Report for:	Scrutiny Committee
Date of Meeting:	18 December 2023
Subject:	3 Rivers Development Ltd – Working Group on behalf of Scrutiny Committee
Working Group Members:	Cllrs. Gordon Czapiewski, Andy Cuddy, Rhys Roberts and Gill Westcott
Supporting Officer:	David Parker, Democratic Services and Policy Research Officer for the Scrutiny Committee
Exempt:	None which are Exempt from publication under paragraph 3, Part 1 of Schedule 12A to the Local Government Act 1972 (as amended) as it contains information relating to the financial or business affairs of any particular person (including the authority holding that information)
Wards Affected:	All
Enclosures:	None

Section 1 – Summary and Recommendations

‘Those who do not learn history are doomed to repeat it’, wrote the philosopher George Santayana in the last century. In the spirit of that thought, upon the decision by Full Council to move to close its wholly owned subsidiary company, 3 Rivers Developments Ltd, the Scrutiny Committee agreed to undertake a Lessons Learned Exercise.

The Scrutiny Committee agreed to set up a Working Group to examine documents and interview some of those involved and to report back. That is the purpose of this report. It should be noted that within the time constraints the working group has not been able to interview every stakeholder of potential interest nor examine every single document from the previous 7 years related to this topic. However, all the relevant material was made available, including documents considered in part 2 linked to commercial confidentiality, council minutes, internal and external reports and various emails and other material that had been used to brief members over the years.

For Noting only

Recommendations that could be considered for Cabinet / Full Council if at any time in the future, the setting up of an SPV was being considered:

1. **When setting up any commercial Special Purpose Vehicle (SPV) in future, ensuring the relevant skills and experience required at board level is indispensable. This should include at least two external directors with specialised skill sets unrelated to the Council.**

2. **Setting up such a commercial SPV should not be undertaken unless members are fully in accordance not only with the objectives of the enterprise but with the necessary distance from commercial decisions required by the shareholder /lender role.**

3. **When setting up a commercial SPV, it should be treated as a commercially independent subsidiary company and seek independent banking/financial advice on the viability of the business plan.**

4. **A commercial company such as an SPV should be audited by an industry-specific independent commercial auditor as a condition of any loan. Cabinet should discuss the structure of any loan to agree minimum safeguards and security.**

5. **Public interest regeneration objectives for particular sites should be separately funded from non-commercial sources, for example by the offer of a grant to attract developers. Putting the work out to commercial tender is essential, even where a Council-owned company bids.**

6. **When investments are made by MDDC, seeking higher returns than are available by market lending is acceptable if the risk profile of those investments is aligned with the preferred risk profile of the Council.**
7. **Any future SPV which undertakes public sector work should have a Teckel and Non-Teckel structure.**
8. **Establishing trust between stakeholders, including elected members, delivery agents/companies, contractors and the public, is a precondition for successful delivery of development projects.**
9. **An agreed exit strategy and decision threshold for exiting from a SPV needs to be clear and in place from the beginning.**
10. **When discussing any future SPV, regard must always be had to the reputation of MDDC as well as the SPV.**

Section 2 – Background

In 2017, MDDC resolved to take advantage of a national change through the Localism Act of 2011, which allowed local government to develop new income streams to supplement revenues and agreed to establish a new property development company to this end. A report produced for MDDC in March 2017 presented a case for the creation of a wholly owned development company whose role would be to build, rent and sell both residential and commercial properties to create a new income stream.

2.1 The Council consulted the Local Government Association (LGA), took legal advice and visited other councils undertaking commercial property development. It set up a new company, 3 Rivers Development Ltd (3RDL) which was formally incorporated with a board initially comprising elected Council Members and a small number of Council Officers.

2.2 It should be acknowledged that the decision of the Council to exploit commercial opportunities through the setting up of a new development company was not universally supported by all members.

2.3 Funding for the new company was provided by MDDC surplus treasury reserves with a commitment to fund up to £20M at a return of 4½ % over base rate. Funds would be agreed on a case-by-case basis with the development company producing project business cases, financial projections and risk assessments and other documents as required. In the absence of a track record, other sources of working capital for the company were considered likely to be prohibitively expensive or simply unavailable.

2.4 Initially, the legislation allowed councils to look at investments anywhere in the country but a subsequent change to Government guidance restricted councils to operating in their own areas.

2.5 The board of the new company initially comprised an elected Cabinet Member, an officer seconded from their previous housing and property role, and the Council's chief financial officer in addition to one other director. Officers were not personally remunerated by the company and received no personal benefit for this. Their time was recharged to the company by the Council prior to the company employing its employees directly.

2.6 Following independent legal advice and observing good practice, a formal shareholder agreement was drawn up between the company and its lender MDDC. Three Rivers Development Limited was incorporated in April 2017.

3.0 Terms of Reference

The working group was set up by Scrutiny Committee on 30th October 2023 to investigate and write a 'Lessons Learned' report on 3RDL, to ensure that opportunities were taken, both to learn from the past, and to ensure better, more informed decision-making in the future. The questions from the Terms of Reference are included in Appendix 1.

3.1 The Working Group broke the analysis into three areas;

- Inception and Start up including; Original directions from Government, Outside consultation, legal advice, Company Incorporation documents and minutes of Council meetings.

- Operational Governance including; Establishment of a new Board, Shareholder Agreements, Loan Agreements, and financial projections, MDDC Meetings to approve actions, Risk Management, Planning Applications.

- Performance and compliance, reporting and monitoring: including the comments and recommendations of formal independent specialist advice commissioned to investigate and improve company performance and financial stability.

3.2 The Group reviewed;

- Council minutes,
- Cabinet minutes,
- Scrutiny Committee minutes,
- Audit Committee minutes,
- E-mails from stakeholders involved,
- Responses to Questionnaires sent out,
- Internal MDDC Reports,
- External Reports, including
- the Bevan Brittan Presentation, Advice Notes from Anthony Collins Solicitors, Strategic Review from Bishop Fleming LLP, Grant Thornton, and the financial viability review from Francis Clark Accountants

- The group also spoke with individual stakeholders.

4.0 Inception and Start Up

In 2016 Central Government was encouraging local authorities to identify other sources of income, including commercial operations allowed for in the 2011 Localism Act. Other councils were taking advantage of the Act. After discussion informally on the potential possibilities of utilising these new freedoms, the S151 Officer was requested to bring a report to Cabinet outlining the advantages of using an SPV to generate new revenue streams to offset cuts in local government budgets and recommending further research into this opportunity. MDDC had at that point reduced its spending commitments by over £3M annually as a result of the "Austerity Programme". The need for more affordable housing was also identified in this initial exploration, though it was always intended for 3RDL to rent or sell housing units on the open market.

4.1 Legal and accountancy advice was taken at the time, but no advice was sought from an independent commercial or banking lender as to the structure or viability of the business plan. Such advice may well have recommended a more specific shareholder agreement and a different loan agreement structure as subsequently recommended in independent reports.

4.2 Specialised commercial property development skill sets at the inception would have significantly strengthened the board.

4.3 Initially the company was relatively successful in securing sites across the region but a national change in Government guidance resulted in significant unexpected and unbudgeted additional costs and consequences as it withdrew from its commitments outside the Council's area. This significantly curtailed the business opportunities available and negatively impacted on long-term commercial viability.

4.4 MDDC always envisaged that 3RDL should take on the difficult site at St George's Court. This was a decision influenced by political considerations regardless of the fact that anticipated returns, though positive, were low.

5.0 Operational Governance and risk management

5.1 Initially the governance set up for the company was 'light', in accordance with its small size, and inexpensive. The board, as described, included two acting officers; one with housing/property expertise and one from finance, plus a cabinet member with property experience. The shareholder function was in practice exercised by the Cabinet on behalf of the Council, rather than by a defined representative or shareholder committee. Named officers acted as the shareholder's representative to undertake day-to-day liaison with the company as required.

Already by 2019 the Council considered the financial risks arising from its exposure to losses by 3RDL and commissioned a number of Advice Notes from Anthony Collins Solicitors (ACS), concerning the adequacy of its governance arrangements and potential processes for closing the company.

- The advice notes provided by ACS between December 2019 and February 2020 called for greater clarity in the Shareholder agreement and Loan Agreements, and the addition of security to those loan agreements, as well as changes to the Articles of Association. These recommendations were fully accepted and implemented.
- They noted that salaries of existing company employees should not normally be expected to increase by more than RPI. The requirement for Council agreement for such increases was included in a revised Shareholder agreement.
- They also noted potential conflicts of interest for Board members whose terms of employment required them to act in the interests of the Council, and they recommended that officers be relieved from these terms when, by virtue of being Directors, they were legally obliged to act in the best interests of the Company. It asked the Council to consider the recruitment of one or more non-executive directors with specific skills in property development as part of the recovery plan if the Council decided to continue with the company. This recommendation was also accepted and implemented in 2020 when a new Finance Director and non-executive director joined the board. These additional costs imposed on the company were not included in the original business plan.

5.2 Risk management

By definition, the culture in both organisations is fundamentally different. Businesses accept taking risks, whereas a council is risk averse. The separation between 3RDL (commercial enterprise) and MDDC (Political body and lender) was never wide enough to enable the Board of 3RDL to take timely, independent, operational decisions.

Early in the life of the company, it is unclear how risks were recorded and managed. Risk reports were presented to the Council, via Cabinet. It is unclear to what extent they were read and understood in some of the cabinet discussions.

External reports called for improvements in controls and procedures to mitigate risk, and in performance monitoring and reporting. There is acknowledgment of a good standard of risk management on several other counts, but it was noted that ‘the risk appetite for the company may differ from that of the Council’.

In 2019 it was reported that the Authority’s risk register reflected the risks to the company. One of the key risks identified was 3RDL undertaking too few projects (to cover its overheads and generate enough profit). The Council could have had a key role in mitigating the risk through its own development activity pipeline. It is debateable whether all stakeholders, including elected members fully understood this possibility, and the severity and nature of the risks to the company and MDDC.

Following an external report, in May 2020, by Bishop Fleming LLP, a crucial decision faced the Council. The 'Strategic Review' looked into the financial outlook for the company and identified the only strategy for the Company to make a positive contribution to Council finances involved continued long-term support to the company but with higher levels of risk associated with new projects. The report noted that by limiting the company's projects to current work already under way, or to current projects and those in the pipeline, this would eventually lead to insolvency; however, the Council's overall exposure to debt would be lower. Regarding the possibility of long-term investment by the Council – the only strategy that would bear a positive return – the Bishop Fleming report remarked that the potential return of around 12% by March 2026 was in their view, not that substantial, given the level of risk involved and timescale required. 'However, this is probably the better solution than the insolvency route for the Company'.

Despite the Council agreeing a further loan to the company in June 2020, relationships between all parties thereafter deteriorated. Publicly Members made no secret of their distrust of the company. This caused reputational damage to both organisations but inevitably made it considerably more difficult for 3RDL to engage and retain contractors resulting in a further loss of public confidence in the company.

Following an external report in 2021 it was noted that the Corporate Risk Register was not effective as a management tool; risks needed to be identified in a timely fashion and more fully described, with risks owned and mitigation strategies put in place for each, with residual risk assessed. The company then introduced risk registers for each project, which were regularly updated. It is unclear whether risks arising from reputational damage due to severe criticism at Council meetings and in the press were seriously addressed at the time, or whether subsequent measures to mitigate these and the Covid-related risks were undertaken.

6. Company performance and monitoring

Initially reports were made to Cabinet every six months in narrative style, identifying projects under way, progress and anticipated returns for the company.

In November 2019 an external report and Governance Review for the Council recommended that key performance indicators be used in reporting and monitoring. An external Follow-Up report in February 2021 repeated the recommendation for greater focus on certain key indicators. Reporting against targets was incorporated in the business plan by May 2021.The report recommended that the Company's accounting procedures should fully allocate overheads to all projects. All projects other than St Georges Court showed a projected positive return, however, not all costs were factored in. Therefore, Cabinet members may not have fully understood the financial projections presented. The introduction of a requirement for the Company to seek Cabinet approval for all projects over £1M reduced its agility in the market to compete for potential profitable sites even further.

In 2020 the company was asked to make quarterly reports to cabinet, and subsequently, monthly, imposing a considerable additional administrative burden on management. Major decisions had to wait for cabinet consideration, sometimes resulting a delay of weeks. Further, a planning application from the company was refused by the Planning Committee, in a manner which, on appeal, was found to be ‘unreasonable’ with costs awarded to 3RDL. These difficulties understandably took a toll on the company’s overall performance.

7.0 Responses to Questions from Terms of Reference

7.1 *While performance and financial risks were regularly considered, were these used to genuinely inform debate and decision making?*

Performance and financial risk management were used to inform debate and decision making at MDDC. Risk registers for the company and for the Council were regularly considered. Initially registers were not always maintained in a timely way or used to deploy mitigation strategies. Risk management improved over time. However, the mismatch between the company and the Council’s attitude to risk hampered its operation, and Cabinet seemed not to grasp the risk to the company’s reputation arising from its own words and behaviour.

As the company developed there was a requirement for additional reports because of the deteriorating relationship and lack of trust between MDDC and the board of 3RDL. This resulted in a loss of agility the company had previously developed. This added to the company’s costs and created additional significant delays.

7.2 *The committee has heard that the tone of Council debate was not always as respectful as members may have liked. The feedback from almost all members of that time was that the whole thing as a subject became toxic; as a collective, members complained of the abusive and disrespectful language used in debate, and individual members complained of bullying language and tactics. This resulted in support being brought in from the Local Government Association (LGA). How much, or how badly, did this context impact on the quality of debate and/or the quality of decisions?*

There is ample evidence of the poor relationship which developed from 2019 onwards between the company and the Members. The aggressive critique which some members levied against the company and those who were striving to improve its financial performance, undoubtedly increased the reputational damage suffered by the company leading to difficulty in maintaining contractors, and resulted in a degree of professional trauma.   It cannot have favoured open discussion in Cabinet to improve management and performance.

The Grant Thornton Report 2021-22 speaks of weaknesses and ‘risks relating to the Council’s conduct of its role as the Company’s Shareholder including its governance and oversight of its arm’s length body, as well as a breakdown of normal good relations between key officer and member groups, both of which are key to effective decision-making.'

7.3 Cost and other implications of governance challenges.
There are some interesting examples of governance challenge and tension; whether these be linked to the planning committee refusing to determine a planning application because of the applicant, the Council's own company being awarded costs because of the unreasonable conduct of its parent council, or the shareholder declining to make timely decisions. All had cost and consequence. Navigating these governance challenges was always going to be required in one way or another, but in a 'chicken and egg' metaphor, did these governance challenges come from an underlying lack of confidence/understanding of the relationship between the two entities, or did an increasing lack of confidence or hesitancy come from experiencing these types of challenges? Could this have been mitigated better / more effectively?

Some of the comments concerning Company governance arising from external reports early in the life of 3RDL were accepted by the Council as constructive, and recommendations of these reports were implemented, at some considerable cost to the company. However, greater independence from the outset between MDDC and 3RDL could have facilitated more effective governance and improved decisions.

More effective governance of the SPV from the outset would have included:

- A more effective shareholder agreement
- More flexible approval processes
- Greater appreciation of operational independence of the SPV
- Avoiding perceived conflict of interests
- Greater buy-in and understanding from the Members of the ambitions and aims of the company

We believe the difficulties in governance could have been mitigated better, not only by more open but less acrimonious discussion, but by an earlier introduction of additional specific skill-sets within the company, providing for a higher degree of confidence and trust on the part of the shareholder, allowing the company to make more timely commercial decisions.

7.4 *Did the Council exercise the correct level of control over its company, and when exercising 'control' were the subsequent commercial impacts always considered? How could this tension between profit ambition and Council ambition be better managed in future?*

7.4.1. As time went on, the increasing control exercised by the cabinet over the company's plans and decisions entailed considerable and uncalculated costs to both the company and MDDC. It was, in effect, counterproductive. This seems to have come, to a degree, from a failure to understand the close connection in financial outcomes between the Council and the company, and the degree of necessary separation required in decision-making. For example;

In early 2022, the government ruled that Special Purpose Vehicles like 3RDL could not invest outside their area. Previously committed effort and expenditure investigating potential projects outside the area was therefore lost, and the company was further handicapped by the lack of viable sites in its reduced operating area.
In our view, the Council imposed too narrow an interpretation of HM Treasury's (HMT) "Local Area" requirement and could have challenged HMT for a wider interpretation which may have increased the area to "commutable to Mid Devon", rather than following such a cautious approach to the new guidance.

Cabinet chose to limit new projects, and in the autumn of 2022, instructed the company to withdraw its bid for Social Housing at the Post Hill site. The company's ability to make a profit was thus further compromised. Post Hill had formed part of the original business plan. 3RDL would have been the constructor and been paid on validations, resulting in considerably less risk in this project.

7.4.2. There seemed to be some confusion about the role the Council occupied as a shareholder of the company and its role as the company's lender. By operating greater and greater involvement in the company's operations, it lacked the clear objectivity required to deliver agreed objectives.

7.4.3 As mentioned above, the degree of Council control reflected the limited appetite of the Council for risk, which with hindsight may have indicated that a development company was not the most appropriate form of commercial enterprise for the Council to initiate to supplement its income. Property development necessarily entails decisions involving risk, and indeed the commercial impacts of increasing levels of control over the company seem not to have been fully taken into account. It is not clear whether better preparation for relationship with a commercial enterprise for councillors, particularly in the atmosphere which developed subsequently, could have mitigated against the damaging consequences of its controls, though perhaps were arms-length commercial enterprises ever again to be considered, improving the understanding and expectations of members would seem advisable. There is nothing in our conclusions which would suggest the Council should not seek local investment opportunities providing a higher rate of return than lending on the market, but investments with a lower risk profile would be more suitable.

7.5 *With respect to the development St George's, how much of the current position has been down to market conditions and economic shocks, and how much has been down to the performance of the company/Council?*

It is accepted by all parties that changes to market conditions, one being huge increases in raw material costs, and the challenges of the Covid pandemic combined to significantly damage the profitability of 3RDL. This could not be foreseen and in our view was not wholly down to the performance of the company or the Council.

The requirement for 3RDL to fulfil the political manifesto that the St Georges site should be developed was a politically led decision. The site would not have been committed without political pressure due to its geographical and design complexity, additional potential operating costs and projected low returns.

Other factors in the outcome for St Georges Court included the withdrawal from Knowle Lane, precipitated by the removal of part of the site from the local plan. This, had several consequences:

- The contractor made allowance for losses on St George's Court to be offset from future profits made from Knowle Lane.
- When Knowle Lane was cancelled the contractor reconsidered its involvement, leading to:
  - Withdrawal of the contractor on St Georges site,
  - Additional costs and a loss of confidence in 3RDL from the sector, leading to difficulty in engaging willing contractors.

Further, the company's operating aim to

- Build properties of decent quality, raising standards of Commercial Development within the District and achieving market-leading building standards for wider comparison,
- Use local trades / suppliers / labour / contractors,
- Put Health and Safety as a priority of operations,

potentially compromised returns and operating at a disadvantage compared to other competitors.

There appeared to be no specific agreed mechanism for local people to be kept involved and informed other than the normal Council meetings, once the development was underway. There was a public consultation on 16 August 2017, but this was following the completion of the design competition, and some of the basic parameters of the scheme had been agreed and set. Initial responses to the consultation at the time were favourable, and Tiverton Civic Society regarded development of the site as an improvement on its then current state; but there was no further formal consultation between 3RDL and the general public once the scheme was underway (as this was not a requirement).

A government document on initiating projects (citing Lessons Learnt from the Ministry of Defence) states that building trust is the key factor in successful project initiation. 'By establishing trust between different parties, whether that is within project teams, between projects and their sponsors, or between projects and wider stakeholders and delivery partners, it is easier to deliver.'

7.6 *The financial updates to Cabinet, Audit and Council were frequent and described progress and implications. Would it have helped to define acceptable thresholds for cost expansion in advance? Bearing in mind that even the latest budget agreed by full council decided to continue the work at the company's most contentious site, was there ever a point where a decision could/should have been made to walk away and cut any losses?*

Financial updates to the Council and Cabinet were numerous and exhaustive but there appeared to be no agreed strategy when St. Georges Court began failing to meet its financial projections.

A review was undertaken at the time and a proposal made to continue to support the St Georges Court development. The record shows that there were opportunities for MDDC to withdraw from the site at the time, but any decision would have had serious and long-lasting consequences both financially and reputationally to MDDC

- Cabinet 11 June 2020 - “The Leader outlined the contents of the report, and a full discussion took place including: Continued support for the company Directorships and appointments Measures to protect the Council’s financial and legal interests Governance arrangements with regard to current and future developments”
- Council 6 January 2021 – Motion 565 “This Council agrees that members must have independent and expert advice on all the options open to the Council about the future of 3RDL and that this advice be made available to all members of the Council at the same time as the new business case is presented.” This was not approved by Council.
- Cabinet 31 January 2023 – financing was approved, with agreement to “Instruct external financial and legal advice should a different scope or direction be considered.”

Each time that option of terminating the development of St Georges Court was considered, the costs appeared to be considerable. The risk of potentially increasing future losses with the prospective reputational damage did not persuade the Council to take the option to close the company.

One mitigation strategy for the risk of failure would have been to agree a phased development schedule, in which each new phase would be based on pre-sales. However, this was not possible for the St Georges Court site. The geography and design necessitated a commitment to complete the build from the outset. Had phased building been possible at this site, that would have helped both mitigate the financial risk and sales.

The particular nature of the St Georges Court site and a lack of interest from other contractors in the market resulted in 3RDL, with the support of MDDC, taking on the commitment to develop the site. The opportunity to consider other competitive bids was not available.

7.7 *The Council had identified company failure (alongside reputational issues) as a strategic risk from the outset, but with numerous internal and external review points across the life of the company, was the risk of ‘owning’ the decision to wind up the company (or any specific site) perceived as greater than the risk of continuing? How does the Council manage and weigh any equivalent risk in future?*

In our view, it is inconceivable that the governing administration at the time, was not aware of the political cycle and delayed making a clear decision until further external advice was commissioned and a new administration elected.

A lack of clear political direction and internal conflict at the time, delayed effective decision making which undoubtedly affected the viability of 3RDL and the reputation of MDDC.

There was no clear exit strategy – either for 3RDL as an SPV or for the Council in regard to its funding commitment. There should have been a clear financial benchmark related to the purposes of the SPV which would trigger a withdrawal, and some consideration at an earlier stage of how project-specific risks, including delays and contractors, could be handled.

8.0 **Further findings of the Working Group**

- An early recommendation had been to set up holding companies with two subsidiaries: – a Teckal Company directed by a board of Shareholders and a non-Teckal entity able to act nimbly *(see reports to Cabinet 29 October 20).* This might have enabled the company to expand its range of potential projects.
    - When appointing Directors to any future SPV, the presence of additional specialist commercial knowledge from the commercial sector on the board should be a prerequisite. In this instance the lack of some additional specialist knowledge at board level at the formation of the company hampered its ability to take advantage of potential commercial opportunities, training Courses and visits to similar enterprises are valuable but don't make up for lack of Business Experience.
- In the circumstances that arose the choice of JCT contract resulted in 3RDL having less flexibility with contractors. With hindsight, these types of contracts may have carried greater risk to 3RDL.
- Cabinet Ambassadors appeared to do a good job in helping members understand the needs and purposes of the company. We do not understand why the role was discontinued.
- Maintaining ambassadors among members, and more participative consultation with the local community before development might, if future schemes were to be considered, pay dividends in attitudes and support.

We accept the aim of developing new and additional income streams for the Council had merit, however, with hindsight, the challenge in bringing two organisations with fundamentally different cultures together required greater thought and consideration and that challenge ultimately proved too difficult to achieve in this instance.
Examples of the difficulties included;

- Council processes and timelines were at odds with the business's need to react quickly to situations as they developed.
- Greater alignment between HRA (Housing Revenue Account) ambitions (e.g. Shapland Place garages) and 3RDL could have resulted in greater opportunity.
- Reliance on Public Works Loan Board (PWLB) meant that when HM Treasury changed the rules there was a loss of potential revenue – Early Business plans had envisaged that the business would seek work outside of the District.
- Certainly, so far as the Planning Committee was concerned 3RDL was expected to work to higher standards.
- Greater visibility on changes to planning assumptions would have at times been useful – from changes to the planning status of major sites through to

awareness of a forward pipeline of applications from the company (as the council would do with other developers where possible).

- Some Councillors objected to 3RDL planning applications in their wards, possibly on non-material grounds.

During its period of operation, genuine and committed efforts were made by those directing the company's operations to see that 3RDL delivered on its contribution to Council finances or, when this became impossible, to minimise losses. Learning throughout this period is evidenced by the fact that the 33 Recommendations arising from the Anthony Collins Solicitors and Bishop Fleming Strategic Review external independent reports (included within the 33 recommendations were recommendations from Scrutiny and Audit Committee) were implemented and embedded in company processes, as evidenced by a report from MDDC's external auditors Grant Thornton. We have also seen the report from external auditors investigating allegations of fraud and malpractice, specifically commissioned by the council to address unsubstantiated rumours and allegations at the time, which indicates that no evidence was ever brought forward that would substantiate these accusations.

In the event substantial losses were made and we have documented some of the shortcomings and circumstances that contributed to the outcome. The ultimate losses to the Council are yet to be determined following the sale of properties, which will cover at least some of the debt owed by the company to MDDC. The net losses are likely to be substantially less than the total indebtedness of 3RDL to the Council, which figure has appeared in local media as the losses.

Any loss to the taxpayer is a serious matter, and perhaps best reflects why the council's cultural approach to risk is intrinsically less tolerant than that which might be most conducive to a successful commercial entity. The conclusions and recommendations of this report are offered in the hope that, should MDDC once more consider commercial undertakings in this way, this outcome will not happen ever again.

Section 4 - Contact Details and Background Papers

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Background papers:
See Appendix below

Appendix 1 -Terms of Reference

Scrutiny Forward Plan Item – 3 Rivers – Terms of Reference

Introduction

Following the decision of full council in September 2023 to move to ‘soft-close’ the council’s wholly-owned development company, a commitment was given that a ‘lessons learned’ process would be undertaken by the council’s scrutiny function to ensure that opportunities were taken to both learn from the past and to ensure better, more-informed decision-making in the future. To be clear, the Leader of the Council has already stated that he has no intention of creating any further council-owned companies in future. However, it is the role of an effective scrutiny function to consider whether better, or more effective, decisions can be made in future.

The basis for this piece of work should be to seek to minimise duplication wherever possible of past and previous reports, of which there have been many. Numerous internal and external reports have been commissioned over the years, at considerable cost to the council, exploring both aspects of governance and finance, in addition to the regular performance and annual reports required by statute. These were received by the various committees of the time and remain part of the record of how the council managed its finance and risk exposure across the years.

The decisions related to this matter span multiple political administrations. Even the decision to wind down the company, starting in February 2023 and concluding in September 2023, span two different leaders, cabinets and councils. As such, it is important to focus on the fact that the decision to soft-close the company was a unanimous one. Whatever the differences of the past, the council has moved from a period of well-evidenced tension on this issue, to a point where it has clarity on its future and unanimity of intent. This provides, perhaps for the first time, an opportunity for genuinely reflective learning and constructive debate on areas that may have been handled better, or which could be used to guide considerations in future.

Decisions taken in relation to the company have been made by a number of different cabinets and councils, and debate, during the 2019-23 administrative term at least, was characterised by frequent change and disagreement, with many councillors (from across all parties and none) repeatedly expressing their frustration with the quality and quantity of discussion in relation to this item. Therefore, with a new administration now in majority control, there has been a commitment to moving the discussion back to a more open and reflective position, realigning the culture back to one of mutual respect and tolerance, and specifically to ensure learning from the handling of this across all administrative settings to guide better decision making in future.

Terms of Reference

The scrutiny committee accepts the work of previous internal and external auditors and reviewers, and acknowledges the efforts made by multiple administrations to ensure high quality decision-making.

However, in order to robustly meet its objectives as a critical friend, the committee wishes to exercise its scrutiny function in specific areas:

- While performance and financial risks were regularly considered, were these used to genuinely inform debate and shape decision-making?

- The committee has heard that the tone of council debate was not always as respectful as members may have liked. The feedback from almost all members of that time was that the whole thing as a subject became toxic; as a collective members complained of the abusive and disrespectful language used in debate, and individual members complained of bullying language and tactics. This resulted in support being brought in from the Local Government Association (LGA). How much, or how badly, did this context impact on the quality of debate and/or the quality of decisions?

- There are some interesting examples of governance challenge and tension; whether these be linked to the planning committee refusing to determine a planning application because of the applicant, the council's own company being awarded costs because of the unreasonable conduct of its parent council, or the shareholder declining to make timely decisions. All had cost and consequence. Navigating these governance challenges was always going to be required in one way or another, but in a 'chicken and egg' metaphor, did these governance challenges come from an underlying lack of confidence/understanding of the relationship between the two entities, or did an increasing lack of confidence or hesitancy come from experiencing these types of challenges? Could this have been mitigated better / more effectively?

- Did the council exercise the correct level of control over its company, and when exercising 'control' were the subsequent commercial impacts always considered? How could this tension between profit ambition and council ambition be better managed in future?

- With respect to the development St George's, how much of the current position has been down to market conditions and economic shocks, and how much has been down to the performance of the company/council?

- The financial updates to cabinet, audit and council were frequent and described progress and implications. Would it have helped to define acceptable thresholds for cost expansion in advance? Bearing in mind that even the latest budget agreed by full council decided to continue the work at the company's most contentious site, was there ever a point where a decision could/should have been made to walk away and cut any losses? (See final line of query, which feels pertinent to inform thinking in future.)

- The council had identified company failure (alongside reputational issues) as a strategic risk from the outset, but with numerous internal and external review points across the life of the company, was the risk of 'owning' the decision to wind up the company (or any specific site) perceived as greater than the risk of continuing? How does the council manage and weigh any equivalent risk in future?

Conclusion

In summary, a comment during the debate at full council made the observation that 'it has taken a change of political makeup to change the direction of travel', and while it might be easy to comment on the challenging political balances of the time, it is nevertheless the role of scrutiny to look in more detail at what can be learned from this episode in order to consider whether more effective decisions can be made in future.

For further Reference please read – Government Legislation

1. Localism Act 2011
2. HMT-PWLB (Public Works Loan Body) - Change of Rules