

## **Cabinet – 11 May 2005**

### **Officer's advice on the scrutiny proposals on Neighbourhood Resource Centres (NRCs)**

#### **1. Purpose of the advice note**

1.1. Following consideration of a report concerning the development of NRCs on 2 March 2005, Cabinet resolved:

- (1) To agree that a sustainability plan, covering a 2 year period up to 31 March 2007, be drawn up in consultation with the Neighbourhood Resource Centres (NRCs) to be submitted to Advantage West Midlands and GOWM by 31 March 2005, these plans must contain the framework for agreed lease arrangements with the Council.
- (2) That the relevant Local Neighbourhood Partnerships (LNPs) receive review reports on the activities of NRCs as part of the reviewing progress of their LNP plan.
- (3) That standard leases for all the NRCs be established, to include clear criteria relating to any concessions, be introduced on 1 April 2005 as outlined.
- (4) That the implementation of the preferred options for each NRC as indicated in the report be agreed.
- (5) That progress on developments at Goscote NRC be submitted to Cabinet by September 2005.

1.2. The decision was subsequently called in by the Regeneration Environment Housing and Community Safety Scrutiny & Performance Panel, which resulted in the Panel making alternative recommendations for Cabinet to consider. These were that the Council should:

- Grant within two months, the NRCs a twenty one year lease to allow these centres to apply for a range of external grants. This lease to place responsibility of day to day running costs with the NRC and external major maintenance with the Council.
- To fix the lease costs at a peppercorn rent for one year with a full review after one year.

1.3. In considering the views of the Scrutiny Panel it is importance to consider the overall context, impact and implications. Officers were requested to provide further advice as to the financial and non-financial implications of the recommendations made by Scrutiny. This note provides that advice.

## 2. Executive Summary

- 2.1. It is clear that a lack of a formal lease arrangement for NRCs has given rise to a number of difficulties. Most notably, it has prevented them from preparing robust business plans and is restricting their capacity to seek external funding. This is because external funders do not see a distinction from the local authority whilst the Council continues to carry all the responsibility for property maintenance. A distinction will only be recognised if a lease is in place.
- 2.2. However, whilst consultants have recommended that the Council introduce leases for a minimum of 21 years, this does not appear to be necessary, as leases for 15 years are likely to be sufficient for the purposes of accessing the levels of external funding that would be appropriate for organisations such as NRCs (**Table 3**). Nevertheless, leases of a minimum of 10 years do appear to be necessary from this perspective, and therefore a lease of between 10 and 15 years appears to be the most appropriate option. The Council will also then be in a position to extend a lease beyond 10 years if the NRC has demonstrated it is sustainable and that such a lease period is required to enable it to bid for external funding.
- 2.3. The financial implications of offering a peppercorn rent to NRCs at least in the short term would not appear to represent a material liability for the Council. Allowing the current (no lease) situation to continue in the medium to longer term would, however, represent a fairly significant loss of potential income to the Council (**Table 2**), which the Council could otherwise look to set aside in an endowment fund for the benefit of these organisations in the future, or use to further the Council's broader policy objectives.
- 2.4. Such a decision could also impact on the wider community and voluntary sector, as applying such a policy is likely to result in pressure from these groups to seek similar "council subsidy", thereby increasing the financial pressure on the Council's medium to longer term financial stability. This would conflict with its fiduciary duty to local taxpayers. Such a decision would also likely to be questioned by the Authority's external auditor in terms of value for money, the wider implications for corporate governance, and the use of resources aspect of the CPA.
- 2.5. Irrespective of Cabinet's final decision, there will need to be a period of time to allow NRCs to put together robust business plans, which will need to incorporate a review of the financial standing of each organisation. If the lease is not for a peppercorn rent, then consideration may also need to be given to when the lease period begins and when the first payment will fall due eg to provide a "grace" period to enable the NRCs to build up to a position where they are able to meet the payment terms. It will be important to recognise that "one size doesn't fit all" and each NRC will need to be viewed in isolation, in terms of determining its capacity to pay any lease that is levied. This could be reflected in the terms of the lease.
- 2.6. Finally, Cabinet may also want to consider establishing a working group consisting of officers from relevant services (finance, property and legal) to facilitate this process and ultimately "sign-off" any lease agreements that are put in place.

### **3. Lease Payments**

- 3.1. Cabinet resolved that the council should introduce a lease arrangement for all NRCs occupying Council owned buildings. The benefits of such an arrangement would be:
- The Council is proposing to introduce standard leases for all community and voluntary organisation – this would put NRCs on a level footing with other community organisations.
  - The arrangements will give security to the NRCs for the use of the buildings and enable NRCs to seek additional external funding sources
  - It will strengthen the Council's relationship with this sector and ensure standards and charges developed are consistently and fairly applied
- 3.2. The "formula" for lease arrangements, proposed in the March Cabinet report was that:
- I. The Council will expect the NRCs to pay 50% per annum of the full market rental value for the lease, representing a 50% reduction in the rate the Council could collect. The lease will be granted for a minimum of 4 years and a maximum of 6 years.
  - II. NRCs will be responsible for the day to day repairs of the property, services and any other costs associated with running and managing the building but not for large capital expenditure.
  - III. The NRCs will also be expected to provide for a minimum of 10% of the market rent as a "responsive repairs budget" to deal with minor repairs and maintenance
- 3.3. The Council recommended a 5-year lease for NRCs to ensure that NRCs were not being over-optimistic about the levels of external funding they could attract. The introduction of 5-year leases would also allow the Council to apply a consistent policy across the voluntary and community sector. It should also be made clear that even with an initial lease period of 5 years, the council would still be able to extend the lease period once it was satisfied that the NRCs were sustainable in the longer term.
- 3.4. Table 1 identifies the annual lease that would be payable by each NRC based upon the Full Rateable Value (FRV) of the property (and the amount payable if the 50% rule was applied):

**Table 1 – Lease Rentals**

<b>NRC</b>	<b>FRV Lease £</b>	<b>50% £</b>
Ryecroft	11,000	5,500
North Walsall	3,000	1,500
Moxley	15,500	7,750
Goscote	13,600	6,800
Willenhall	31,100	15,550

- 3.5. The report to Scrutiny noted that if the 50% rule was implemented this could cause some of the NRCs to close, as they would be unable to generate sufficient resources to meet the payments. It is clear from the Cabinet report that a number of the NRCs do generate significant income streams and have been successful in attracting external funding. Therefore, there is likely to be some capacity for some of the NRCs (eg Willenhall/Moxley) to contribute towards meeting a lease rental.
- 3.6. It is also worth noting that:
- Ryecroft NRC has “sublet” a first floor room, for the equivalent of £6,000 per annum, which is actually a higher charge per sq. ft than would be proposed by the Council. This would also be sufficient for them to fully cover the 50% charge
  - Goscote NRC has also sublet two rooms for the total of £2,760 per annum.
  - Neither of the resource centres has a lease with which to create a sublease from, therefore these sub-leases are both unlawful and invalid.
- 3.7. Whilst the sub-leases may be unlawful, if a lease arrangement was formalised, the Council could nevertheless offer, as part of the lease agreement, to recognise the cashflow implications of each NRC. For example, an NRC may not receive income from sub-lettings until the end of the financial year, and as a result the Council's terms could be to pay the lease rental once the income was received.
- 3.8. Such issues could be picked up as part of a complete financial review of NRC finances. Unfortunately, this has so far not been possible and it is worth noting that none of the reports commissioned by the Council have been able to accurately determine the true state of their financial affairs.
- 3.9. This has been partly due to the NRCs not operating a system of open book accounting. This is unhelpful, particularly given that as registered charities they are required to disclose such information to the Charity Commission. Such a request would not appear to be unreasonable if the organisations are seeking the Council's support. At this time the Council is being asked to agree to a longer lease without having all of the available information on which to base its decision.
- 3.10. As such, any decision to implement the leasing policy should include a clause that will allow the Council full access to the NRC's accounts. To do otherwise increases the Council's exposure to the risk of the NRCs not being sustainable.

#### **4. Financial implications of scrutiny recommendations**

- 4.1. There is no budgetary provision contained within the Council's 2005/06 revenue budget for either the income that would be received from these payments being made or any costs that the Council would have to incur to meet the repairs liability that would result from the agreement to be responsible for external repairs. In the current year, any additional costs would require resources to be diverted from other priority areas or balances/contingencies. In future years, extra costs would be a new budget pressure as part of the annual budget/council tax setting process within the Council's medium term financial plan.
- 4.2. The approved 2005/06 budget included use of the prudential code to begin to address the significant maintenance backlog that has built up within the Council's property portfolio. Part of this backlog can be attributed to other examples of the Council offering peppercorn rents to community/voluntary organisations, which have then not provided any resources for the maintenance of the property they occupy. This has arisen on the assumption that the Council will meet all such costs.
- 4.3. Whilst this assumption may not be unreasonable from the perspective of a voluntary organisation providing important community services, e.g. they would see first call on any income received to support those services, the issue would presumably be viewed differently if those organisations actually owned the building. In other words, they would look to put some resources aside to provide for future maintenance liabilities; otherwise they would risk the very asset from which the services were provided.
- 4.4. It is therefore not unreasonable for the Council to assume that the first call on any income generated should contribute towards these costs, and that this contribution should not necessarily be ring-fenced solely for NRCs but should act as a contribution towards these costs across the voluntary sector. This point is particularly pertinent given the following:
  - At the recent Walsall Voluntary and Community Sector conference, one of the key ambitions for the future development of the sector was having a common framework, standards and active support from all organisations
  - There have been numerous recent examples of failing boilers and leaking roofs at community centres, with a total estimated maintenance backlog on all such properties of over £1m.
- 4.5. The issue for the Council to consider, therefore, is primarily one of "opportunity cost". The original recommendation to forgo 50% of the FRV rental income effectively means that the Council would be forgoing an income stream that whilst not material in terms of its overall revenue position (particularly on an annual basis), over the life of the lease, would be a material amount.
- 4.6. This is particularly significant in light of the fact that the council has a policy-led medium term approach to budget setting and financial decision making which represents best practice. This enables funding decisions to reflect the council's vision, priorities, aims, objectives and pledges. The council's vision reflects the council's desire to be an organisation that is closely engaged with partner

organisations and local residents, with local access to services and an organisation that listens to the views of stakeholders.

- 4.7. Budget decisions are made with the intention of delivering the vision, the ten priority themes and the annual pledges within those themes. The majority of those are undertaken within the formal annual budget cycle, with others taking place throughout the year as projects and developments arise, including the need to ensure our processes and infrastructure are modernised. The identification of creative funding solutions and the need to regularise the situation relating to leases, which has evolved over several decades is an example of such a decision, and the situation with NRCs represents an opportunity to resolve it.
- 4.8. The decision therefore, from a medium term financial planning perspective, is whether any income received is available to either:
- Establish an “endowment fund” to be used to meet future maintenance liabilities across the community/voluntary sector
  - Used to support other Council priorities
- 4.9. Any variation to this policy such as basing the amount on ability to pay or forgoing the rental charge entirely would clearly reduce the amount of resources available that could be re-invested into the local community.
- 4.10. The Council would of course also need to consider the longer term financial implications and Table 2 summarises the cash flow implications of the proposals outlined above, with a detailed analysis shown at Appendix 1.

**Table 2 – Summary of Financial Implications**

	<b>21 Year Lease £</b>	<b>15 Year Lease £</b>	<b>10 Year Lease £</b>
<b>Option 1</b>			
Income “forgone” at FRV	1,933,365	1,292,480	816,195
Capital Expenditure	398,660	266,510	168,300
Revenue Maintenance	193,335	129,250	81,620
<b>Total “cost” Option 1</b>	<b>2,525,360</b>	<b>1,688,240</b>	<b>1,066,115</b>
<b>Option 2</b>			
Income “forgone” at 50% FRV	966,685	646,240	408,100
Capital Expenditure	398,660	266,510	168,300
Revenue Maintenance	193,335	129,250	81,620
<b>Total “cost” Option 2</b>	<b>1,558,680</b>	<b>1,042,000</b>	<b>658,020</b>

- The figures assume 2.1% annual inflation over the life of the lease for both income and expenditure
- The capital and revenue expenditure figures are based upon the likely maintenance requirements over the life of the lease, as assessed by the Councils surveyors

Option 1 shows the financial implications if a peppercorn rent was applied for the whole of a 21 year lease, as well as the Council funding the major capital

expenditure requirements. This would result in a total “cost” to the Council i.e. income foregone and costs of maintenance of £2.525m.

Option 2 shows the financial implications if Cabinet implement their original proposal

- 4.11. If one of the reasons for moving to a longer lease period is to facilitate NRCs in accessing external funding, then it would not be possible for the NRCs to either bid for that funding or materially change the fabric of the building, without both the consent and the professional support of the Council.
- 4.12. Option 2 would be to implement the original recommendation of the Cabinet report which would mean that the Council would subsidise the lease payments, resulting in a total “cost” of £1.558m.
- 4.13. If Cabinet resolved to grant a 21 year lease, with a peppercorn rent for one year, and then a maximum lease payable of 50% in subsequent years, this would still result in a significant amount of income being foregone over that period. This may be a valid approach but would need to be weighed up in terms of the benefit of supporting the local community. In making a decision Cabinet are also advised to consider:

a. Competing priorities

These resources could be used to re-invest in the local community or could be used to meet cost pressures in other service areas. From the Council’s perspective of allocating resources to its priority areas, the NRCs by asking for a peppercorn rent, are effectively asking all council tax payers to subsidise the activities of a relatively small number of community groups.

b. The view of the Audit Commission District Auditor Local Manager (DA)

Discussions have taken place with the DA to ascertain his view on this issue. He has commented that for the Council to implement this proposal it would need to be able to demonstrate that it has satisfied itself that:

- Does the Council have the legal power to implement such a decision?

The DA has commented that the Council needs to satisfy itself that it has the necessary powers. The most appropriate place to seek such powers would be in the Economic, Environmental, Social and Wellbeing powers contained in the Local Government Act 2000. The Council would need to identify how it sees those powers relate to the planned policy.’

- Are the proposals “reasonable” and do they represent value for money?

The Council needs to weigh up the benefits gained from supporting the NRCs in terms of community engagement with the financial cost of subsidising their activities. Whilst the DA is not in a position to offer direct advice to the Council, he has indicated (assuming the Council has satisfied itself it has the legal powers) that the 50% subsidy does not appear to be unreasonable, taking these issues into consideration. A higher level of subsidy however, may raise

questions from the DA in terms of reasonableness, VFM and risk to the Council.

The Council also needs to consider the wider dimensions of its policy making, particularly in light of the Gershon agenda, and the DA would no doubt expect the Council to be examining all areas of its activity, in terms of funding the 2.5% efficiencies required.

c. Risk

Appendix 2 identifies and categorises the main risks associated with the various proposals. The most significant risks needing to be managed are:

- Buildings not adequately maintained
- NRCs unable to pay lease rentals
- NRCs not able to attract external funding
- NRCs unsustainable

These risks could be managed by having as part of any lease, a requirement that each NRC prepares a business case which includes proposals for addressing the maintenance requirement's and demonstrates how it will become self-financing.

## 5. Other issues to consider

### Granting of a 21 Year Lease

- 5.1. The Cabinet report recommended that a lease of a minimum of 4 years and a maximum of 6 years be granted. One of the other main issues raised by the Scrutiny Panel was that this length of lease would not be sufficient for the NRCs to attract external funding.
- 5.2. Two of the main sources of funding for the voluntary sector are the Community Fund (shortly to become the Big Lottery Fund) and the New Opportunities Fund. Present guidelines state the minimum length of lease required is as follows:

**Table 3 – Example of Lease Requirements of External Funding Agencies**

Total Capital Cost of Work	Length of lease
<u>Community Fund</u>	
Less than £30,000	5 years
£30,000 - £100,000	10 years
£100,000 - £250,000	15 years
More than £250,000	20 years
<u>NOF</u>	
Below £5,000	3 years
£5,001 to £10,000	5 years



£10,001 to £50,000	10 years
£50,001 to £100,000	15 years
£100,001 to £5 Million	20 years
Above £5 Million	40 years

NB – the value is not the amount of funding applied for but the total capital cost of the work

- 5.3. Therefore, whilst a 21 year lease maybe too long in that it effectively ties the Council into an arrangement for an extended period and does not appear to be necessary to enable community organisations to access external funding, the above table shows that a strict five year lease policy will disqualify occupiers of Council-owned buildings from accessing funding from the main lottery distributor.
- 5.4. Therefore there does not appear to be a need to offer leases in excess of 15 years. This will cover the majority of applications. It will also enable the volunteer pool to remain motivated. If extensions are required the policy will ensure that the authority, as land lord, is fully consulted on proposals.

### **How NRCs fit with the development of LNPs/Strategic Partnership**

- 5.5. A key question is how the NRCs relate to the establishment of LNPs and to the development of the Council's strategic partnership: Putting the Citizen First.
- 5.6. At this time there does not appear to be any mention of any of the NRCs in any of the LNP plans. This clearly raises questions about how the NRCs are engaging with their local communities, and therefore their sustainability. Furthermore, the Council's strategic partner will be managing the properties, which presents the NRCs with an opportunity to broaden their involvement in the local community.
- 5.7. For example, the business plans that are recommended to be prepared by the NRCs could include proposals for income generation that could relate to LNP/Strategic Partnership activity such as:
- Hosting LNP meetings, workshops and events
  - Acting as "customer contact" centres to enable local communities to access Council and other agency services

### **Consultant's reports**

- 5.8. The Scrutiny Panel identified the issue that consultants have been commissioned to review the NRCs but that Cabinet's resolution differed from the recommendations made by the consultants, in particular that the NRCs were given a 21 year lease with leases starting at a peppercorn rate.
- 5.9. It should be noted that the Council does not necessarily have to agree with the recommendations made by consultants. It is also worth noting that the various reports produced have focused primarily on the implications for the NRCs and not on the impact of their proposals on the Council or the wider voluntary and community sector. From the Council's perspective, it would appear that the most

significant issue is the potential loss of income that would arise from a decision to forgo levying a lease rental. It also fails to recognise that the Council would be willing to “ring-fence” any such income for the purpose of being re-invested in the community.

### **Criteria for accessing the “endowment fund”**

5.10. To ensure that any endowment fund that is established, can be accessed fairly by voluntary/community organisations, there would need to be pre-determined criteria that was clear, understandable and equitable. The principles that would need to be included in such criteria are as follows:

- Assessed need e.g. the condition of a building relative to others
- Availability of resources – the ability of the NRC to contribute/match fund from other sources
- Affordability – total resources available in the “endowment” fund
- Contribution made – the level of contribution to the “endowment” already made

5.11. There are a number of ways this could be achieved. For example the framework already in place for the Council’s capital programme allocation and/or NRF allocations. The allocation of capital resources, for example, is based on weightings that take into consideration the following:

- the links to the Council’s vision/priorities,
- whether the expenditure is unavoidable
- whether match funding can be drawn in
- what performance measures are in place
- how it links to other plans and strategies
- what is the risk of the project not proceeding

### **Clawback**

5.12. The 2 March Cabinet report identified that the total amount of public subsidy used to set up the NRCs totalled. The majority of this was SRB2 and ERDF funding. The report identified that the main external funders (AWM for SRB and GOWM for ERDF) were keen to avoid any clawback.

5.13. For the activity in the community to be sustained, there needs to be a robust strategy in place for keeping the assets in a sound state of repair. As has been suggested earlier in this note, one way of achieving this would be to ring-fence the rental income from across the voluntary sector, to provide for an on-going, sustainable programme of repairs.

## **6. Options for Cabinet**

6.1. There are 3 options that Cabinet may wish to consider regarding the future establishment of formal lease arrangements for the 5 NRCs, as follows:

- a. Implement the recommendations proposed by the Regeneration Environment Housing and Community Safety Scrutiny & Performance Panel.**

A peppercorn rent would apply for the first year, after which time a review of future charging arrangements would be undertaken, based upon the ability to pay. As a “worst case scenario”, the future application of a peppercorn rent would result in the forgoing of an income stream, over a period of 20 years, of £1.9m.

In order to deliver a satisfactory outcome both in the short and longer term, Cabinet may also want to consider establishing an officer working group, consisting of representatives of relevant service areas, property, finance and legal services who's remit would be to take responsibility for reviewing each NRCs business plan and signing off the lease agreements.

**b. Implement the original Cabinet recommendation of 2 March 2005.**

A lease based upon 50% of the FRV of each NRC property would be payable, along with a 10% of FRV contribution towards maintenance costs. This would still result in the Council effectively subsidising NRCs by almost £1m.

If Cabinet was mindful to implement the original recommendation, it would need to provide for a longer implementation timetable, to enable the business plans to be produced, as there has been little progress during the scrutiny process.

Either option would also place the liability for major external repairs on the Council, which are estimated to be c£400,000 over the next 20 years.

**c. Implement alternative recommendations**

During the scrutiny process, there have been no firm alternative recommendations put forward by the NRCs themselves. However, one possibility would be to link the amount payable to the actual maintenance liability. Therefore levying 10% of the FRV for maintenance would raise almost half of the amount necessary for estimated major external works. Therefore a 20% levy would be sufficient to cover this liability over the time period. This would however, increase the amount of effective subsidy being granted by the Council.

Any alternative recommendation would also need to be subject to a consultation process which will result in a further delay to the implementation of the decision.

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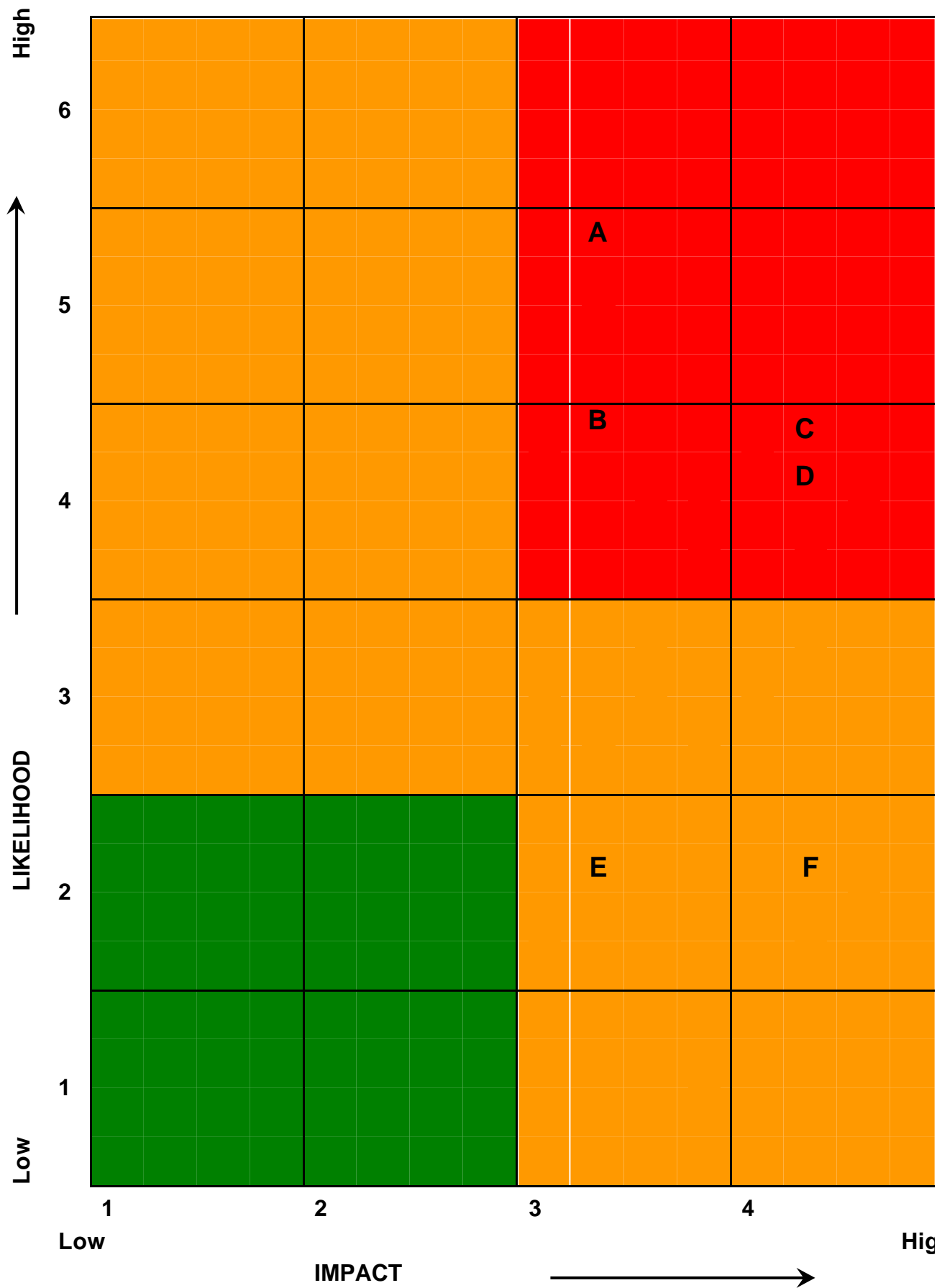
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**Neighbourhood Resource Centres  
Summary Of Estimated Costs**

<b>Year</b>	<b>Unrealised Income @ FRV</b>	<b>Unrealised Income @ 50% FRV</b>	<b>Capital Works</b>	<b>Revenue Works (@ 10% of FRV)</b>	<b>Total @ FRV</b>	<b>Total @ 50% FRV</b>
1	74,200	37,100	15,300	7,420	96,920	59,820
2	75,758	37,879	15,621	7,576	98,955	61,076
3	77,349	38,675	15,949	7,735	101,033	62,359
4	78,973	39,487	16,284	7,897	103,155	63,668
5	80,632	40,316	16,626	8,063	105,321	65,005
6	82,325	41,163	16,975	8,233	107,533	66,371
7	84,054	42,027	17,332	8,405	109,791	67,764
8	85,819	42,910	17,696	8,582	112,097	69,187
9	87,621	43,811	18,067	8,762	114,451	70,640
10	89,461	44,731	18,447	8,946	116,854	72,124
<b>10 year total</b>	<b>816,194</b>	<b>408,097</b>	<b>168,299</b>	<b>81,619</b>	<b>1,066,112</b>	<b>658,015</b>
11	91,340	45,670	18,834	9,134	119,308	73,638
12	93,258	46,629	19,230	9,326	121,814	75,185
13	95,217	47,608	19,634	9,522	124,372	76,764
14	97,216	48,608	20,046	9,722	126,984	78,376
15	99,258	49,629	20,467	9,926	129,650	80,022
<b>15 year total</b>	<b>1,292,482</b>	<b>646,241</b>	<b>266,509</b>	<b>129,248</b>	<b>1,688,240</b>	<b>1,041,999</b>
16	101,342	50,671	20,897	10,134	132,373	81,702
17	103,470	51,735	21,336	10,347	135,153	83,418
18	105,643	52,822	21,784	10,564	137,991	85,169
19	107,862	53,931	22,241	10,786	140,889	86,958
20	110,127	55,063	22,708	11,013	143,848	88,784
21	112,439	56,220	23,185	11,244	146,868	90,649
<b>21 year total</b>	<b>1,933,366</b>	<b>966,683</b>	<b>398,659</b>	<b>193,337</b>	<b>2,525,362</b>	<b>1,558,679</b>



## **Risks**

- A – Buildings not adequately maintained
- B – NRCs unable to pay lease rentals
- C – NRCs not able to attract external funding
- D – NRCs unsustainable
- E – Council not seen to be supportive of Community/Voluntary sector
- F – AWM/GOWM clawback funding