order-making power to impose conditions on the exercise of any trading power by a best value authority, including where this is undertaken through a company.

## The 2004 Order and future Orders

6. The 2004 Order provides, in respect of English FRAs, powers to trade in function-related activities through a company. In summary, the 2004 Order provides that:

<sup>1</sup> See section 95(7) of the Act for the best value authorities that are not included within the scope of the power.

- named FRAs are authorised to provide specified services for a commercial purpose;
  - the authority shall recover the costs of any accommodation, goods, services, staff or any other thing it supplies to a company in pursuance of any agreement or arrangement to facilitate the exercise of the power.
7. Future Orders, will lay further requirements on authorities wishing to access trading powers so that FRAs are brought within the general trading framework applicable to all other best value authorities:
- before exercising the power, the authority will be required to prepare a business case as specified in **Annex B** in support of the proposed exercise of the power which must be approved by the authority;
  - where an authority ceases to be a best value authority to which the Order applies anything which that authority is in the process of doing at the time the Order ceases to apply to that authority, may be completed by that authority; and any agreement or arrangement shall cease to have effect at the end of the period of 2 years from the date of the Order ceasing to apply to that authority.

## Background

8. The *Local Authorities (Goods and Services) Act 1970* governs the way in which local authorities are allowed to 'trade' with other **public** bodies. It authorises local authorities to enter into agreements with public bodies for the provision of goods, materials, and administrative, professional and technical services, for the use of vehicles, plant and apparatus, and for the carrying out of maintenance. There is also a power for the Secretary of State to designate by order that any person(s) exercising functions of a public nature shall be a public body for the purposes of the Act.
9. The Local Government White Paper, 'Strong Local Leadership – Quality Public Services' (DTLR, December 2001) went further than the earlier Consultation Paper, proposing to provide wider powers to trade for all authorities where this helps achieve best value and the delivery of public services.
10. The powers under the Act enable local authorities to trade with private bodies and persons for profit (i.e. where fees are fixed at more than cost recovery). The 2004 Order was introduced since some authorities had interpreted Section 3 of the Fire Services Act 1947 as giving them the power to trade and for those areas where authorities had so interpreted it the position was preserved through the Order. In all cases the power to trade is only exercisable through a company. This will help to ensure a level playing field with the private sector.

## Context for Trading

11. Trading will help create a dynamic and entrepreneurial public sector that will increase diversity and choice in the delivery of public services. Trading should encourage best value authorities, including FRAs, to extend and improve the range of services they offer and will introduce new players into the market. Trading with a wider range of bodies should help to increase the scope for partnership working and provide business opportunities for the private sector.
12. Trading activity needs to contribute towards Best Value in the related function. Authorities can only set up trading arms in **function-related** activities. Authorities need to be clear that they have the power to engage in an activity before they trade in it.
13. Surpluses on commercial operations under the section 95 trading power (i.e. post tax surpluses) would be available to individual authorities to use as they see fit. Trading should be conducted on a fully transparent basis and authorities should not distort markets through the provision of inappropriate subsidies to trading companies.

## Charging and Trading

14. Section 19 of the Fire and Rescue Services Act 2004 provides FRAs to charge for services specified by the Secretary of State in an Order. The first such Order (SI 2004/2305) came into force on 1st October 2004. Separate guidance has been issued on use of the section 19 power.
15. The charging and trading powers are separate and may be exercised separately. The essential difference between charging and trading is that charging is limited to cost recovery whereas trading (through a company) permits the making of a profit. The other main difference is that while all FRAs are able to access the charging powers only those authorities specified by name or category in a trading Order, whether the 2004 Order or those made in the future, may access trading powers.

## Relationship with Local Authorities (Goods and Services) Act 1970 and Local Government Acts 2000 and 2003

16. The *Local Authorities (Goods and Services) Act 1970* has served local government well. Authorities have made extensive use of these powers to provide goods and services to other authorities, both to make use of surplus capacity and to secure the benefit of economies of scale. However, the 1970 Act restricts the type of services provided and the bodies with whom an authority can trade. The new trading powers contain no such restrictions.

17. Existing *public to public* trading activities under the *Local Authorities (Goods and Services) Act 1970* ('the 1970 Act') will remain. These will operate in parallel with the section 95 trading power. Applications from bodies seeking public body designation under section 1(5) of the 1970 Act will not receive Ministerial approval where it appears that the body seeking the designation is largely a local authority sponsored vehicle designed perhaps to avoid the statutory framework in sections 95 and 96 of the Act. The powers contained in the Trading Order are primarily concerned with *public to private* trading.

## Trading through a Company

### Restrictions on Power to Trade

18. Section 95 of the Act enables Best Value authorities to provide on a commercial basis, anything that is related to a function of the authority or is ancillary, conducive or facilitative to the exercise of that power. The power is widely drawn to include all functions, whether express, implied or incidental.
19. Whilst the power to trade is widely drawn it is subject to restrictions, principally:
- the power must be exercised through a company (within the meaning of Part 5 of the *Local Government and Housing Act 1989*);
  - the trading must be function-related;
  - the power cannot be used to authorise trading in anything which an authority is statutorily obliged to do in relation to a person;
  - Section 95 trading may also be regulated through the imposition of conditions by order, under section 96 of the Act;
  - alternative arrangements exist for FRAs that were already trading under section 3(1)(e) of the Fire Services Act 1947 on 1st April 2004;
  - any company established for the purposes of carrying out trading under this section, in which a FRA has an interest, shall be subject to the rules about controlled, influenced, regulated and minority interest companies provided by Part 5 of the *Local Government and Housing Act 1989* and the *Local Authorities (Companies) Order 1995*<sup>2</sup>.
20. In deciding whether and how to exercise the trading power, authorities must still have regard to their own procedural rules, Wednesbury principles of reasonableness, proper purposes and fiduciary duty. A business case and risk analysis will be required, except for trading conducted by virtue of the 2004 Order. Authorities will not be able to

<sup>2</sup> Notwithstanding the repeal of that Order by the Local Authorities (Capital Finance) (Consequential, Transitional and Saving Provisions) Order 2004 which came into force on 1 April 2004.

delegate some formal decisions and determinations to companies, unless they are covered by an Order under the Deregulation and Contracting Out Act 1994.

## Local Government Capital Control System

21. Part 1 of the *Local Government Act 2003* introduced a new system of local government capital expenditure controls (the Prudential Capital Finance System) for the financial years beginning on, or after, 1 April 2004. Local authorities are now free to borrow for capital projects without Government consent – provided they can afford to service the debt without extra Government support. Authorities are required to have regard to CIPFA's 'Prudential Code for Capital Finance in Local Authorities' in making their determinations. The Government retains a reserve power to impose limits on borrowing either nationally, to protect the country's economic interests, or on individual authorities (sections 2 and 4).
22. Section 18 of the 2003 Act allows companies controlled or influenced by a local authority<sup>3</sup> to be brought within the new capital controls by regulations. The current wording of this section relies on definitions of 'company', 'control' and 'influence' contained in Part 5 of the *Local Government and Housing Act 1989*. No regulations have been made under section 18 and none are planned (but see para 23 below).
23. Therefore, when an authority sets its own limits in accordance with section 3 of the 2003 Act and the Prudential Code, it sets them purely for the authority – the borrowing the authority is to undertake, considering its own revenue account resources available to service the borrowing. But the Prudential Code (in paragraph 31) says – "Where the authority has interests in companies or other similar related entities, the authority needs to have regard to its financial commitments and obligations to those companies/entities". In other words, the authority needs to have regard to any obligation to pay amounts to a company, or a risk that a company will call on the authority's resources that will reduce the resources available to service debt and hence reduce the borrowing limits. Any transactions of such companies that have an impact on the authority's finances will have to be taken into account in assessing the affordability of any proposed borrowing by the authority. However, whilst the Prudential Code currently does not operate on a group basis, if ever a national limit were to be imposed under section 4, it would be the intention to make regulations under section 18 to apply the limit to local authority groups rather than just to the core authority.

## Providing Services to Trading Companies

24. An authority has the power to do anything which is calculated to facilitate or is conducive or incidental to the discharge of its express powers. The power to trade in function-related activities under section 95(1) is an express power. Accordingly, if for example it appeared to an authority that the arrangements for the carrying out of function-related trading would be most appropriately handled by a 'company', the authority would be able to establish a company for that purpose under its subsidiary powers. Authorities may wish to extend to companies carrying out function-related

<sup>3</sup> By virtue of section 23 of the same Act all Fire and Rescue Authorities come within the definition of a local authority for the purposes of section 18

trading, assistance of whatever kind they think appropriate, including providing staff and other support services. There are several different ways in which authorities can provide services to the companies through which they trade. Providing such assistance is incidental to, or part and parcel of, the power to enter into an arrangement with a company for the purpose of exercising the power to trade. Accordingly, the following ancillary and express powers may also be used in connection with a company involved for the purpose of exercising the power under section 95:

- power to certify agreements related to the company under the *Local Government (Contracts) Act 1997* (i.e. long-term contracts for services or other agreements providing finance in connection with such contracts);
- power to enter into shareholders agreements before and after the establishment of the company;
- power to enter into agreements with the company for the supply of, works, goods and services (by and to the company), the transfer and secondment of staff, the provision of premises, and the exercise of intellectual property and other contractual rights;
- any consequential activity;
- power to hold, buy, or sell shares and receive dividend payments.

25. Because the power to trade is subject to a restriction requiring it to be exercised through a company, it follows that the authority has the requisite power to enter into arrangements with a company in order for the trading power under section 95 to be exercised. It is not necessary therefore, for the company to be expressly designated as a public body under the *Local Authorities (Goods and Services) Act 1970*, in order for the authority to be able to provide it with staff, goods etc, for the purpose of exercising the power to trade.

## Preparing to Trade

26. Local authorities will need to be prudent, in particular, about putting council tax payers' money at risk. The council may wish to discuss these proposals with their auditor to check the auditor is satisfied with the arrangements the council has made for managing the risks in the process. Local authorities remain bound by European legislation, domestic law, general administrative legal principles such as *Wednesbury* reasonableness, and their fiduciary duty. A number of steps need to be considered by authorities when preparing to trade. These are set out at **Annex A**.

## Making a Business Case and Business Planning

27. There is a distinction to be drawn between the business case and the business plan:
- the **business case** assesses the risk involved in the proposed trading enterprise and decides whether or not it should proceed. It starts the process of business planning;
  - the **business plan** sets out the objectives of the business, how they are to be achieved and standards met adjusted in the light of experience and changing circumstances. It is a comprehensive analysis of the business situation at a particular point in time.

### Making A Business Case

28. There are a number of steps that should be undertaken to make a business case and produce a business plan. These are set out in **Annex B** along with an outline of a possible Business Plan. The Annex also includes extracts from *Developing a Successful Business Plan – a Ten Step Guide* (PricewaterhouseCoopers, 1997) which authorities may find helpful. The business plan is not an end in itself – it is a means of ensuring business success. Business planning is much more than an annual event of producing the business plan. For example, if unforeseen circumstances occur, elements in the plan may be in need of revision.

### Organisational Issues

29. The organisational model for the business venture will need to be considered and defined at an early stage. Although an authority may want to establish a company for the purpose of using it as a vehicle for function-related trading, it does not have to proceed in that way. It may equally trade through a company in which it has not been directly involved in setting up for this purpose. An authority need not establish its own company, nor are the commercial purposes necessarily just those of the authority. It would be possible for an authority to agree with an established commercial company to trade through it on a contractual basis to mutual benefit. Whatever an authority chooses to call or establish as their trading body, it has to fit the description of ‘companies’ under Part 5 of the *Local Government and Housing Act 1989*. Definitions of a company in Part 5 include:
- (a) a company limited by shares;
  - (b) a company limited by guarantee and not having a share capital;
  - (c) a company limited by guarantee and having a share capital;
  - (d) an unlimited company;
  - (e) a society registered or deemed to be registered under the *Industrial and Provident Societies Act 1965*.

30. Any of these forms may comprise a company for the purposes of section 95. However, it seems most likely that the company form taken will be a company limited by shares which provides more flexibility to trading companies, particularly with regard to distributions of profit and raising risk capital. The choice will have a fundamental impact on how people are employed, and the skills and numbers required.
31. All of the options listed above have a different legal status that will impact on how they are run, managed and financed. Depending on the model chosen, the operation will need to be open to an appropriate level of scrutiny. The authority's section 151 Officer, and probably the authority's Monitoring Officer, will need to be involved to different extents at different stages of preparation.
32. A trading company will be a separate legal entity from the authority. It will derive its legal authority from its Memorandum of Association and the Companies Acts. Its directors and officers will derive their authority from the articles of association and the law relating to companies. The objects of the company will be defined in its memorandum and articles of association. They should be drawn carefully to ensure they cover all potential trading activity. Table A of the *Companies Act 1985* contains model articles of association for a trading company which are normally used as a base by most companies and adapted to specific circumstances.

## Trading Companies

### Structure

33. A company may be limited by shares or by guarantee. A trading company is likely to be limited by shares. Other vehicles such as companies limited by guarantees (with or without share capital), are unlikely to be appropriate for a trading company as these are more appropriate for a not-for-profit company which may also be registered as a charity. An unlimited company is unlikely to offer the level of protection the local authority would want. However special vehicles which can be created in this framework, such as Industrial and Provident Societies, may offer a more flexible approach suitable for some circumstances.
34. The company will be run by its board of directors answerable to the membership in accordance with the articles of association. A board of between 3 and 8 directors is most likely to be practical. The participating authority should be represented on the board, and its level of representation and voting rights are likely to be proportionate to its shareholding. The members or officers who are appointed directors will participate directly in the activities of the company, and are answerable to the company and have the powers and duties of company directors whilst they do so. Other local authority members and officers may become involved if, by agreement, they are given the right to attend board meetings as observers. They cannot participate in decision-making, though, and must avoid so doing for fear of becoming shadow directors.

## Governance Framework

35. Authorities will need to have regard to the accountability and governance framework for the company. They may wish to refer to '*The Combined Code – Principles of Good Corporate Governance and Code of Best Practice*', originally published by the Stock Exchange in June 1998 (updated 2003). It was produced by the Hampel Committee and superseded the work of Cadbury and Greenbury. It gives a broad framework for corporate and internal controls. Reference may also be made to guidance produced by the Strategic Partnering Taskforce (DCLG), which can be found on the DCLG website: <http://www.communities.gov.uk/ssdp>.

## Conflicts of Interest

36. Authority members and officers should be aware of potential conflicts of interest when carrying out their roles for their authorities, or when acting as directors of trading companies. The conduct of authority members is governed by their authority's code of conduct. That code must include, as a minimum, the mandatory provisions of the model code of conduct, issued by the Office of the Deputy Prime Minister (ODPM) in November 2001.
37. Members must register certain financial and other interests as set out in the Code of Conduct. Members should have regard to the specific categories of interests set out in the Code but should note that these include naming any company for which they are a remunerated director and also membership of or a position of general control or management in any company or industrial and provident society. The Code of Conduct for members sets out the circumstances in which a member should regard himself as having a 'personal interest' in any matter. These include any matter relating to any interest which the member is obliged to register. Members who consider they have a personal interest in any matter should declare that interest if the matter is discussed at a meeting of the authority. In addition, a member with a personal interest also has a prejudicial interest if the interest is one where a member of the public, if he or she knew all the relevant facts, would think that the interest was so important that it would be likely to prejudice his judgement of the public interest. A member with a prejudicial interest in a matter being discussed must withdraw from the meeting. Members themselves must decide whether or not they have personal or prejudicial interests in particular issues.
38. A Director's principal duty is to the company, but any members that are elected as directors are still bound by relevant codes of conduct, in so far as they do not conflict with their legal obligations under company law. In addition when voting as a director on company matters, regard must be had to any rules on declaring interests as set out in the Memorandum and Articles and any restriction in those on voting in certain circumstances. If the company is set up by the authority specifically to take advantage of section 95 it may be considered advisable to adopt similar rules on interests to those contained in the Code of Conduct as members will be familiar with these and it will ensure consistency amongst all directors.

## Personal Liability for Directors

39. Company directors may incur personal liability, for example in respect of breach of duty, wrongful trading, fraudulent trading, breach of a disqualification order and other specific liabilities such as corporate manslaughter. It is good practice for the company to insure against this risk. It is advisable for directors to check the company's indemnity policy and good practice for authorities to issue guidance to their nominated directors on the responsibilities and liabilities of being a director of a company. Such guidance should cover matters such as a director's duties to act in the best interests of the company, provision and use of information, duty to employees and the fiduciary duty to creditors, as well as warning of the potential for personal liability. Authorities may be able to indemnify members and officers against this personal risk. However, any such indemnity will generally only cover actions taken honestly and in good faith.
40. The Local Government Act 2000 contains a power at section 101 to make provision by Order enabling 'relevant authorities'<sup>4</sup> to indemnify their officers and members. The Government proposes to bring forward an Order which is intended to clarify the position which will be in addition to any existing powers that authorities have relied upon.

## Nominees to Trading Company Board

41. The authority will need to consider whom they should nominate to be on the board of the company. For an authority operating executive arrangements, the responsibility for making decisions about the company, including who should be their nominee or nominees, may be made by either the executive or the full council depending on the circumstances. A member of the executive might find him or herself in a situation where their position on the board of the company might lead to their having a personal and prejudicial interest in a matter the executive was dealing with which might restrict their ability to take decisions on the executive. If a nominee is an officer of the authority, the authority or executive, as the case may be, may want to consider whether they should be the Chief Executive, or where there is more than one nominee whether the Chief Executive should be one of the nominees.
42. A successful company will be one that works alongside the authority in delivering joint objectives. The authority will have to consider how to balance the need to assist the company to achieve its trading objectives with the principles of transparency, accountability and probity. Where the business of the company has moved to being more significant, an authority should consider the benefits which the appointment of independent (or non-executive) directors could bring to the business.
43. The managing director will probably be an employee of the company, but in exceptional circumstances may be seconded from the authority or another shareholder. Arrangements must be established to ensure that the managing director has no conflict of interest. If it is an authority secondee the authority may wish to set up arrangements for appropriate information use and confidentiality to ensure that they and the company can be satisfied their position is not weakened by the secondment.

<sup>4</sup> Fire and Rescue Authorities are 'relevant authorities' for the purposes of s101 as they are referenced in section 21(1) of the Local Government and Housing Act 1989

44. The company's articles of association will set out the internal operation of the company, e.g. shareholding, voting rights, the appointment of directors, the operation of the board, declarations and conflicts of interest, indemnities/insurance cover and financial regulations.

## Directors Fees/Remuneration

45. Authorities will wish to give consideration to the remuneration and rewards of the directors and management. Private sector companies often have remuneration committees that determine pay levels and whether other incentives, such as share options and employee share option plans, should be in place. Any authority considering paying members for their responsibilities in respect of the company should do so in the context of the normal arrangements for members' allowances.

## Shareholding

46. Either the authority will be the sole shareholder or it may, initially or later, allocate or sell shares to others. If it chooses to exercise its powers under section 95, through a company previously established by others to achieve different commercial objectives, it will need to satisfy itself that its own commercial objectives will be satisfied through this particular company. If it is not to be the sole shareholder, it should enter into a shareholders' agreement with the other shareholders and the company, covering matters such as:
- the allocation, transfer and disposal of shares;
  - the rights to be attached to different classes of shares;
  - 'golden shares', under which a particular shareholder can reserve the right to veto fundamental changes, for example changes to the business objectives, the business plan, or the appointment of the managing director. Authorities should make full use of this principle to safeguard matters which are fundamental to the purpose for which they are establishing the company, but need to take care that they do not change the status of the company for the purposes of Part 5 of the 1989 Act;
  - exit and termination provisions.

## Staffing, Personnel and Employment Issues

47. Whether the trading company is established as a company for direct service provision using existing employees, or as a joint arrangement with another local authority (also using existing employees), the company will be a separate legal entity. Local government employees may be transferred to the company. This may amount to a transfer under the *Transfer of Undertakings (Protection of Employment) Regulations 2006* ("TUPE") or it may be subject to Directions made under section 101 of the 2003 Act. Whether or not there is a TUPE transfer depends on the facts of the individual case.
48. It is the responsibility of local government to promote a well-trained and motivated workforce. Authorities should consult their employees and recognised trade unions or

staff representatives throughout, with full disclosure of information on all matters affecting the workforce. Full, effective and continuous communication is key to managing transfers well.

49. However, if the decision is to establish an organisation, which is separate from the authority that has created it, there are a number of issues associated with employing people to deliver services. Employees for the new enterprise can only come from one of four sources, which are:
  - (i) recruitment from the local/national market place;
  - (ii) transfer of staff from within the authority;
  - (iii) secondment of staff from the authority;
  - (iv) another arrangement, e.g. taking over the employees of another existing business through a merger/take-over/purchase of that business.
50. Depending on the facts, in the case of ii) iii) and iv) above TUPE may apply. However this is dependent on the particular circumstances regarding the establishment of the authority trading company and/or arrangements regarding secondment of staff to a commercial company through which the authority is trading. In the case of ii) the Code of Practice on Workforce Matters in Local Authority Service Contracts (Annex D of ODPM Circular 03/2003 published 13 March 2003) concerned with new joiners to an outsourced workforce, will also apply.

## Recruitment Issues

51. Any recruitment exercise needs to determine the duties and responsibilities of new employees and the skills, knowledge and experience, which will be required. Appropriate salaries will need to be established and it may be useful to evaluate the jobs through a recognised mechanism. At the same time, the other terms and conditions will need to be established, including hours to be worked, pay arrangements, flexibility of working hours/patterns and arrangements, leave entitlement, sick pay arrangements, statutory/best practice policy requirements and pension arrangements/entitlement.
52. For a new limited company these terms and conditions may be the same as existing local authority terms and conditions, and existing staff may transfer across with appropriate safeguards. If terms and conditions in the new company are unrelated to local government terms remember that, if the aim is to attract some local government employees in to the business to take advantage of their specific knowledge or expertise, then the attractiveness of the offer, particularly in relation to pensions, will vary for potential employees. Care must also be taken not to create equal pay tensions between groups of employees doing work of the same kind.
53. There is a need to comply with existing employment legislation, for example:
  - Race Relations, Sexual Discrimination, and Disability Discrimination legislation;

- Working Time Directive;
- National Minimum Wage legislation;
- Employer's Liability and Public Liability Insurance requirement;
- Statutory Sick Pay/Maternity Pay/Paternity and Adoption Leave;
- Time off for Dependents;
- Health and Safety.

## Transfer of Staff

54. Where existing authority workers are transferred to the new business, which is seen as separate from the work of the authority, the expectation would be that their existing terms and conditions will be protected under the *Transfer of Undertakings (Protection of Employment) Regulations 2006 ('TUPE')* or under Directions to be made under section 101 of the Act, unless there are exceptional circumstances. In particular, this means that all their contractual entitlements are protected whilst they continue to carry out the work which previously formed a part of the working practices of the authority, and throughout their employment with the new employer, unless their terms and conditions are changed for a reason other than the transfer. This is also the case for any employee transferred from one business to another.

## TUPE Regulations

55. These aim to ensure that:

- the contract of employment between the existing employer and its employees, with their rights and liabilities are transferred automatically to the new employer
- it would be automatically unfair to dismiss employees in connection with the transfer, unless this is for specific and defined reasons
- collective agreements in place with the existing employer are transferred to the new employer
- the existing employer is obliged to inform and consult with employee representatives whose members are affected by the transfer.

56. The 1981 TUPE Regulations, which had been amended on a number of occasions, have been replaced by the Transfer of Functions (Protection of Employment) Regulations 2006, which came into force on 6th April 2006. These preserve the same general rights conferred on employees, and obligations imposed on employers, as the earlier Regulations, but introduce some additional matters. The main changes include a duty on the transferor employer to supply information to the transferee employer, provisions relating to agreed variations of contracts of employment on the occurrence of a relevant transfer, and provisions relating to dismissals for reasons connected with a relevant transfer.

57. The position of transferring staff is also affected by the Pensions Act 2004, which came into force on 6th April 2005. The Act (and Regulations made under it: the Transfer of Employment (Pension Protection) Regulations 2005) require a transferee employer to secure that the employee is, or is eligible to become, an active member of an occupational pension scheme in relation to which the transferee is the employer, or to make alternative pension provision by way of contributions to a stakeholder pension scheme of which the employee is a member.
58. The *Code of Practice on Workforce Matters in Local Authority Service Contracts* (Annex D of ODPM Circular 03/2003) is intended to ensure that new joiners to transferred out workforces are offered terms and conditions which are, overall, no less favourable than those of transferred staff. These best value duties in relation to staff transfers are equally relevant to the transfer or secondment of staff as part of setting up trading companies under section 96.
59. Sections 101 and 102 of the Act confer new powers on the Secretary of State to require best value authorities in England, when engaged in contracting-out exercises, to deal with staff matters in accordance with directions. The background to this is the commitment made as part of a package of workforce measures, following the Review of Best Value, to make statutory within local government the provisions in the Cabinet Office *Statement of Practice of Staff Transfers in the Public Sector* and the Annex to it, *A Fair Deal for Staff Powers*.

## Local Authority Assistance to Companies

60. If a trading company is established for commercial purposes, then necessarily it will seek to make a profit. Any financial assistance, in cash or in kind, given by an authority that establishes or participates in it, should be for a limited period, against the expectation of returns later. Any assistance should therefore be provided under a formal agreement with the company. The agreement must be entered into for a commercial purpose. The agreement may provide for grants, loans or guarantees. Before entering into such an agreement, the authority should satisfy itself that it will achieve its objective, and the company should satisfy itself that it will meet its objective in terms of its business plan. In addition the usual rules on vires, Wednesbury reasonableness and fiduciary duty apply. Also the conditions in the relevant trading Order and the requirements of competition legislation need to be met.
61. Under the conditions provided in article 3(3) of the 2004 Order an authority must recover the costs of any accommodation, goods, services, staff or any other thing it supplies to a company in pursuance of any agreement or arrangement to facilitate the exercise of the power. Each authority making use of the power to trade will need to establish a robust methodology for assessing the costs to the authority of providing assistance to a trading company. Authorities are free to decide what methodology to adopt. They may however find it helpful to draw on existing and familiar principles as set out in the CIPFA *Best Value Accounting Code of Practice*. One option would be to use the Code's definition of 'Total Cost'. As an alternative, authorities may wish to consider adding to total cost an appropriate contribution for Corporate and Democratic Core (CDC) and Non-Distributed Costs (NDC), as those terms are defined in the Code, as part of the costs of provision. The Code offers guidance on practice authorities might adopt and is amended from time to time to take account of changes in requirements.

62. An authority that establishes a trading company should expect to receive income from that company either in the form of dividend payments or through the growth in value of its shares or other investments in the company, which it can subsequently realise. Income from a trading company may be applied in any area of the authority's activities to support expenditure, subsidise services, or reduce local taxation.
63. The authority will only be responsible for debts and losses of a limited liability company to the extent of the nominal value of its shareholding, and, more significantly, to the extent of any guarantee or contractual arrangement that it has entered into. If there is no such guarantee or agreement, the authority would not be under any obligation to meet the company's debts, and if it wished to do so it would have to satisfy itself that it had the legal power and that it was exercising that power properly.
64. However there are other risks if the company cannot meet its debts, if that company provides services that would otherwise be provided by the authority. This might arise in the context of insolvency or where the company is unable to deliver on any contracts with the authority which may give rise to losses or liability on the authority in respect of any failure by the company to deliver. In considering structures, the authority should ensure that it takes appropriate steps to avoid automatically assuming responsibility for any aspects of an unsuccessful company. This should include the actual provision of services.

## Transparency

65. It is important that trading companies can operate on an equal footing with their competitors, but it is equally important that they are not used as a device for inhibiting legitimate public access to information about local government and local government services. The authority should ensure that its own internal auditors have access to information held by the company and its subsidiaries.
66. The authority should ensure that its overview and scrutiny committees are able to exercise their powers in relation to the discharge of authority functions under the relevant legislation. When an authority (or a committee or executive) meets to consider the affairs of the trading company, such matters may be exempt from disclosure to the public if they fall within Schedule 12A of the *Local Government Act 1972* (as provided in section 100A(4) of the 1972 Act). Matters described in Part I of the Schedule are exempt from disclosure if the authority so provides by resolution, although Part II of the Schedule qualifies a number of the exemptions and provides the condition on all exemptions that information is only exempt if the public interest in maintaining the exemption outweighs the public interest in disclosure. Local authorities are also subject to the disclosure requirements set out in the Freedom of Information Act 2000, some of which are similarly subject to the public interest test.
67. The *Data Protection Act 1998* ('DPA') requires data controllers to register with the Information Commissioner. A data controller is an individual or a body which determines the purposes for which, and the manner in which, information about individuals (i.e. personal data) is to be processed (which includes obtaining, holding, using, storing, altering and disposing of personal data). Where the company is simply a data *processor* in respect of local authority data (in other words it does not determine

the manner in which and the purposes for which the data are to be processed), then it does not need to register with the Information Commissioner, but the local authority would need to have in place a processing contract with the company, the basic terms of which are prescribed in the DPA. It is very likely that a trading company if it processes personal data will need to notify the Information Commissioner under the DPA 1998 especially if it employs staff, keeps client lists etc. For example, processing includes collection, organisation, retrieval, alteration, storage and disclosure and destruction of data which means that it is likely that a company would be covered by the provision.

68. The FOIA will apply to the authority which may consider that there should be an agreement in place with the company to ensure that information which is held by the trading company on behalf of the authority, which the authority is under an obligation to disclose, can be easily accessed. A distinction needs to be drawn between the authority dealing with or through a separate private company, which would not be subject to FOI requirements, as it would not be a 'public authority' and a company which the authority set up to trade in an activity related to one of its functions. Where a person (including a legal person, e.g. a company) or body provides under a contract with the authority any service the provision of which is a function of the authority, such a person or body may be designated a 'public authority' for purposes of FOI requirements, by order under section 5(1)(b) of the FOIA. There is a possibility that a company carrying out contracted out services could be designated a public authority in its own right and subject to the section 1 obligation.
69. The authority should consider appointing a 'contract officer' and/or 'contract member' with primary responsibility for liaison between the company and the authority, and for access to information about it. It might wish to place limitations on these individuals to ensure that they are fully accountable to the authority as a whole and to ensure that the Section 151 Officer/Monitoring Officer countersigns major decisions about the company's operations.
70. The authority or, where they are operating executive arrangements, the executive should view the company's audited accounts and reports on the activity and trading position of the company. The authority should also approve the business plan and see the accounts at least annually but are likely to require more frequent reports.

## Procurement

71. The EU procurement rules may apply where the authority provides services, supplies or staff to the trading company, where the authority buys services, supplies or staff from the company or where the company itself buys services. It is likely that the procurement rules will apply to procurement by the company, if the company has been established to meet needs in the general interest, does not have an 'industrial or commercial character', and is wholly or mainly funded by a body (such as a local authority) to which the rules apply, or is subject to management supervision by such a body, or has more than half its membership or board of directors appointed by such a body. The company should not become a means for avoiding normal good practice in local authority procurement, certainly so far as probity and anti-fraud measures are concerned. It should adopt a formal procurement policy.

## State Aid

72. If the State (this includes local authorities) provides aid that affects trade between Member States and distorts competition (through conferring a benefit) this could contravene the EC prohibition on the granting of state aid. Although there is no definition of state aid, Article 87(1) of the Treaty establishing the European Communities sets out four elements – all of which must be satisfied if a measure is to constitute state aid. These are given, with some further information in Annex C. If the four tests are met, or if there is a risk that they are met, then there is an obligation to notify the European Commission, before measures are put into effect. If there are advantages of any kind then authorities need to examine this issue. Some types of aid, such as ‘de minimis’ aid, are covered by block exemption regulations published by the Commission. These provide an exemption from the need to pre-notify the Commission, provided all the requirements set out in the relevant regulation are met.
73. As the rules governing state aid are not straightforward, it is essential to consider at the earliest possible stage whether a measure will present problems and to obtain specialist advice.

## Taxation

74. Authorities should plan ahead and understand that local authority companies will be subject to taxation, especially VAT and corporation tax. Further information about corporation tax may be obtained from the tax office that deals with the company’s affairs or alternatively from the tax office that deals with the local authority’s affairs. Authorities must also consider the VAT implications of establishing a trading company. The limited company as a normal trader is not entitled to recover tax under the special VAT rules that apply to local authorities (section 33 of the Value Added Tax Act 1994). Therefore, the normal VAT rules apply to that company. Any queries about the VAT affairs of the trading company should be referred to the National Advice Service on 0845 010 9000, and HM Customs and Excise’s website [www.hmce.gov.uk](http://www.hmce.gov.uk). All public notices can be found on Customs’ website. However, local authorities may find the following guidance useful: VAT Notice 700/1 ‘Should I be registered for VAT?’

## Human Rights Act

75. If any company set up under these provisions is held to be carrying out the function of a public authority they shall be bound by the Human Rights Act 1998 (see *Donoghue v Poplar HARCA*). In that case the company set up by the local authority to own and manage certain of its housing stock was held to be carrying out the functions of a public nature in respect of accommodation provided for the authority’s nominated tenant.

## Anti-competition Legislation and Competition with Local Businesses

76. The requirement to use companies for trading under section 95 places local authorities in the same position as any other commercial undertaking as to the need to meet costs and make a profit. If authority trading operations were to prove successful, there could be some impact on local markets especially small businesses. The successful development of larger trading operations by authorities however, could reasonably be expected to lead to new economic opportunities as well as possible disadvantages for small businesses, as suppliers or in specialist markets.

### Competition Law

77. The *Competition Act 1998* introduced two prohibitions which reflect Articles 81 and 82 of the EC Treaty respectively. The Chapter I prohibition covers agreements between undertakings that have the object or effect of distorting competition in the United Kingdom, or a part of the United Kingdom. The Chapter II prohibition makes unlawful conduct by one or more undertakings which amounts to an abuse of a dominant position in a market in the United Kingdom.
78. Authorities should consider any proposed charging and trading activities very carefully against the requirements of competition law, consulting their own lawyers as necessary. Trading by local authorities may be subject to the provisions in the *Competition Act 1998* and/or Articles 81 and 82 of the EC Treaty.
79. Whether or not a local authority may be considered an undertaking with respect to a particular activity (and therefore subject to competition rules), depends on whether the activity is ‘an economic activity’, a term which has a complex legal meaning. Neither the legal status of the trading body (i.e. being a company or not) nor the way in which it is funded are determinative on this. Therefore, the new provisions do not make a significant difference in local authorities’ obligation to abide by competition rules. Guidelines on the two prohibitions and additional guidance on when a public body may be an undertaking can be found at [www.oft.gov.uk](http://www.oft.gov.uk)
80. Authorities who, having read the guidance, are still unsure about whether they may be considered undertakings with respect to an activity and whether that activity may infringe competition rules, are urged to seek legal advice.

### Exit Strategy

81. Authorities may require an exit strategy from trading. The Authority may fail in a trading operation or decide that it wishes anyway to withdraw. This situation may have implications for staff involved.

## Annex A: Preparing to Trade

A number of steps need to be considered:

### Preparing to Trade

*Market Analysis* – Initial opportunities for trading are most likely to arise in the context of existing service provision. This will be because local authorities understand the market and know what is involved in delivering that service. Before an authority commits to any business venture there is a need to confirm if there is either an existing demand or a strong potential demand for service or product. Analysis should be undertaken by researching customers, products and competition. This will result in a better understanding of the competitive position, the chance to spot opportunities, risks being reduced, and, better decision making.

*Customer Research* – This will identify the numbers and types of people whom might become customers. ‘Profiling’ customers enables authorities to locate the ‘ideal’ customers for the product or service. The aim is to understand as much as possible about customers’ behaviour, needs, expectations and buying patterns. The more precisely a market niche is identified; the more selling opportunities there are likely to be.

*Service/Product Research* – This looks at what is being sold, how it compares with other services or products and how it might be developed or refined. If the service is not new and if there is little difference in product/service between competitors, then another approach may need to be found, e.g. more convenient, after-sales service.

*Competition Research* – The level and strength of competition indicates how difficult it will be to gain a share of that market. Identifying similar products and potentially similar customers will highlight whether there is a gap in the market. A detailed analysis of competitors’ strengths and weakness will demonstrate whether there is a place for the product or service.

*Risk Analysis* – Researching customers, products and competition will provide information that will enable an evaluation of risks to be undertaken in context. Risks may arise in the internal environment (e.g. staff, internal customers, office technology, wages, finance); the micro-environment (e.g. external customers, distributors, suppliers, competitors), and the macro environment (e.g. political, economic, socio-cultural and technological factors).

*Carrying Out Analysis and Research* – a research brief should specify the information needed to evaluate the target market and the opportunity to gain entry. Possible sources of information about the target market include the Internet, Trade Associations, the local library, local Business Link, Chamber of Commerce or Enterprise Agency. The range of information needed includes:

- market data: what is the size and growth rate of the market? Who are the potential customers? Consider both local and national markets.

- competitive data: who are direct competitors? What are their services and prices?
- internal data: what information is already available to assess the strengths and weaknesses of your service/product and its core capabilities?
- what is the future outlook for the service/product?

NB Desk research involves data already available, for example, economic trends and specific industry sector reports. Field research requires the collection of information directly from potential customers. Examples include market surveys, telephone questionnaires and focus group research. Professional market research companies can be used to carry out this research. The cost of using a company needs to be balanced against the type of information needed.

# Annex B: Business Case and Business Plans

## A. Making a Business Case

There are a number of steps that should be undertaken to make a business case and produce a business plan:

### Business Case and Business Plan

The following should be undertaken:

- an analysis of current activities, including resources, costs and standards of the business.
- an assessment of risks faced and how significant these risks are (there are commercial models on the market to help quantify the risk to a business).
- conduct a strengths/weakness/opportunities/threats (SWOT) analysis against the general objective of reducing risks and achieving business success. Some of the questions raised may only be answered by conducting research. Consider dependencies, a range of scenarios and draw up contingency plans.
- consider options to exploit strengths and opportunities, correct weaknesses and reduce threats. Assess options in terms of priorities, practicalities (in terms of resources and time) and financial viability.
- check against factors determining long term trends – political, economic, demographic, social, technological, legislative and environmental factors.
- create a customer/service matrix, identifying current and new areas for both dimensions.
- subject the intended pattern of activity to a further SWOT check and amend if necessary.
- taking account of the likelihood of risk occurring.
- if risks are too high, then do not proceed. From this analysis and research:
  - define your trading activities.
  - set business objectives, levels, standards and performance criteria.
  - decide on costing and charging policies and systems.
  - define resource requirements in terms of staff and operational resources.
  - outline start up costs and investment required.

- identify sources of finance.
- produce a co-ordinated action programme.
- produce a master budget.
- define monitoring, evaluation and revision processes.

### *Purposes of a Business Plan*

The business plan has at least 3 purposes:

#### Purposes of Business Plan

- to demonstrate to members, potential investors and the company board that the business is a viable enterprise, with an identified market, an achievable set of business objectives, and an adequacy of managerial and other necessary skills and experience
- to assure potential clients the business is well-run and has the capability and resources to ensure reliability and quality
- as an internal management tool to ensure that all parts of the business work together towards common and consistent goals, and that these goals are based on sound analyses, assumptions and are consistent with LA objectives

## **B. Possible Business Plan**

### *Overview*

A brief statement of the fundamental features of the business, its nature, size, what it aims to do for whom, what makes it unique and those features that will give it particular credibility and point to its viability.

### *Summary*

The summary can include background information and be written so that it can be used on its own. The important elements will be:

- the fundamental purpose and character of the business including the mission statement and core values.
- primary or core objectives. What does the business hope to achieve over the next one to three years?
- business history.
- summary of all key elements of the plan.
- a statement highlighting the advantages of the business to an investor.

*Management and Staffing* (see also ‘Organisational Issues’ below)

- a description of staffing – managerial, professional/technical, administrative and external suppliers of advice, information or services. Overall numbers and the names, qualifications and experience of key staff.
- an analysis of what the business needs in terms of skills and experience and any planned action to ensure these needs are met. This might include planned recruitment, training initiatives, and staff (re) deployment or redundancy.

*Products/Services*

- a description of what the business produces and to what standard.
- what skills and processes are involved? Processes will include performance and quality management, including success criteria, and protective measures such as copyrights, licence rights and insurances.

*Markets and Marketing*

- market analysis – who are the current and potential customers and competitors?
- marketing – how does the business promote itself?
- marketing strategies – how might the business develop?

*Action Programme for the Development of the Business*

- What needs to be done to ensure that the plan’s objectives are met?
- an action programme to meet the requirements of clients, reflect demographic or other trends
- description of how the business may need to develop if it is to respond effectively to a changing business environment e.g. organisational structure, systems and skills
- intangible issues, such as image and reputation.

*Operational Resources*

A qualitative as well as quantitative evaluation of resources – other than staffing and finance (considered in other section(s) – needed to fulfil the operational objectives of the business. These will include premises, transport, ICT systems, other plant and equipment and information (including market intelligence, databases and proprietary knowledge).

*Finance*

Effective financial control will be essential to avoid business failure. This section will include the essential elements of accountancy processes and financial factors and targets

(normally over a three year period) including estimates of expenditure and income, charging policies, cash flow, capital programmes and financing and budgets.

### *Performance Review and Revision*

Systems for monitoring progress against the plan, comparing performance against targets and success criteria and of reviewing the plan itself. There are various types of review and revision – frequent monitoring and running adjustments, reactions to unpredicted occurrences and comprehensive annual review and revision. Systems may be described to monitor expenditure, income and other budgetary control, output returns, non-productive time, employee absence and turnover and analysis of customer complaints and of customer opinion surveys. There should be frequent reporting to the Board. Consideration might be given to the appointment of independent directors.

### *Risk Assessment and Sensitivity Analysis*

All projects are subject to uncertainty and a degree of risk, e.g. inflation, fluctuations in demand etc, which is why it is essential to build a risk management assessment into the financial projections. Sensitivity analysis will help to determine the most robust options. By identifying the main variables and uncertainties in a project, assessing their cost implications, including any losses of income, and reviewing the potential range of feasible outcomes, sensitivity analysis should establish which options will be able to offer the flexibility to cope with change while still retaining an ability to deliver the required option. Risk and uncertainty will never be eliminated and so any assessment should also identify the planned management responses for dealing with each of the main risk factors.

### *Supporting Appendices*

This may include profiles of key partnership players, market research studies, technical specifications, detailed organisation charts, legal documents such as copies of contracts, agreements, leases etc.

## **C. Developing a Successful Business Plan – Guide by PricewaterhouseCoopers**

In 1997, Pricewaterhouse published, *Developing a Successful Business Plan – a Ten Step Guide* – Pricewaterhouse (1997). These extracts are reproduced by permission of PricewaterhouseCoopers.

### *Step 1 – Capture The Interest And Imagination Of The Potential Investor*

#### ***Articulate the key investment criteria of the opportunity***

- What does the business do?
- What is its key markets?
- Key selling points/critical success factors

- Barriers to entry
- Competitive advantage

***Identify risks and how they will be managed: Outline the strategic objectives***

- Plans for developing new products
- Identify new target markets
- Detail plans for implementing this strategy

***Briefly state business's qualifications***

- What is the businesses past success record?
- What abilities do management bring to the venture?

***Present your financial projections summary***

- How much growth is expected?
- What earnings are projected?
- Relate financial projection to the strategic objectives
- Over what period of time will these be achieved?
- Present an overview of sensitivities

***Indicate the amount, form and use of finance***

- How much finance is required?
- What will the money be used for?

***Step 2 – Your Capability To Offer Genuine Insight***

***Provide a history of the development of your business***

- Date and form of incorporation
- Major acquisitions and disposals, creating the group in its current form
- What are the major accomplishments of your business?
- What setbacks have you met?

***Describe the industry in which you operate***

- What is the size of the industry?
- Who are the major participants in the industry? (Competitors? Market leaders? Suppliers?)

- What factors are important to success in your industry?
- If available, what do published forecasts say about the future growth and profile of the industry?
- What fashions, legislation or environmental trends affect your industry?
- What barriers to entry exist?
- How do macroeconomic issues effect the industry?
- Discuss trends in corporate activity in the sector and prices paid for business (this helps investors formulate and evaluate exit potential)

### ***Step 3 – Analysis That’s Sharp Enough Cut the Competition***

#### ***What is the state of your market?***

- Show that a market exists for your products or services
- Show you understand market forces and have the abilities and resources to supply and market effectively
- Offer a realistic estimate of potential market share based on sound assumptions
- Give a concise, realistic appraisal of the competition – use charts if they will get the information across more effectively (including SWOT analyses)
- Don’t knock your competitors unjustifiably – show how you can achieve sales goals despite competition

#### ***Describe your customers***

- Who are they? (Individuals? Manufactures? End users?)
- Where are they located geographically?
- How sensitive are they to price, quality and service?
- Who buys or expresses an interest in the product?
- Expand on how you will approach entry to market advertising expenditure, direct marketing etc.
- Remember your gain in market share lost by a competitor.
- What is the competitive edge of the business?
- Outline the geographical focus of your selling effort.

#### ***Step 4 – Will This Product Double Their Money?***

##### ***Present the product well***

- Use charts, photographs or drawings if you think they will help
- Describe advantages clearly and avoid too much technical information
- Consider use of an appendix for highly technical explanations

##### ***Describe it succinctly***

- What need does it fulfil and how does it relate to the market place?
- What features make your product unique? (Cost? Technology? Versatility?)
- Is it patented or copyrighted?
- How is your product perceived in the industry?
- Compare prices of competing product.

##### ***Describe product development***

- How fully developed is it? (Working model? In production? In use?)
- What needs to be done next – will finance be used on product development?
- Are there opportunities to expand the product line?
- Are additional specialist staff required to continue the development?

##### ***Consider brand issues***

- Discuss intellectual property protection
- How valuable is your brand in the market?
- What impact will branding have on the success of the product?
- How much will the branding costs be – is it a worthwhile investment?

##### ***Discuss competitive products on the market***

- How do they compare in quality and feature with your product?
- Articulate your own pricing policy
- Why do customers buy competitors' products?
- What pricing strategies are pursued for these products?
- Is it normal to pay commissions or offer other discounts?

### ***Step 5 – Yes It Does Run Like Clockwork***

#### ***Describe the production process***

- How will critical elements be controlled? (Bottlenecks? Quality? Delivery?)
- To what extent are you dependent on key factors? (Suppliers? Materials? Skilled Labour?) How are these issues being addressed/are they available?
- What make or buy decisions are involved?
- What raw materials are required?
- What is your relationship with suppliers?
- What is the production capacity? Is it sufficient for the future?
- Discuss contractual relationships with suppliers
- Discuss quality assurance procedures
- Discuss approach to solutions of production problems
- Are there any key processes that give you a competitive advantage?

#### ***Evaluate your plant and equipment needs***

- What are your facilities and equipment needs?
- What future additions will be required for expansion and how much will they cost?
- Outline the ongoing capital maintenance requirements
- Is there a need to rely on sub-contractors?
- Outline capital expenditure needs going forward
- Discuss potential for asset financing opportunities

#### ***What are your needs for premises?***

- What are your existing premises and where are they located?
- Are the existing premises suitable for your needs?
- Do you need additional premises?

### ***Step 6 – Your Cue To Blow Your Own Trumpet***

#### ***Identify Key management personnel and their backgrounds***

- Who are the key managers and what have they accomplished in the past?

- What are their goals for the organisation?
- Is there a balance of skills among the members of management (marketing, research, finance, administration)?

***Be frank***

- Openly discuss the strengths of current management
- Indicate what additional skills will be required as the venture grows
- Include full profiles of key individuals and an organisation chart in appendices
- Highlight industry expertise
- Highlight previous roles where money was invested by institutions
- Individual weaknesses should not be identified – team weaknesses should be considered and ways of addressing them identified

***Discuss the structure of the organisation***

- How are responsibilities distributed?
- Try to demonstrate that management isn't a one-man show
- What additions to management are anticipated?
- Show how the board will function

***Describe the role of any outsiders in the venture***

- Are there to be any non-executives on the board of directors?
- What skills will they bring to the organisation?

***Discuss personnel requirements***

- What are your employee needs?
- Discuss any particular trade skills needed
- What are your labour costs, including benefits?
- How will you attract sufficient, suitably qualified employees?
- What is the state of your industrial relations? Financial commitment from management will be expected.

### *Step 7 – This Is How We're Going To Get There*

#### ***Show how the strategy will work***

- How does the new strategy relate to the existing strategy?
- The strategy should build on specific competitive advantages
- Ensure internal consistency
- Co-ordinate figures with those in other Sections
- Show that the timings are realistic
- Why has it not been done before?

#### ***Outline the strategy in respect of:***

- Capital expenditure program
- Staff Recruitment
- Product testing
- Contacting distributors or licensing product
- Marketing
- Selling
- Accounting functions
- Obtaining and processing orders
- Protecting competitive advantage

#### ***Timetable or identify key points***

- Expected completion dates
- Milestones

### *Step 8 – And All The Figures Add Up*

#### ***Clarity and presentation***

- Show the careful thought that the financial projections and the assumptions have been given
- Document your assumptions explicitly making reference to market intelligence and market share projections (this may be best in an appendix)

- Include a commentary on the financial projections
- Avoid too many spreadsheets – be clear and concise – but use appendices where necessary

***Include historical statements***

- If possible include audited financial data for the past two to five years and relate projections to historical information

***Present financial projections***

- Prepare projected income, cash flow and balance sheets for the next three to five years (monthly for 1st year, quarterly thereafter – if practical)
- Model the impact of capital expenditure, fixed costs and R&D on the cash flow
- Include a break-even/sensitivity analysis, identifying the split between fixed and variable costs
- Include and identify as such a contingency element (but do not be too prudent so as to diminish management equity share)
- Explain the dynamics of profit to cash flow conversion
- Identify key value drivers and the impact these drivers have on profit and cash flow
- Model realistic/practical sensitivities

***Step 9 – I Just Couldn't Put It Down***

***Get the basics right***

- Punctuation, spelling and grammar should be 100% correct
- Make sure the document is checked through for errors by several people

***Make it readable***

- Keep it in the style of one writer
- Edit vigorously to cut waffle and present ideas more sharply. Keep paragraphs short (a few sentences each)
- Only use jargon if there is no other way of expressing yourself.
- Explain technical terms and issues clearly.
- Give the argument a clear logical flow

***Present it well***

- Avoid design gimmicks
- Avoid extravagant production techniques
- Number pages
- Ensure overall clarity
- Differentiate headings from sub headings
- Don't cram more than 350 or so words onto a page
- Use appendices to contain more detailed material where appropriate

***Step 10 – Every Last Item Adds***

***Supporting your case***

- Profiles of key management personnel (including track record and brief CV)
- Market research studies
- Photographs or drawings of the product
- Detailed technical specifications/patents
- Organisation chart
- Letters of commitment from potential customers and suppliers
- Plant layout
- Press coverage about your business and its operating environment
- Detailed financial models

## Annex C: State Aid

1. If the State (this includes local authorities) provides aid that affects intra-Community trade and distorts competition by favouring certain undertakings or the production of certain goods, this could constitute unlawful state aid. As a broad indication, the giving of a loan at a rate of interest below the Commission threshold (i.e. at a non commercial rate), equity investment on less favourable terms than the private sector (e.g. in terms of risk and reward), grant funding, guarantees, provision of vehicles, facilities etc, free of charge could all amount to unlawful state aid. In practice the test of whether a measure affects intra-community trade is very easily satisfied.
2. It is particularly important to be aware of the situations in which state aid may be an issue, as the European Commission has the power, in cases of unlawful aid, to halt payments and to order repayment of aid already paid, with interest. Not only is this politically embarrassing, but it is also potentially very disruptive and damaging to the recipient of the aid in question.
3. There is no definition as such of state aid. Article 87(1) of the Treaty establishing the European Communities ('the TEC') sets out four elements all of which must be satisfied if a measure is to constitute state aid. These are:
  - The aid must be granted by the state or through state resources;
  - The aid favours certain undertakings or the production of certain goods;
  - The aid affects trade between Member States; and
  - The aid will distort, or has the potential to distort competition.
4. It is often very difficult even to establish, in any case, whether these four elements are met. Although there is no definition of aid in the TEC, examples of aid might include subsidies, loans on preferential interest rates, guarantees on especially favourable terms, provision of goods or services on preferential terms and indemnities against operating losses.
5. Other rules set out both within the TEC and within separate guidelines, frameworks and regulations produced by the Commission may apply to a measure – taking it outside the Article 87(1) elements, or exempting it altogether, provided always that specific requirements are fulfilled. Special rules apply to particular sectors and to aid for particular purposes, for example, aid for training, for small or medium-sized enterprises, or for enterprises entrusted by the state with a 'public service mission'. These rules are complex and even if the criteria for their application are satisfied, notification of the measure in question to the Commission may still be mandatory.
6. As the rules governing state aid are not straightforward, it is essential to consider at the earliest possible stage whether a scheme will present problems and to obtain specialist advice. If the Commission has to be notified, this is a long process and can take many months. The earlier the issue of state aid is addressed, the more likely a solution can be

found: whether through re-structuring a scheme to avoid problems, or by obtaining Commission clearance in sufficient time for its implementation.

7. Queries on the interrelationship between local authority trading and the state aid rules can be directed to the state aid team in DCLG. Useful guidance is also contained in the DTI booklet 'European Community State Aid', which is available on the DTI Website: **<http://www.dti.gov.uk/europe/stateaid>**.