Governance, Financial and Commercial Review of Woking Borough Council

for the Secretary of State for Levelling Up Housing and Communities

May 2023

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A note on the text:
This report is comprised of two documents (Parts One and Two) that summarise the findings of two periods of investigation by the review panel in 2023: the field work for the first was undertaken in January and February, the second in April and May. The second period of investigation was undertaken due to the presentation of fresh evidence and updated reporting of the council's finances, the seriousness of which raised concerns for both the panel and DLUHC. The numbered recommendations included in this document are drawn from the first period of investigation, but remain relevant in light of the findings of the second period of investigation. The conclusions within Part Two represent the most up-to-date picture of both the council's position and the degree of support required.

Some of the contents of this report is commercially sensitive in nature and therefore certain information has been redacted.

Contents

Woking as a place

1. Woking Borough Council (WBC) is one of 11 borough and district councils in the county of Surrey. It is a modern and diverse town born out of the railway and communication revolution. Comprising 6,357 hectares, 60% of the borough is designated green belt land and large areas of the borough's open space are protected.
2. Approximately 100,000 people live in the borough and the council provides services to around 43,000 homes. Woking, West Byfleet and Knaphill are the borough's main urban and economic centres followed by Brookwood, Byfleet, Goldsworth Park, Horsell, Kingfield, Old Woking, Sheerwater, St Johns and Westfield, which have their own identities and local interests.
3. Woking is the third most densely populated borough in Surrey. The average household size is 2.49 persons, slightly above both the regional and national average. Compared to the rest of Surrey Woking has a young population, with the second highest proportion of under 16s and the second lowest number of over 65s in the county. However, in common with the rest of the country, the borough has an ageing population, with the over 65s expected to increase by 3,900, more than 20% in the next 10 years.
4. Residents are generally healthier than the English average. However, in the most deprived areas of the borough, life expectancy is approximately 5 years lower.
5. The borough benefits from excellent transport links and proximity to London makes Woking an important regional hub with enormous potential for growth. Woking has a large economic workforce. 85% of the working-age population is economically active, the second highest proportion in Surrey and well above both regional and national averages.
6. Woking has 30 elected members. The council had been led by the Conservative group for 14 years until May 2022 when the Liberal Democrats formed a new administration following the local elections. The current political breakdown (reflecting May 2023 elections) is 20 Liberal Democrats, 4 Conservative, 3 Independent and 3 Labour. At the time of the initial field work for this review the Liberal Democrats had been in control of the council for 10 months.

Background to the review

7. Throughout the summer of 2022 the Department for Levelling Up Housing and Communities (DLUHC) were in discussion with Woking Borough Council (the council) regarding the sustainability of Woking's financial position. This was due to concerns with the council's level of debt and the risk this poses to financial sustainability.
8. Following DLUHC's initial engagement, in January 2023 the Secretary of State commissioned a non-statutory review of governance, finance and commercial aspects of the council's business and appointed a review team of Jim Taylor, Carol Culley OBE and Mervyn Greer.
9. The fieldwork took place between 23rd January 2023 and 24th February 2023. During that period 73 interviews were conducted by the team and significant council documentation was reviewed. The panel were asked to undertake further work by

DLUHC at the end of April. This was due to additional council-commissioned external reports emerging, which indicated further concerning financial developments. The additional work by the panel is outlined in Part Two of this review. Jim Taylor is an ex-Chief Executive Officer of three Metropolitan Borough Local Authorities and was appointed in March 2022 by the Secretary of State as a commissioner at Sandwell Council. He also led on a Governance review of Slough Borough Council for the Secretary of State in 2021. He was a member of the team conducting a recent governance review of Northumberland County Council.

10. Carol Culley OBE is the current Deputy Chief Executive and section 151 officer at Manchester City Council. She is CIPFA qualified and has a diploma in management and is CIPFA Junior Vice President, a member of the CIPFA Council and Chair of the CIPFA Public Financial Board.
11. Mervyn Greer is a Crown Representative at the Cabinet Office where, amongst other responsibilities for strategic suppliers to HMG, is the appointed Crown Representative for Local Government Commercial and the LGA. His background is in property and built asset management in the private sector, where he was responsible for major outsourcing and property related commercial contracts. He retired from the private sector in 2016. He was a member of the team which conducted the initial statutory inspection of Liverpool City Council in 2021.

Part One: Executive Summary

12. Woking Borough Council is the most indebted local authority relative to its size in the UK, with borrowing of £1.9bn compared to a net budget of £24m. The two largest commercial schemes in the council's portfolio are the regeneration of Victoria Place in the town centre and the regeneration of Sheerwater housing stock; financing these schemes account for the majority of the council's debt. The council's historic investment and borrowing decisions are disproportionate to its ability to manage complex commercial activity and the council lacks the commercial skills and capacity to identify a longer-term strategy to resolve its commercial arrangements. This report considers the areas of leadership and governance, finance and commercial.

Strategy, governance and leadership

13. A new Chief Executive and leadership team, working with a new political administration, are making great efforts to deal with these significant issues to provide financial stability for the future of Woking. They have placed financial resilience at the heart of their priorities and now understand and recognise the significant challenges faced by the council and significant changes are underway in how the council manages its finances and governs its companies. These positive changes in the most part remain in their infancy, with concerted efforts from autumn 2022 and efforts must continue to be made to identify a sustainable solution to the council’s finances.
14. The new leadership team is essentially rebuilding most internal processes as they had not been fit for purpose. Management information to inform decision making is recognised as inadequate and plans are in place to rectify this. Financial information does not currently enable managers to be agile in their approach to departmental budgets. The constitution is being reviewed. New company governance and processes have been put in place from October 2022 to manage the companies with the establishment of a Shareholder Advisory Group (SAG). The council’s approach to procurement is being redeveloped as are its processes for change management, digitisation, and transformation. All these developments are in their early stages, nevertheless the review team recognise that these initiatives are required and have the correct direction of travel.
15. There are some very committed and talented members of staff at all levels in Woking, particularly at the senior level. New staff brought in have made a positive difference to the skills required within the council. Despite this, there is not enough capacity or capability to manage the significant number of issues the council is now facing. In reshaping the council, new skills and approaches can be built up in most areas, but this will take time that the council does not have.
16. Despite recent best efforts of the new leadership team, the council does not have the commercial skills or capacity to identify the longer-term strategy to resolve its commercial arrangements. From the historic base, the sheer scale and complexity of the investment and commercial activity of the council, means that the council will never have the capacity to effectively manage all the commercial and economic considerations which would only be enacted properly by expert investors and

developers steeped in experience for a programme of this nature. This is why the council must look to find partners to share risk and any benefit from the council's ongoing programmes.

Finance

17. Woking Borough Council has £1.9 billion of borrowing and a further capital financing requirement to 2025/26 which extends the debt to £2.4 billion. The associated capital financing costs are £62m per year. It is the most indebted council relative to its size in the UK. The two largest commercial schemes in the council's portfolio are the regeneration of Victoria Place through the company Victoria Square Woking Limited (VSWL) in the town centre, and the regeneration of Sheerwater housing stock and public realm facilities, through the Thameswey Group. These two schemes alone have accounted for the majority of the current debt level.
18. Due to the Covid pandemic and the current economic climate, the council car parking and commercial income has reduced whilst its debt repayments have remained relatively constant but are forecast to grow.
19. In March 2021, the council applied to the Department for Levelling Up Housing and Communities (DLUHC) for Exceptional Financial Support (EFS), but at that time the previous chief executive in his statement to DLUHC remained confident that the council's financial strategy was able to withstand normal economic cycles. The council felt that an injection of emergency funds would bridge a gap which would then bring their financial plan into line. In July 2021, DLUHC refused this request. At that time, the council was holding reserves which could be used to support the budget and there had been no significant evidence that services had been redesigned or altered to fit a budget envelope of similar sized borough councils. The position of the council was not based on an evidence-based assessment of the council's financial position and was optimistic.
20. It is difficult to conclude the council has complied historically with accounting best practice and the Prudential Framework. The scale of borrowing was disproportionate to the council's assets and ability to manage complex commercial activity. There was insufficient regard to the level of risk the council was being exposed to. The decisions to invest were made in line with the constitution, assessed against the Prudential Framework, the 2018/19 and earlier accounts had unqualified VfM opinions. However, given the scale of the borrowing and the fact that future risks of refinancing were not considered it cannot be argued that the approach had been prudent. The arrangements put in place for VSWL and Sheerwater were taken without an adequate assessment of the risks to the council or a full assessment of the legal considerations, including state aid/subsidy, best value consideration and the structure of the financing arrangements.
21. The leadership of the council has changed at an officer and political level since the major commercial decisions were made. The new leadership team is to be commended for a systematic and whole systems approach to establish and address the council's financial challenge and to fundamentally redesign governance. The establishment of the 'Woking for All' strategy and the iterative approach to the

Medium-Term Financial Strategy, alongside management of risk, commissioning independent advice and reviews, has established that the financial position of the council is significantly worse than the position set out in March 2021 at the time of the application to DLUHC for Exceptional Financial Support. These positive steps in the most part remain in their infancy, with concerted efforts from autumn 2022. The direction of travel is encouraging; however, time is not a luxury the council has due to its current financial position.

22. The council is probably able to set a balanced budget for the years 2023/24 and 2024/25 with the use of its reserves. This gives a possible two-year window to work on the consolidation of strategic plans to deal with the model of the regeneration vehicles. This is if all its assumptions materialise and there is not an immediate need to make provision for Minimum Revenue Provision (MRP). The current council's MRP Policy is that no provision is required to be made on £1.3 billion of council borrowing associated with the loans. The new administration has commissioned an independent review of the current MRP policy. According to the council's own calculations prior to the independent review there could be a material risk of an under provision of MRP when reviewed against the DLUHC Consultation on changes to the capital framework: Minimum Revenue Provision in 2022. This under provision amounted to £11.9 million annually in 2021, rising to £23.4 million annually when averaged over a 50-year period.
23. Whilst a balanced budget can be achieved in 2023/24 and potentially in 2024/25 using reserve balances to bridge the budget shortfall, this will not be achieved in 2025/26 unless the savings required can be fully delivered and there are no further external shocks or risks. This does not take into account any changes in MRP policy. Despite best efforts of the current leadership team, it is likely that the council will need to issue a section 114 notice within the coming two-year budget period.
24. A balanced budget for 2023/24 can only be achieved with a disproportionate use of reserves and non-recurrent funds. In setting the budget, the Section 25 report to Council in February 2023 has highlighted that there is a real risk that a section 114 notice could be issued during the upcoming financial year, if the assumptions made do not materialise.
25. A significant risk to balancing the budget is the ability to deliver the savings included in the 2023/24 budget and to deliver the target of £11m savings over a three-year period. This equates to 25% of the council budget. This will fundamentally change the services the council delivers and will require political will and a step change in activity to reconfigure services accordingly. The level of work that has recently been carried out on the budget is encouraging, but it is important the council guard against optimism bias and continue to monitor the position closely. The council does not have a history of redesigning its services or of the decision making needed to save circa £11m over three years.
26. Section 114 of the 1988 Act further requires the Section 151 Officer to report to full Council if it appears to him/her that the expenditure of the Council incurred (including expenditure it proposes to incur) in a financial year is likely to exceed the resources (including sums borrowed) available to it to meet that expenditure. In making such

assessments we advise the Section 151 Officer to look at both the immediate-term as well as at the wider sustainability of the budget and reserves position.

27. The current finance team have a wealth of experience and knowledge, but limited capacity to deliver the type of financial information that is required and there is a lack of management accountancy experience. It is recognised that the format of the financial information and reporting requires an overhaul and has not been fit for purpose.

Commercial

28. The two largest commercial schemes in Woking BC's portfolio are undoubtedly the regeneration of Victoria Place in the town centre and the regeneration of Sheerwater housing stock and public realm facilities. These two schemes alone have accounted for the majority of the current £1.9bn debt level. As a result of the complexities of the loan facilities this debt level is predicted to rise to £2.4bn within the next two years. Added to this is the complex arrangements by which the council has decided to deliver and manage these major projects, placing 100% of risk with the council and this is a key factor contributing to the council's current precarious financial position.
29. Until 2022, Woking Council's vision had been one of local and economic social regeneration which included investment in sustainable energy particularly through its community heat networks. The strategy was based on commercialisation and income generation to develop a greater degree of financial independence and to avoid service transformation. This approach was considered an alternative to taking a more fundamental look at changing council services through transformation and significant restructure, as had been the common approach in Local Government at that time.
30. During the period 2016-2019, the council embarked on an ambitious regeneration programme, funded by money borrowed from Public Works Loan Board at lower than commercial interest rates. This was used to fund a number of commercial properties within the borough and, more significantly, to support the regeneration of the Town Centre via a joint venture and through its wholly owned Thameswey group of companies for sustainable energy and housing, most notably, the plans for the regeneration of Sheerwater. The council then loaned money to the joint venture and the companies to develop the schemes. The council received a margin on some of these loan transactions. This margin, along with the rental income from the commercial priorities, contributed to the council's budget to fund services. This process was used by the council to generate funds for its regeneration schemes over several years. The council is effectively self-funding the borrowing costs through additional borrowing, which is deferring risk.
31. The loans to the regeneration companies on business cases of 50 years and over have built in an inherent dependency for ongoing capital support. Working capital support to service the debt has been provided by a 'revolving' loan facility. Effectively, the council lends money to its companies and the companies then use this money to pay back to the council. This has created an extremely high debt profile which is not backed by assets in any way matching that debt. Some companies are making

operational losses but still extending their borrowing to cover principal and interest repayment costs.

32. The council sought to bring benefits to the communities of Woking 'upfront' and in the shorter term, for example, in Sheerwater, by providing the social infrastructure of the development (leisure centre and community facilities) and social housing, before the 'profit making' element of market housing. As a result of this sequencing, development is taking place whilst the companies are in their loss-making phase of the business plans.
33. These investment and borrowing decisions leave a legacy for the council and pose the biggest threat to its future financial resilience. Although work has started, there is currently no long-term commercial strategy in place. Commercially, the council is overstretched and remains reliant on further support in the form of additional skills and capacity to continue to find a resolvable solution to its commercial position. The leadership team has put in place several initiatives and actions to get to grips with the current situation but is yet to set out a structured overarching council commercial strategy, to maximise the assets the council now holds. Until this strategy is in place the council remains open to commercial risk brought about by a piecemeal approach to challenges and opportunities the council now faces. Before confidence can be restored in the council's management of future financial risk there must be a clear commercial strategy, more robust commercial risk assessment in all business cases put forward and commercial expertise in the council.
34. The situation is well understood by the council leadership team and there are actions in place to reconfigure and have greater control over the schemes. There is an integrated service and financial framework provided by the 'Woking for All Strategy'. However, these actions appear to be taking place outside of the 'Business as Usual' of the council. This leads to the conclusion that, despite many initiatives and advice being actioned there is no overarching strategy for the whole situation under the council's control. There is a huge amount of council energy and resource (both officer and member) being expended on remodelling of business plans, financial models and programming to try to manage the relationship with their subsidiary companies and regeneration projects. The focus of the leadership team should not be distracted away from managing the council's services on behalf of its communities.
35. The justification historically within the council for the sizable investment model had been the alignment of the investments to the social regeneration of the borough. The intent and social value of these two major investments will have an impact on the borough and its ability to attract business and investment in this highly competitive region. However, the reality is that the council currently has double the level of borrowing per head of population compared to the next highest council and is struggling to set a balanced budget. The council has amongst the strongest economic vitality prospects outside of London, higher than average earnings of its population and relatively lower levels of deprivation. Therefore, the quantum of the borrowing and the scale of investments made, for the council to shoulder on its own, had been disproportionate, too large and the risk taken is disproportionate to the social impact.

36. The introduction of the new Shareholder Liaison Service and the Shareholder Advisory Group, coupled with changes made recently to the directorship of the Thameswey company, gives greater comfort that high level governance of Thameswey Group and VSWL is much improved. However, further development of reporting content notably in commercial risk analysis is necessary to underpin and fully inform decisions.
37. There had been a long-term regeneration focus without adequate attention to short term financial viability of the council and the associated risks of the scale of these investments on the council's budget. Many of the regeneration business cases had a 50-year plus time horizons.
38. [Content redacted for commercial sensitivity.]
39. The review team recognise that to avoid a requirement to write off a significant amount of debt now, the current arrangements would need to be maintained while the sustainable strategies are pursued at pace. The council have estimated that this will require c£100m per annum additional borrowing for the three-year period 2023/24 to 2025/26, based on current investment plans. It is acknowledged that this is a risk, but on balance it is felt to be a lesser risk than halting all activities now.
40. As set out in the commercial section of this report, a rapid sale of assets would be an inappropriate course to recommend and would be very detrimental to the Council financial position. With VSWL the current value of the assets has been estimated to be £300m to £350m against the outstanding debt of c£700m. [Content redacted for commercial sensitivity.] Therefore, by stopping the working capital support without a longer-term strategy in place, the council would need to write off a significant amount of outstanding debt.
41. There had been little capacity and capability put in place to manage the scale of commercial activity, the client function was inadequate. The council had the corporate capacity of a small district council, yet the investment portfolio of a very large city/metropolitan council. Despite best recent efforts of the new leadership team, the council still lacks capacity to deal with this scale of commercial activity.
42. There is little evidence to suggest that the systems and processes were initially put in place to ensure that the developments were delivered in an effective way from the outset.
43. There is some evidence to suggest that some investment decisions were made without appropriate business cases and records of robust land valuation. In some cases, project scope had been increased and budgets had to be extended. For example, the scope of Victoria Square had increased from the initial approval of approximately £460m in November 2016 to £700m in February 2021. Some strategic asset acquisitions lacked evidence of robust valuation, which resulted in borrowing more than the asset value.
44. Not enough attention had been given to consider the council's financial resilience and its risk profile. It was the belief that the council's commercial income and its ability to take margins on loans to companies would cover any financial eventuality. This has proved not to be the case. [Content redacted for commercial sensitivity.]
45. Prudential indicators have been set, monitored, and published in the Capital Strategy Report and have been assessed for affordability as required by the code. The initial

assessment of affordability of the regeneration schemes was dependent on the cash flow forecast rather than a robust financial investment model so the risks to principal repayment were not fully understood. There is little evidence that adequate consideration was given to option appraisal or that decisions were being made with sufficient regard to the long run financing implications and potential risks to the authority, especially regarding proportionality to the council's overall resources. The indicators showed that by 2020/21 debt costs would be at almost 100% of the net revenue income.

Recommendations

[S] short term 6 months [M] medium term 12 months [L] long term 2 years

46. Based on the report findings, that the Secretary of State considers the appropriate mechanism to support and challenge the council to give it the best opportunity to resolve its financial and commercial position. [S]
47. That the council consolidate the recently introduced spending controls with rigour. [S]
48. Develop a long-term commercial strategy to consider external partnering which could include all council assets. [S to L]
49. Implement the planned redesign of the system for management information to better inform decision making. This should include asset management, ICT, financial information and reporting, the integration of finance information and performance reporting. There is a need to streamline reporting to avoid constant updates to the Medium-Term Financial Plan. [S]
50. Develop a clear budget planning timeline that aligns the work on service redesign, savings, consultation timescales and implementation. [S]
51. Review the scrutiny function and establish a regeneration scrutiny panel which would discuss regeneration schemes in public (on the understanding that some commercial information may need to be restricted to the public). Review the number and function of the member-only working groups and reduce the number of meetings overall. [L]
52. Review and agree an approach to implement the expert advice on MRP treatment and the approach to any potential loan impairments. [S]
53. Develop a small client team to oversee Victoria Square and other strategic developments. [M]
54. Conduct the planned assessment against the Financial Management Code [S]
55. Review the council's position on subsidy/state aid and best consideration with regard to its wholly owned companies and review and reassess the legal position of the structure of company financing arrangements. [S]
56. Seek tax advice on company structures and financing and to ensure best consideration duties are met. [S]
57. Ensure the accounting treatment is correct for MRP, the treatment of receipts in the capital adjustment account and impairment. [S]
58. Further assess the impairment risk to the council loans. [S]

59. Continue the review of the constitution and pay particular attention to the content of reports to inform decision making, in particular the appropriate management of risk. Ensure that future reporting includes detail on alternative options, external tax and legal advice and appropriate commercial risk analysis. [L]
60. Work to close the several outstanding annual accounting years as soon as possible. This will require high level discussion between DLUHC, the external auditors BDO and the council. [S]
61. Review the decisions to acquire land during the period 2015-2019 regarding valuation, shareholder direction, legal advice, VfM and general governance of such decisions. [M]
62. Prepare a 30 year Housing Revenue Account (HRA) Business Plan and takes steps to ensure the current HRA is in balance. [S]
63. Define and implement an organisational design programme to support new ways of working and the Fit for The Future (FFTF) change programme. Ensure the change programme includes an analysis of skills and capability for the future needs of the council. [M]
64. Ensure that the FFTF change programme urgently realises savings and embeds a culture of service redesign. [S]
65. Strengthen staffing capacity and capability across the council particularly in Finance, Legal and Commercial as part of the FFTF change programme. [M]
66. Review the provision of earmarked reserves and update the earmarked reserves for the current planned use of reserves. Ensure HRA reserves are separately accounted for and not included in the General Fund balance and that the HRA earmarked reserves do not fall into a negative position. [S]
67. Continue to review the 23 council-owned companies to evaluate fitness for purpose. [S to L]
68. Strengthen the Shareholder Advisory Group with independent external advisors. [S]
69. Develop the reporting content from the Shareholder Liaison Service to the Shareholder Advisory Group with particular emphasis to commercial risk analysis. [S]

Governance commentary

Strategic direction

70. The organisation now has a five-year corporate plan, 'Woking for All'. It sets out the policy priorities of the administration; healthier, engaged, greener and prospering communities, underpinned by an overarching need for a high performing council. The plan was formulated following member, community roadshow and senior manager engagement. The community engagement was in response to an independent resident survey undertaken in 2020/21. According to the survey, residents valued the services provided by the council, but they did not trust the council (based on the levels of reported debt).
71. The new administration from May 2022 set out its post manifesto priorities and the first of these was noted as 'Getting the council's finances under control'.

72. The corporate plan has more than 200 actions which are monitored. The progress on the actions was reported to the Executive on 6th October 2022 and again on 2nd February 2023. According to the council reports, over 80% of the actions were rated as green, achieved or on target.

Internal processes

73. The new leadership team is essentially rebuilding most internal processes as they had been deemed not fit for purpose. Management information to inform decision making is recognised as inadequate and plans are in place to rectify this. Financial information does not currently enable managers to be agile in their approach to departmental budgets. The constitution is being reviewed. New company governance and processes have been put in place to manage the companies with the establishment of a Shareholder Advisory Group (SAG). The council's approach to procurement is being redeveloped as are its processes for change management, digitisation, and transformation. All these developments are in their early stages, nevertheless the review team recognise that these initiatives are required and have the correct direction of travel.

Culture and leadership

74. The council has a permanent Chief Executive appointed in April 2021. She is supported by three new capable permanent Directors. One Director is due to leave the council for a promoted post, but this will give an opportunity to add more commercial expertise to the senior team. There have been new senior appointments; for example, to lead the changes to the Shareholder function, lead the change and digital programme and to strengthen the finance team. The Monitoring Officer (MO) is leaving the council for a promoted post in April. The Section 151 officer indicated her intention in November 2022 to leave the council. There are plans in place to replace these two crucial roles. An experienced interim Section 151 officer has started in March and the Deputy MO at the council will act up pending a recruitment process.
75. The new leadership team is determined to develop a distributed leadership model. This will promote decision making at all levels and will empower staff to be creative, innovative and be encouraged to suggest solutions to ongoing issues. The review team were made aware of many examples of a 'dependency culture', staff used to pass decisions 'up the line' as this was described as the predominant culture previously. Some staff feel that the new leadership approach indicates that current senior staff are not interested in their work, but this is not the case. Due to the significant immediate issues with council debt and the council budget, the senior team acknowledge that they have not had as much time as they would like to properly engage with staff. The organisation is getting used to this new leadership style and the council is planning a programme of organisational development, previously lacking, to accelerate and embed this culture change. There is a long way to go to embed this new way of working.
76. The review team found there to be a good relationship between members and officers, however, this was described as not always having been the case.

77. The council is very open to support and challenge, evidenced by the significant number of external reviews commissioned to quickly understand existing practice. The council uses the outcome of this activity in a positive proactive manner. The new political administration has pledged to make public any significant documentation as and when necessary and has already demonstrated transparency.

Council services

78. In an independent survey during 2021/22, residents did express satisfaction with council services and the current rating of most services provided by the council does perform well compared to other statistical neighbours. As a result of commercial income supporting the core budget, the council did not choose to reform at scale its services to residents, whilst neighbouring authorities (and most nationally) engaged in significant change programmes and spent time reforming services.
79. The immediate focus of the council is dominated by financial and commercial considerations which does place a strain on 'business-as-usual' to deliver services.
80. Councillors, senior officers, and the workforce in Woking have not experienced the council working within tight financial constraints. They are not used to making decisions to reduce and reform services based on a clear set of strategic priorities. The budget situation in Woking will now require a significant change programme, which is due to be rolled out. It is imperative that everybody commits to the savings targets and delivers them in what will be a very short period. This is to give the council a fighting chance to remain solvent in the coming years. There will be hard political decisions to make in the coming months.

Capacity and capability

81. There are some very committed and talented members of staff at all levels in Woking, particularly at the senior level. New staff brought in have made a positive difference to the skills required within the council. Despite this, there is not enough capacity or capability to manage the significant number of issues the council is now facing. In reshaping the council, new skills and approaches can be built up in most areas, but this will take time that the council does not have.
82. From the historic base, the sheer scale and complexity of the investment and commercial activity of the council, means that the council will never have the capacity to effectively manage all the commercial and economic considerations which would only be enacted properly by expert investors and developers steeped in experience for a programme of this nature. This is why the council must look to find partners to share risk and any benefit from the council's ongoing programmes.
83. Nevertheless, the current knowledge in the council about investment, debt and commercial aspects of development, outside of the financial team is impressive for a small council. This however, will not be sufficient to move forward.

Decision making

84. There is evidence to suggest that historic business cases for investment decisions were considered at the executive and at full council, the review team did not have time to examine every decision in detail.

85. The decisions examined by the review team were made 'in plain sight' and would be deemed to be in line with the constitution at that time. However, the level of understanding of risk by decision makers is less clear. The reports taken through the council decision making process historically did not show enough evidence of the level of risk or financial analyses that the review team would normally expect. Further work is needed to review this area, but presentations made to full council are very high level and there is little evidence of the commercial risks that members would be required to consider.
86. What is clear is that the investments by the previous leadership were made with little provision or consideration of the council capacity and capability to manage these programmes effectively and efficiently. The council constitution determined that the previous Chief Executive could hold an 'Opportunity Acquisition Fund', which gave him delegated responsibility to spend up to £3m on regeneration projects without formal recourse to the executive or council. This delegation is very unusual and has now been removed by the new leadership and executive.
87. Several development decisions and acquisition of land and/or property undertaken historically by the council are being reviewed by the Monitoring Officer to enable current business plans to be drawn up to develop this land and property held by the council. [Content redacted for commercial sensitivity.] Several parcels of land were acquired by the council between 2015 and 2016. Enquiries to date indicate the paper trail is limited in respect of valuations, shareholder directions and company board minutes for the acquisition. [Content redacted for commercial sensitivity.] There may have been a rationale to purchase this land at the time, but it is unclear whether some of this land was acquired at a market rate based on a robust valuation to ensure value for money.

Financial commentary

The Council's financial position

88. The strategic and policy context are set out in the 'Woking for All' Strategy and underpinning documents, the Woking Economic Development Action Plan and the Draft Town Centre Masterplan. The council have produced a 'Plan on a Page' setting out the council change programme to be delivered over the next three years.
89. The Woking for All Strategy includes a new strategic outcome and additional priority commitments relating to affordability, financial control and delivery of value for money, with the strategic objective of being 'a financially sustainable council with sustainable and affordable plans.' This is accompanied by priority commitments to: get the council's finances under control; consider new approaches to increasing income and make decisions in an open and transparent way.
90. A material refresh of the MTFS was carried out and reported to the Executive in July 2022. This recognised:
    - The strategic and corporate context for the Medium-Term Financial Strategy (MTFS).

91. The financial challenges the council is facing including:
    - Inflation costs for pay, non-pay, and energy
    - Pressures on car parking income and commercial rent. These budgets are still at pre covid levels and total c£30m and the shortfalls against this target are one of the main reasons for the overspend. The budgets have been rebased for 2023/24.
92. The need to make significant savings to offset those pressures, targeting £11m by 2025/26. There has since been additional capacity bought into the council with some systematic work to look at how these savings could be identified.
93. As with many local authorities during 2022/23, the in-year financial position has continued to deteriorate. The monitoring reported to Executive in January 2023 (based on the October position) shows a projected outturn or year-end overspend of £3.173m. The most material variation is an increase in the parking income shortfall, alongside some new service pressures emerging.
94. The final projected outturn overspend position for 2023 is more likely to be in the region of £3.5m to £4m.
95. The table below sets out the comparison of the position when the 2022/23 MTFS was set. The figures shown are the budget gap which will need to be met with reserves.

Table 1

	2022/23 £’000	**2023/24 £’000**	**2024/25 £’000**	**2025/26 £’000**
March 2022	4,134	4,929	4,490	5,450
July 2022	7,414	8,874	9,935	11,181
February 2023*	8,841**	8,345	9,476	10,482

*As per February 2023 MTFP

**Assumes outturn overspend of £3.4m

96. The council is clearly attempting to get to grips with the financial position and have reached out for additional support, including from Surrey County Council and the LGA and are building their own capacity to deliver the change programme. The latter includes a focus on delivering savings and improving the management information to move the council away from the reliance on the use of reserves. The challenge is the scale and extent of the change required. The council is aware what it needs to do but does not have either the skills or capacity to fully execute, or the luxury of time to implement the changes required to deliver a balanced budget.
97. Proposals for the additional staffing capacity required have been developed. The funding is estimated to cost £3.2m over a two-year period. This must be seen in the context of the need to reduce the debt burden and potential S114 position. The review team feel that this ‘invest to save’ funding is required in order to enable the council to realise the targets for balancing the budget over the three-year period.
98. The December 2022 MTFS update was stark. The Finance Director (Section 151 officer) stated that, based on current analysis, the expenditure that authority is

projecting for 2023/24 - 2025/26 could exceed the resources that the council has at its disposal to meet the expenditure'. This would in effect trigger a section 114 notice.

The Housing Revenue Account (HRA)

99. The HRA is a landlord account, recording expenditure and income arising from the provision of housing accommodation by local housing authorities and is a ring-fenced account within the General Fund. Legislative features are:
    - It is a ring-fenced account within the General Fund
    - no general discretion to breach the ring-fence.
    - cannot budget for a deficit.
    - all borrowing within the HRA is in line with the Prudential Code.
100. The HRA budget should be set each year in the context of a 30-year business plan. The Business Plan is a statutory requirement used to assess the ongoing financial viability of the HRA and its ability to deliver the council's housing priorities.
101. The HRA has not been considered in detail as part of this review but there are some issues which should be highlighted.
102. The HRA is in deficit for 2022/23 (an estimated deficit before the use of reserves of £804.8k in 2022/23 increasing to £1.6m in 2023/24) and the balance has had to be met from reserves. The maximum allowable rent increase of 7% has been applied generating almost £1.7m of income. However, budgeted spend has increased by £2.2m, with pressures on the maintenance budgets where contracted costs have increased by 10.1% and a £1.5m increase in supervision and management costs. Salary and other central costs have been allocated to the HRA in accordance with normal accounting rules to show the full cost of the service. An initial review of recharges was conducted in 2022-23 with a full review planned for 2023-24. There appears to be an increase over and above what would reasonably be expected from pressures in pay costs etc and it is essential that the review of recharges is carried out.
103. The HRA deficit is driven by the Sheerwater Regeneration project where approximately 426 HRA dwellings will be demolished. The vacant land will be transferred to Thameswey Developments Ltd with the new replacement affordable housing dwellings owned and managed by Thameswey Housing Ltd. The HRA loses the rental income from these dwellings, whilst still incurring costs to maintain and secure them. There are now only around 90 occupied HRA dwellings within that scheme and it is assumed that there will be a further 50% reduction in occupied homes (and therefore rental income) within the 2023/24 budget.
104. In addition [content redacted for commercial sensitivity], abortive costs relating to the work with New Vision Housing were also met from the HRA. The review team have been told that these are due to be repaid to the HRA in March 2024, although Thameswater Housing Ltd will need to be supported with the working capital to be able to do so.
105. The two HRA reserves are:
    - HRA working balance of £334k per annum.
    - The Housing Investment Reserve (HIP) – this is due to decline from £4.2m in 2020/21 to a negative position of £266k in 2024/25. The balance on the HIP

Reserve was £2.6m on 31 March 2022 and is forecast to have dropped to £221.5k by 31 March 2024 after the transfer from reserves to the HRA and will go into a negative position in the following year. This is a further deterioration from the predicted reserve position in March 2022.

106. No 30-year business plan exists for the HRA. It is important that the 30-year business plan is prepared and used to assess the long-term viability of the current HRA arrangements. The business plan will need to address the impact of the reduction in housing stock on the longer-term viability of the HRA.

An overview of council's commercial operations / investments / company portfolio and respective management arrangements

107. The major financial impact is from the previous commercial activity, particularly with the Thameswey Companies and Sheerwater Regeneration and Victoria Square Woking Ltd. Whilst the council understand the need for a long-term solution for the investment cost, this is still not reflected in a strong and resourced client side and in the council's business as usual activity. For example, the Risk Register excludes these commercial activities and there are separate asset planning processes. The financial risks that the council is exposed to on their regeneration investments are material and cover:
    - The scale of exposure to market valued assets and long-term debt, and
    - The need to make prudent provision for the repayment of debt and the associated accounting risks of the Minimum Revenue Provision (MRP) and impairment of the council loans.

The scale of exposure to market valued assets and long-term debt

108. Following July 2021 Council and the notice of motion about the council's financial affairs, Ernst & Young (EY) were commissioned, after a tender process, to undertake a comprehensive statement on the Council's affairs and work to assess the council's medium term financial resilience. The comprehensive statement on the Council's financial affairs, including its assets, borrowing, investments and contractual obligations was presented to the Council's Overview and Scrutiny Committee on 24th January 2022 and Executive Cabinet on 3rd February 2022 as part of the Medium-Term Financial Strategy reports. The work on financial resilience was reported to the March 2022 Executive Cabinet. Both reports can be found on the council's website.

109. According to the review, 37% of the council's asset base is investment properties which have a net book value of £330m at the end of 2020/21. They are valued at fair value, or the price that would be received for selling the asset and were revalued £43m downwards during that year to reflect the market position. These assets which are separate to the investments in VSWL and the Thamsewey development, currently generate c£22m income that supports the revenue budget.

110. The borrowing position was £1.8bn, of which 98% is with PWLB. The annual interest paid as a proportion of net service expenditure is 135%. Whilst this was deemed to be affordable at 90% of the Capital Financing Requirement (CFR) this leaves the council financially exposed. It also does not consider the future borrowing

requirements and recent increases in PWLB rates (the average interest on the £1.8bn is 1.62%).

111. The council investments total £1.15bn of long-term investments to Joint Ventures or Group Companies, £38m in associated share capitalisation and £18m to external organisations. For the long-term investments, the council has moved from equity to a loan capital model and whilst there is sufficient turnover to meet short term debt repayments, this is largely due to the working capital facilities provided by the council. The loans are secured against the subsidiaries assets which means they would revert to the council in the event of default. Victoria Square (Woking) Ltd has a negative asset value, indicating that the liabilities of the company are greater than the assets. [Content redacted for commercial sensitivity.] The shares held by the council have not been revalued in the Statement of Accounts since their acquisition.

112. As the debt gearing is so high for VSWL and Thameswey group, it is recommended that the council has up to date tax advice on their structure and gearing.

Associated accounting risks, Minimum Revenue Provision (MRP) and impairment

113. The position against the statutory codes and guidance is set out later in this report. In summary the position is that:
    - If the proposed new MRP guidance is implemented, the council estimate the risk initially as £11.9 million annually in 2021, rising to £23.4 million annually when averaged over a 50-year period. This is a complex issue and the council will need specialist accounting advice.
    - Capital Adjustment account – the council needs to be ensured that the capital receipts from the loan repayments are applied to write down the requirement for the Capital Financing Requirement or CFR. The Capital Strategy reports set out the receipts set aside but the council needs to be ensured this follows through into the accounting treatment.
    - The impairment risks for the loans, particularly to VSWL have not been assessed and could be material given the value of the assets is so much lower than the value of the loans.
    - The shares held by the council have not been revalued since their acquisition.

114. The council's current position therefore is not in line with the proportionality and changes to the Prudential Code in 2017.

115. In summary, there is a significant financial risk to the council and if the changes to the MRP guidance (consulted on in 2022) are implemented there will be insufficient resources to cover those additional costs. At that point, there would need to be a discussion with relevant parties as to how a sustainable position can be reached.

Other issues

116. As set out in the EY 'comprehensive statement' as of 31st March 2021, there were £17m of loans to external organisations (assuming an expected repayment to the council of £9.25m) the most material being £6.3m to the Peacock Centre, which has been recovered in full through the administration process, and £6.4m to Greenfield School. These loans should be carefully monitored.

117. Opportunity to Purchase Budget – The previous Chief Executive's delegated authority to make strategic acquisitions of land and property for a value of up to £3m was used to make a number of purchases, largely between 2016 and 2019. These sites include 10 Acre Farm (£1.5m), Robin Hood Pub (£1.4m), Anchor Pub (0.9m). In addition, a land assembly acquisition, known as Brookwood Lye was acquired by Thameswey in 2017 for £18m.
118. As set out in the commercial section of this report, a rapid sale of assets would be an inappropriate course to recommend and would be very detrimental to the council's financial position. With VSWL the current value of the assets has been estimated to be £300m to £350m against the outstanding debt of c£700m. In a sale position [content redacted for commercial sensitivity] the council would need to write off a significant amount of outstanding debt. By halting the working capital support without a longer-term strategy in place, the sale position would de facto be required.
119. In both these cases the review team advise that to avoid a requirement to write off a significant amount of debt now the current arrangements would need to be maintained while the sustainable strategies are pursued at pace. The council have estimated that this will require c.£100m per annum additional borrowing for the three-year period 2023/24 to 2025/26, based on current investment plans. It is acknowledged that this is a risk but on balance it is felt to be a lesser risk than halting all activities now.
120. If the arrangements continue, the financial impact of the accounting risks related to the need to apply a more prudent level of MRP and the potential that some of the loans will need to be impaired cannot be ignored. There is a need to make a more prudent provision to support the level of debt. There will need to be a discussion and agreed approach with DLUHC and with the External Auditors on how these risks can be managed and accommodated.

Financial governance arrangements

121. The finance team within the council is small with the Section 151 officer having responsibility for the Finance, the Revenues and Benefits Service and the Internal Audit service, currently provided externally by Mazars. The finance function has no management accountancy or commercial finance expertise. With the reduction in government expenditure and the additional freedoms in the 2011 Localism Act, the council embraced the move to commercialism with significant investments particularly between 2016 and 2019. There is no commercial expertise within the finance function. The team was not geared up to deal with the scale of the investments made by the council, nor was the function strengthened to effectively manage those investments.
122. The council have historically been confident in the approach that they have taken. Justification for the approach is described as investments not being made 'out of' borough or purely for investment purposes. The belief was that the council response was prudent and delivered significant benefits to the borough. This rationale is reflected in the language of the reports and previous assessments of the S25 position. However, this justification did not reflect the reality of the situation.

123. Previous S25 reports have used the CIPFA Resilience Index and highlighted risks with future government funding and specific pressures (and in 2021 the need to reduce the reliance on reserves). However, they have not highlighted risks associated with the very high levels of borrowing until the most recent report.
124. Both the 2022/23 and the 2023/24 Capital Strategy Reports conclude 'The Finance Director is satisfied that the proposed capital programme is prudent, affordable and sustainable, and that the revenue impacts of the projects included have been recognised in the budget'. This statement was optimistic and not realistic.
125. The February 2023 papers contain a separate S25 report that is much more realistic about the risks faced.

Position against statutory codes and guidance

Prudential Code

126. Under the Prudential Framework, local authorities have freedoms to borrow and invest without the need for government consent, if borrowing is affordable. The Framework includes the Prudential Code and Treasury Management Code. The former is to ensure that the capital investment plans of local authorities are affordable, prudent and sustainable and the latter governs the council's Treasury Management activity.
127. The Prudential Code was strengthened in 2017 to include a stronger emphasis on the prudence and affordability of capital plans and borrowing, stating that 'The local authority shall ensure that all of its capital expenditure, investments and borrowing decisions are prudent and sustainable. In doing so it will take into account its arrangements for the repayment of debt (including through MRP/loans fund repayments) and consideration of risk and the impact, and potential impact, on the authority's overall fiscal sustainability. The fundamental objective in the consideration of the affordability of the authority's capital plans is to ensure that the level of investment in capital assets proposed means that the total capital investment of the authority remains within sustainable limits.'
128. The codes were further strengthened in late 2021 with requirements around proportionality, alongside the existing Code objectives of affordability and prudence. This is to be implemented for 2023/24.
129. The decisions to invest in the regeneration of Sheerwater and Victoria Place were both made in 2016 and the council had already committed to this path when the Prudential Code was strengthened. The weaknesses in the reports used in the decision-making process and lack of an adequate assessment of risk have been addressed elsewhere in this report.
130. The Prudential Indicators have been set, monitored and published in the Capital Strategy Report and have been assessed for affordability as required. The initial assessment of affordability was dependent on the cash flow forecast rather than a robust financial appraisal so the risks to principal repayment were not fully understood. There is no evidence that adequate consideration was given to option appraisal or that decisions were being made with sufficient regard to the long run

financing implications and potential risks to the authority, especially regarding proportionality to the council's overall resources. The indicators showed that by 2020/21 debt costs would be at almost 100% of the net revenue income. Efforts were made however to de-risk the Council and protect against economic shocks by matching interest rates.

131. The council is now in the following position:
    - External debt of £1.9bn (internal borrowing 4%), MRP of £7.4m or 0.37% of debt.
    - With a population of 100,008 this means debt per head of £19k
    - 4th highest level of debt in the country and the highest level of debt per head.

132. It is difficult to conclude the council has complied with accounting best practice and the prudential framework. The scale of borrowing was disproportionate to the council's assets and ability to manage complex commercial activity. There was insufficient regard to the level of risk the council was being exposed to, particularly as the borrowing for VSWL and Thameswey Development covered development costs and the working capital to repay the loans for the majority of the financing period. The decisions to invest were made in line with the constitution, assessed against the Prudential Framework, the 2018/19 and earlier accounts had unqualified VfM opinions.

133. Given the scale of the borrowing and the fact that future risks of refinancing were not considered it cannot be argued that the approach was prudent.

134. The leadership of the council has changed at an officer and political level since these decisions were made and efforts must continue to be made to identify a sustainable solution to the council's finances.

Minimum Revenue Provision (MRP)

135. Where authorities borrow to finance capital spend, they are required under regulations to set aside money each year from their revenue account. This is referred to as Minimum Revenue Provision (MRP) and is to make sure they can afford to repay the principal of their debt.

136. An underpinning principle of the local authority financial system is that all capital expenditure has to be financed either from capital receipts, capital grant or eventually from revenue income. The broad aim of prudent provision is to require local authorities to put aside revenue over time to cover the gap between their Capital Financing Requirement (CFR) and grant income/capital receipts. In doing so, local authorities can align the period over which they charge MRP to one that is commensurate with the period over which their capital expenditure provides benefits.

137. In 2019, the MRP guidance was updated and the commentary states that 'Whilst recognising that local authorities have options other than building up prudent provision to repay debt, the Government has identified that there is a mismatch between the weighted average lifetime of local authority debt and the length of time it would take to fully provide for that debt based on current levels of MRP charged. Whilst this is not a risk if ease of access to PWLB remains unchanged, assuming that

this will remain the case over the length of longer dated local authority debt instruments is not a prudent approach. For this reason, the Government has changed the definition of "prudent provision" to highlight that there is a balance between matching MRP to the service potential of assets and to the weighted average lifetime of local authority debt.'

138. In signing off the 2018/19 Audit Opinion, the External Auditors reviewed the council's policy that there are no charges on the borrowing used to fund the loans to subsidiaries, as the intention is that these entities will be able to make sufficient returns in the future to be able to repay these loans and the receipts will be used to repay the debt. At that point the council were satisfied that the business models would result in full repayment of the loans over the next 50 years and no MRP was required. The External Auditors recommended that:
    - The council reviews its existing MRP policy to confirm that it is compliant with the new CLG guidance for investments supported by borrowing from 1 April 2019.
    - For pre-April 2019 investments, that the council closely monitor the business plans of the subsidiaries to confirm that, in the current environment, the loans will be fully repaid, or, in the event of any risk, it considers whether it would be appropriate to commence making an MRP charge against that borrowing.
139. The council have chosen their MRP approach on the basis that that there is sufficient cashflow in the entities' business plans to cover the loan repayments and that the provision of MRP for share capital over 100 years is a prudent provision, considering the underlying assets of the companies. Their Treasury advisors have reviewed the MRP for Thameswey and recommended that as part of its annual impairment review WBC should consider:
    - The third parties' financial position and whether the assets held provide sufficient collateral to cover the loan value in event of default and that business plans still forecast sufficient surpluses.
    - Whether there are adverse changes in economic or business conditions which could reduce the ability of the borrower to meet the loan obligations
    - Should this review provide an indication that the third party could default on a loan repayment then the Authority should consider commencing a prudent MRP provision. Consideration of MRP provision should be given for any loan provided to a third party.
140. Once loan repayments become due under the loan agreement, the council set aside the capital receipts arising from the repayments to reduce the capital financing requirement in lieu of MRP.
141. The MRP Policy has been updated to reflect the annuity asset life approach for property acquisition and the justification where assets lives beyond 50 years are used. It also commits to reviewing its approach going forward if the recently consulted on changes to MRP policy are implemented.
142. It should be noticed that there is a challenge to the 2019/20 accounts regarding the treatment of MRP.

143. DLUHC launched a further MRP consultation in November 2021 which closed in February 2022. The proposals are to strengthen the 2003 Regulations to make explicit that capital receipts may not be used in place of the revenue charge (although not to prevent authorities using capital receipts to reduce their overall debt position) and that prudent MRP must be determined with respect to the authority's total capital financing requirement. This is to stop the intentional exclusion of debt from the MRP determination because it relates to an investment asset or capital loan. Revised regulations have not yet been published.
144. The council's own assessment, as set out in the response to the DLUHC consultation, is that 64% of their borrowing, or £1.169bn, will not be compliant with the proposed changes in the guidance as drafted. The current level of MRP provided for in the council's general fund is £6.2m per annum – using the council's calculations this would increase by £11.9m (192%) in the first year and £23.4m (377%) averaged over 50 years.
145. In the consultation response the council expressed concerns about the proposed changes on the basis that as the investment is not for commercial purposes there are not excess yields from which to set aside further funds in the short term. To set aside MRP would risk undermining the business plans for the investment in the Borough. The council has since committed to "should those or other changes be taken forward the Council will review its approach going forward as required".
146. The loans to VSWL and Thameswey are complex with a mix of annuity and interest only loans. The repayment of the annuity loans includes repayment of principal in a similar way to how a mortgage operates and secures repayment of principal over the life of the loan. However, the profile of the principal repayment is considerably backloaded meaning there is additional risk at the start of the loan period. This should have called into question the MRP policy that was followed prior to the November 2021 consultation.
147. The council has commissioned an expert external review of their approach to impairment and MRP. With the complexity of the financing and MRP arrangements alongside the changes to the MRP guidance, this review is welcomed. With the financial position of the council, significant changes to MRP treatment cannot be covered by available resources and a discussion will be required with DLUHC and external auditors on how this can be implemented in a sustainable way.

Capital Adjustment Account and impairment

148. As referenced earlier in the report, there is a need to ensure that the capital receipts received from the repayment of the loans are being accounted for to reduce the capital financing requirement. The loans need to be assessed for any impairment risk.

Future capital financing charges

149. The loan funding provided to Thameswey and Victoria Square includes a revolving credit facility which provides working capital to cover the financing costs for the previous debt. If the funding is stopped, however the position is not viable and there is a risk the debt will not be recovered. The loan interest payable is based on the PWLB rate. The impact on the council's capital financing budget is not significant. Capital

financing costs are due to increase in 2023/24 and are then forecast to be relatively steady. The exposure to increased PWLB rates for borrowing to support VSWL and Thameswey is also limited as the increases are passported on to the companies.

150. The impact on the capital financing budget will need to be carefully evaluated if any changes are made to the VSWL and Thameswey structures. The impact of the increased capital financing costs for future borrowing due to the increase in PWLB costs should also be considered.

Financial governance and budget management

Transformation programme and Fit for the Future (FFTF)

151. The council has not been through a significant process of transformation and service redesign. As a result, there is limited experience and the lack of the right infrastructure to support the scale of the change that is now required.
152. This has started to change. A golden thread from the new Corporate Plan to the budget decisions has been established and the culture at a senior level has shifted significantly. This is not yet reflected throughout the whole council and work will be required to ensure this is embedded across each layer in the organisation. All services need to understand the severity of the budget situation. There has been a need to 'rebuild the council very fast'.
153. Example of the progress made to bring the organisational infrastructure into place include the following:
    - Risk management training has been carried out with the senior leadership team (CLT) and members with support from the council's insurance provider. A Risk Strategy and Appetite Statement is in place alongside a Risk Register which is monitored quarterly and reported to the Executive.
    - Work is underway to improve procurement and contract monitoring. Discussions are underway with a potential partner to provide a 'trusted advisor' relationship and a dedicated business partner resource. Whilst arrangements are in place for the large contracts, the contract monitoring function itself was disbanded 7-8 years ago.
    - A Project Management Office (PMO) function has been established to deliver the Fit For The Future (FFTF) 'Plan on a Page'. Two new posts have been recruited to support the PMO and benefits realisation work.
154. FFTF is a series of CLT priorities to make the council fit for the future. The scope is broad and ambitious and includes:
    - Savings and income
    - Asset management
    - Governance and controls – including the 'Programme on a Page'
    - Transformation and channel shift
155. Rigour is being provided with the establishment of a new PMO and a high level roadmap for the programme is now in place. There is a risk however, that the scope becomes too broad. While understandable, it is also noticeable that the work does not relate to that required to establish the longer-term asset management

programme and a solution for Thameswey companies and VSWL. At the appropriate stage some of the programmes will need transitioning into business as usual so the focus can be on driving the benefits realisation work.

156. The benefits realisation work is split into different phases. A MTFP group led by the Strategic Director for Corporate Resources has been established to ensure delivery and track progress. This brings together key personnel from finance, transformation and the PMO. Additional support has also been provided by the LGA who have provided the Council with a separate report on the budget position and the effectiveness of the savings process. The work of the LGA has informed this report.

157. *FFTF 1 – Summer 2021* – This predated the establishment of the PMO and was based on a spreadsheet exercise led by Finance. Round 1 was tasked to deliver £2.4m in 2022/23 from 95 savings options. Effective monitoring was not in place and the delivery has been mixed with some double counting and a net total of £1.2m achieved. The savings have been taken out as part of the 2022/23 budget. As the savings are now 'mainstreamed' and taken out of budgets it is hard to track this through into the recent financial reports.

158. *FFTF 2 – Summer 2022* - Managers were asked to identify further savings over the summer and early autumn 2022. A long list of 120 were identified and mapped from 2022 to 2025/26 with a final list of just over 60 savings and cuts measures delivering £4m across 2022/23-2025/26. These were reported to the November 2022 Executive meeting and form part of the 23rd February 2023 budget reports.

- £598k of the savings will be delivered in 2022/23. Of these £377k relate to removing vacancies and a small restructuring.
- £1.978m are due to be delivered in 2023/24 alongside the savings already identified in 2022/23. Of these just over £1.255m relate to corporate measures with £550k to be achieved from reductions in one-off contract spend, £160k relates to a revaluation appeal for car parks (which will impact on the overall business rates retained income if achieved) and £146k reduced pension costs post revaluation.
- £1.21m to be delivered in 2024/25 - including a further £550k for one off contract spend and £146k for pensions.

159. These measures do not yet include the more challenging reductions and service reconfigurations that will be required to achieve the scale of the budget cuts required. The new post in the PMO will manage the benefits realisation, to ensure that all savings identified are delivered and properly reflected in the council's general ledger. Based on the success rate from Round 1 the council will need to be extremely focused to ensure that these savings are achieved.

160. Work has started on the '*Third Round'(FFTF3)* of budget cuts and savings. This is based on the recent work on the impact of each service delivering just the statutory minimum. Ninety functions have been mapped, with 25 workshops involving 30 managers. A potential £5.5m has been identified but this would include very significant service closures. This is a good starting point, but a more realistic assessment has been that around £3m could be deliverable.

161. The need for pace is well understood by the council but there has to be clarity on how the work will align with the MTFP process with a timeline for how and when decisions on service redesign will be made. Broadly this has been described as:

- A clear strategy will be in place and proposed measures will be in place by autumn with consultation on the changes from autumn into the winter. The consultation process will need to be carefully managed with a clear understanding on how changes relate to statutory provision.
- The second year will then be focused on implementing service redesign.
- The process will be completed by the end of 2 years.

162. Traditionally, the council has been a 'cash rich' council and not too close to the detailed budget position, which means that a culture of ensuring services are delivered at best value is not embedded and there is a limited awareness of the cost of service delivery. The PMO team will need strengthening and to act as an internal consultancy to support the benefits realisation and changes that must be delivered. The Finance team are very stretched and struggling to manage all the additional demands. Integration of the work of the PMO and the Finance function is key. The role of the new Section 151 officer will be critical to this.
163. Additional HR support to deliver organisational change will be required. The ICT infrastructure and management information is being improved but the lack of an asset management system will hamper the work required to really get to grips with the council's large estate. More work is required on the provision of integrated financial and performance information which will be picked up through the review of the Green Book.
164. To provide the capacity required there is a £3.2m capital receipt request which identifies a requirement for an organisational development specialist, design lead and business analyst to work with all the service managers. If this is approved by the council, this will need to be submitted to the Government before the beginning of the financial year. This will allow the council to fund the 'invest to save' transformation work without placing additional burden on the revenue budget.
165. A balance must be struck between organisational and service redesign and the urgent need to deliver cashable savings that would lead to a sustainable budget. Setting set up a programme management approach to delivering the change in accordance with best practice will need to ensure this is delivered at pace and within acceptable financial parameters. The need to prioritise the savings work must be at the front and centre of the Fit for the Future programme.
166. There will be some difficult political budget decisions that have to be made. Resident perspectives are important and it has been relayed that there are concerns about the levels of debt the Council has and what this will mean for levels of council tax.

Expenditure Controls

167. A recruitment freeze is in place with leadership team permission required to fill a vacancy. This has taken some time to bed in with some differences of opinion on what is an essential post, but this process is now working effectively and can be tracked by a monitoring spreadsheet.
168. The other expenditure controls had been delayed while work was carried out to look at how spending could be stopped and the impact of the measures monitored. During

the period of fieldwork for this review, the planned further controls were put in place. These have now been expedited as per below.

The controls in place include:

- A freeze on non-essential recruitment to vacant posts.
- Reviews of Investment Programme, Thameswey Business Plan and projects.
- An additional £400k of savings included in MTFP for 2022/23. The restrictions of spending to 'essential only' has been communicated to all managers as of 8th February 2023.
- A weekly cost control panel and reporting process is proposed.

Financial information and reporting

169. The current finance team have a wealth of experience and knowledge, but limited capacity to deliver the type of financial information that is required and there is a lack of management accountancy experience. It is recognised that the format of the financial information and reporting needs an overhaul and is not fit for purpose.
170. Savings are monitored by the Programme Team and cross referenced to the financial ledger. The Finance team are undertaking work to finalise restructuring the general ledger to reflect the new organisation structure in time for 1 April 2023. The current budget structure and monitoring process is complex with cost units which contain staffing and overheads which are then allocated to the service units. Notional capital charges are also allocated to services and netted off again in the budget. A great deal of effort goes into this work and the resource could usefully be deployed on other tasks.
171. Detailed information is in place for the staffing budget which is monitored on a spreadsheet on a post-by-post basis. Managers have access to the financial system Integra.
172. The senior officer team (CLT) and the Executive receive the Green Book which is the formal monitoring report. It reflects the material issues (staffing, interest, car parking income, commercial income), it does not provide the standard monitoring information by service area with the projected outturn that you would expect. Performance and finance information is not integrated and there is no narrative that explains the position or indeed provides insight or recommendations. CLT feel that they are not receiving the quality of financial reports they require.
173. A report to October 2022 Executive described plans for a new format of the Green Book. Capacity will be required to deliver this and it will also need to drive the benefit realisation work. The new Green Book is due to go live in April 2023.
174. Surrey County Council have also provided some additional technical support which has been welcomed.
175. In March 2022, a financial resilience framework was introduced which provides more of the levers to manage the budgets. This alongside improved financial reporting will provide some of the key enablers for financial control.

Reporting against the financial management code

176. The Financial Management Code sets out the standards of financial management expected for local authorities. The Code builds on the CIPFA Prudential and Treasury Management Codes taking a principle-based approach to financial management, considering areas including financial leadership and governance, sustainability and assurance. It requires a longer-term view to be taken to financial planning and it is expected that local authorities will self-assess against the requirements of the Code. The council do not currently carry out this assessment. For 2023/24 a separate S25 Report has been made and this includes the commitment to programme a review in 2023/24 as part of its delivery of the MTFS strategy. This will form an important part of assessing the effectiveness of the financial management arrangements.

Financial viability

Revenue budget – risks and delivery of savings

177. The Council has a net budget of approximately £24m when benefits and capital charges are excluded. £36m of this is funded by sales, fees and charges and rent. The previous growth in the rental income, which is now c£20m and has protected the council from previously having to make reductions in services.
178. Due to the format of the current monitoring reports, there is little detailed scrutiny of the service budgets and it is important that the changes to financial and performance reporting endorsed by Overview and Scrutiny and Executive in October and November 2022, are implemented for the new financial year. These reports are required to effectively understand and monitor financial and operational performance as well as the delivery of the savings required.
179. The biggest risks to the revenue budget position are the performance of the commercial investment estate and the parking income. Aside from general inflationary pressures, these are the main factors behind the 2022/23 projected overspend and increased use of reserves required in year. The commercial rent and car parking budgets were at pre-covid levels, offset by the use of reserves and did not reflect current levels of performance. This has been corrected in the 2023/24 budget.
    - The car parking budget has been rebased and modelled over three years to reflect the reduced level of activity post covid, in part offset by the new car parking charges introduced. A top down and bottom-up approach to budget setting has been taken with a combination of seeking to achieve an income target whilst considering likely activity levels. It is important this is carefully monitored and not impacted by optimism bias.
    - The commercial rental budget has also been rebased and reduced by c£2.5m to reflect current income levels. Detailed analysis of leases sits behind this, but the service is hampered by the lack of an effective asset management system.
180. The amount of work that has been carried out is encouraging, but it is important the council guard against optimism bias and continue to monitor the position closely.

181. Another significant risk is the ability to deliver savings included in the 2023/24 Budget and to deliver the target of £11m over the three-year period. This equates to taking out over 25% of the council budget. This will fundamentally change what the council can deliver and will require political will and a step change in activity to identify savings and reconfigure services.
182. A policy setting out the intended flexible use of capital receipts to fund transformation project costs is being prepared and will be included with the budget papers to Council in February 2023. If approved, this will allow the Council to fund the Transformation work without placing significant additional burden on the revenue budget although there will be a cost.

2023/24 Budget position, reserves and future resilience

183. A combination of factors will enable a balanced budget to be delivered for 2023/24 and potentially 2024/25 (aside from the risk with MRP):
    - A better-than-expected financial settlement – with c£1m from additional New Homes Bonus funding, the new services grant and changes to business rates.
    - The inclusion of £1.8m of savings.
    - The continued and increasing requirement to use reserves to support the budget position. The council will have sufficient reserves for 2023/24 and 2024/25 only.
184. No allowance has been made for the next savings round in the budget position as the proposals are not sufficiently well developed or consulted on.
185. The council have assessed a prudent level of reserves to be £10m to reflect 10% of operational expenditure (£5m) plus £5m for business change and budget savings risk. Efforts have been made to strengthen the reserves position and this has been achieved in 2022/23 through the release of development funds and a one-off saving from renegotiating a car parking charge.

Table 2

	Opening Balance £'000	**Estimated Use Of Reserves* £'000**	**Additions £'000**	**Closing Balance £'000**
2022/23	24,998	(9,525)	7,466	22,939
2023/24	22,939	(8,957)	0	13,982
2024/25	13,982	(9,476)	0	4,506

*includes planned use of Investment Programme Reserve as well as support to Revenue Budget

186. The use of reserves to cover revenue deficits is forecast to reduce balances beneath the minimum level and there is a real risk all reserves will be used during 2025/26. The actions taken to reduce the use of reserves have improved the position in 2024/25. There remains a risk that if the targeted £11m cuts and savings are not

delivered then all available balances will be used during 2025/26. This is before any MRP changes are considered.

187. The 2023/24 MTFP does not include a detailed schedule of earmarked reserves. It is important that the position on all of the individual reserves is reviewed and recast so that the planned use of reserves is appropriately allocated. It is also important that the Housing Investment Reserve, which is an HRA reserve, is kept separate and is not allowed to go into a negative balance.

188. Whilst a balanced budget can be achieved in 2023/24 and potentially in 2024/25 this will not be achieved in 2025/26 unless the savings required can be fully delivered and there are no further external shocks or risks. This does not take into account any changes in MRP policy.

Assurance

189. The external audit process and 'signing off' the accounts are a key part of the external assurance framework for a local authority.

190. BDO are the current auditors and took over from KPMG for the 2018/19 audit process. Under the most recent PSAA process Grant Thornton has been awarded the contract and will take over for the 2023/24 accounts. The last fully signed off accounts are for 2018/19 which have been signed off without qualification. Audit opinion for 2019/20 was dependent on the work on the group consolidation of Thameswey accounts which has been delayed due to a change in the Thameswey auditors and issues with the valuation methodology. To resolve this a significant additional piece of work is now needed requiring resources from BDO, the council and Thameswey to give assurance over material balances in the Thameswey accounts [content redacted for commercial sensitivity]. BDO are also responsible for the Housing Benefit claim audit which has also not been signed off.

191. Work on 2020/21 Accounts has not started. 2021/22 and shortly 2022/23 will then need to be completed. This results in three sets of annual accounts being open, which is a risk to the council's awareness of its financial baseline.

Commercial commentary

192. The two largest commercial schemes in Woking BC's portfolio are undoubtedly the regeneration of Victoria Place in the town centre and the regeneration of Sheerwater housing stock and public realm facilities. These two schemes alone have accounted for the majority of the current £1.9bn debt level. As a result of the complexities of the loan facilities this debt level is predicted to rise to £2.4bn within the next two years. Added to this is the complex arrangements by which the council has decided to deliver and manage these major projects, placing 100% of risk with the council and this is a key factor contributing to the council's current precarious financial position.

193. The review found that, by-and-large, this situation is well understood by the Council Leadership Team (CLT) and there are actions in place to reconfigure and have greater control over these schemes. Despite the council's finance and service plan, these actions appear to be taking place outside of the 'Business as Usual' of the council. This leads to the conclusion that, despite many initiatives and advice being actioned there

is no overarching strategy for the whole situation under the council's control. There is a huge amount of council energy and resource (both officer and member) being expended on remodelling of business plans, financial models and programming to try to manage the relationship with their subsidiary companies and regeneration projects. The focus of the CLT should not be distracted away from managing the council's services on behalf of its communities.

Commercial strategy

194. There are a few new initiatives either in development or in the early stages of implementation. These are the Fit for the Future Strategy, Corporate Asset Management Strategy, Thameswey Business Plan options appraisal, Commercial Strategy review for Victoria Square (Woking) Ltd (VSWL) and the Medium-Term Financial Strategy. Although these are linked at several points the council is yet to develop a robust commercial strategy that will support the Council in paying down its current debt burden.
195. There is no further capacity for the council to make new investments or borrowing in its current circumstances. However, there will be a need to invest in the new structures to improve management information and commercially to improve their management and returns on their commercial estate. It is recognised that this will be hard to achieve against a backdrop of a potential s114 regime, but their asset portfolio is the key area in which the council can generate capital receipts to reduce debt.
196. Following further discussion with the senior team the opportunity to develop a commercial strategy to manage the two major investment projects and to leverage its property investment portfolio more effectively was discussed.
197. The council commissioned Porter Brook Associates to review and recommend a strategy for Victoria Place and the wider town centre. The review team has not seen the second draft final report from Porter Brook but have interviewed their principal consultant.
198. Following established business planning processes, it is recommended that the council's senior team clarify their commercial goals for Victoria Place, their objectives by which success in achieving goals will be measured and the strategies that will be deployed to achieve objectives. Once this work has been completed a second phase of work may require a different partner who can drive delivery of the strategy(ies) and drive business inward investments.
199. What is accepted by the council is that they do not have the capacity nor expertise to do this alone. The review team's recommendation is that the council develop a small but effective intelligent client function to oversee this, and other, strategic relationships. It should be noted that VSWL and the investments that have gone into Victoria Place are very complex and have developed over time with minimal oversight or application of due diligence and transparency. This short review has not been able to take a deep dive into the complicated arrangements and pressures.

Future debt costs

200. The borrowing requirement is largely driven by the investment in the Thameswey Group of companies and VSWL. The total capital financing requirement or CFR is

forecast as £2.1m in 2022/23, reaching £2.4bn by 2025/26. Of this £2.4bn, £1.7bn is for their capital investments, £522k for general fund services and the balance for the HRA. It should be noted that the February 2021 Capital Strategy included a £3bn CFR for 2024/25.

201. As part of the role of SAG and the business plan review, work is being carried out to minimise the investment required in future years and this has been reflected in the CFR position.
202. As of 31 March 2022 (and as set out in the February 2023 Investment Programme Report) the council had £1.18bn of loans of which £1.15bn are to VSWL and the Thameswey Group of Companies, with a further £161m due to be advanced in 2022/23, which includes the last substantive commitment to VSWL. Most of the lending beyond that date is to Thameswey Housing Ltd and Thameswey (Sheerwater). Shareholdings at that date equal £37.8m, of which £31.2m is with Thameswey Ltd. The council are scheduled to borrow £173m in 2022/23, £118m in 2023/24 and c£110m per annum in 2024/25 and 2025/26 by which time the majority of the projected borrowing is completed.
203. The loans are split between long term debt support and a revolving loan facility. For the years in the business plans where the profits are not sufficient to meet operating costs and loan repayment costs, the companies take further loan advances through a revolving loan agreement. These are within the limit of the approved loan facility and the overall level of borrowing agreed as part of the business plan. In addition, the Council does make a margin on some of the loans. This was to spread the benefit of the regeneration scheme to the Council over the life of the scheme. This arrangement is being reviewed. As mentioned earlier in the report the position has been reviewed by EY. The review recognised that company losses were forecast in the short-term reflecting the long-term nature of the business plans and / or the development being undertaken.
204. The gross capital financing budget is £62.1m for 2023/24 rising to £67m in 2025/26. The net budget after repayment of interest is considered is £18.8m rising to £19.3m. The increase in borrowing costs has been factored into the revenue budget position.
205. The structure of the funding agreements with Thameswey and VSWL mean that the increases in borrowing costs is passed directly on to the companies so, to a certain extent, the council is correct in stating that it is insulated from the impact of the increase in borrowing costs. However, given that working capital is also provided to support the company's cash flow to repay the loans, an increase in the cost of the loan may ultimately lead to an increased working capital support and hence the borrowing requirement.

Investment decisions – debt levels and repayment timescales

206. The previous investment and borrowing decisions leave a legacy for the council and pose the biggest threat to its future financial resilience. Although work has started, there is currently no long-term commercial strategy in place.
207. Support needs to be provided to assist the council in developing its longer-term commercial strategy and sustaining the current arrangements until a resolution can

be achieved. In order to resolve the current arrangements and avoid a more significant write off of debt, the revolving credit facility support and some investment will need to be continued. The current investment plans to continue require c£100m borrowing per annum. The strengthened client-side arrangements recommended in this report along with some form of external support and oversight will be critical to ensuring effective management of risk and the move to more sustainable long-term arrangements.

208. The council is largely insulated from the increase in capital financing costs whilst the revolving credit arrangement remains in place. The bigger risk is the lack of provision previously made to protect against non-payment of debt. When the changes to the MRP code are implemented, provision does need to be set aside. This may well be unaffordable for the council and the risk that the loans will need impairing due to the reduction in asset values cannot be mitigated from within the council's budget.

Oversight of commercial and investment risk

209. Measures are currently being implemented through the Shareholder Liaison Service to provide senior officers and members, who have been appointed to the board of Thameswey and VSWL, to improve understanding, decision making and direct the forward strategies of both companies. However, having reviewed a recent paper from the Shareholder Liaison Service to the Shareholder Advisory Group on 8th February 2023, it is considered that the two recommendations made lack sufficient commercial analysis of risks for a fully informed decision to be made.

Wholly owned companies

210. The Council currently has 23 wholly owned companies some of which are inactive and the majority are set up to deliver small community support services. Ownership of these companies and a plan to reduce their number, or reliance on the Council, is being developed. The review team concentrated on the relationship with the two major company holdings, these being Thameswey Group (100% owned by the council) and Victoria Square (Woking) Ltd (a 48%/52% joint venture with Moyallen Holdings (Woking) Ltd).

211. Thameswey Group comprises 13 companies separated into two broad sectors, housing regeneration/development and energy. Originally set up in 1999 to spearhead the council's carbon reduction target commitments, the remit of Thameswey was extended in 2009 to include residential and commercial schemes across the borough. Thameswey Group is reliant on loan facilities from the council and has stated that without continued funding support from the council there is significant doubt in their ability to continue [content redacted for commercial sensitivity].

212. The introduction of the Shareholder Liaison Service and the Shareholder Advisory Group (SAG) coupled with the changes made recently to the directorship of the Thameswey gives greater comfort that high-level governance of Thameswey Group and VSWL is much improved. However further development of the reporting content from the Shareholder Liaison Service to the SAG, in particular commercial risk analysis to underpin and fully inform decisions is necessary.

213. It is also recommended that tighter control of the relationship at a (tactical) project level will improve transparency over draw down of loans and expenditure. The Fit for the Future programme sets out clear intention to focus on best practice project (and contract) management. This will give greater confidence that there is strong oversight of wholly owned companies at strategic and tactical delivery levels.

Assistance and support to Council Companies

214. Any support provided by a council to a trading company counts as assistance, whether in cash or other forms. Therefore, significant subsidies in grants, assets, or services could be deemed state aid, which is regulated under European competition rules, which has now been replaced by the UK Subsidy Control Act 2022.
215. It is important to note that state aid and subsidies can take many different forms, and includes soft loans, grants, guarantees, overly favourable contracts, and soft support such as free office accommodation or services. To avoid issues with state aid, the trading company should pay commercial rates for all staff time, premises, payroll, finance, HR, assets, access to IT systems and other support it gets from the local authority. The local authority also ought to avoid treating a local authority trading company more favourably than it would treat any other third-party contractor.
216. It is commonly argued that state aid restrictions do not apply between local authorities and their Teckal vehicles (companies established by local authorities to provide services back to it/them), based on the argument that this is an internal contract and would thus not have an impact on competition. However, this is a difficult argument to maintain and is very unlikely to be successful, especially if the company is allowed to trade outside of the council, with third parties.
217. There is also the requirement to achieve 'best consideration' for the disposal of a local authority asset including land, irrespective of whether land transfers are to externally joint ventures or wholly owned companies. Transferring land or property assets to internal or external companies will also attract Stamp Duty Land Tax (SDLT) and this would occur again at final sale effectively paying SDLT twice. Until assets are ready for final sale then transfers should not be made. The Review team have not had the opportunity to review all the arrangements regarding the transfer of land and assets but if this duty is not met, or consent achieved, then the transactions are potentially ultra vires.
218. Assurance has been given that the position of state aid had been considered at the outset of these company arrangements, but the documentation and advice has not been examined and there was no reference to external advice being sought in the 2016 reports. This type of advice is required to be taken regularly and to date the council has not yet reviewed its position on state aid. The council needs to undertake this exercise as soon as is possible.

Commercial income

219. The council's assets currently generate c£30m of income annually. This is made up of c £22m from commercial properties and c£8m from car parking. Both income streams are subject to volume variations. Until there is a clear commercial strategy to maintain the income from major investments such as Victoria Place then it is difficult to predict how stable this will be. The Fit for the Future programme will be critical in ensuring that projected benefits from investments are realised or adjustments to forecast are made.

220. The council has commissioned a Property Asset Management Strategy for its existing operational, office and commercial estate. At the time of the rapid review this was not available for the review team. It will be critical that this strategy maximises the value from the estate and reduces operational cost.

Commercial decision making

221. From our discussions and interviews a picture emerges of strong senior level ambition to drive through the redevelopment of the town centre and the regeneration of Sheerwater. Some of the officers who were at the council at the time these decisions were made commented on the lack of involvement or transparency of what was being decided. The information and presentations made to Council, that have been seen by the review team outline compelling cases and forecasts for the developments and these formed the basis of approvals given. Some members felt that there was not enough commercial information for them to be fully informed on the decisions to be taken. What is clearly apparent is the fact that there was little consideration, when pushing through the schemes, of how the Council would manage the new developments to maximise returns as they became operational. There remains a clear absence of expertise and capacity to fulfil the Council's role as an 'intelligent client'.
222. The main commercial activities took place between 2016 to 2019 including the approvals of Sheerwater and the Victoria Place redevelopment and most of the major acquisitions. The model adopted for the regeneration of Sheerwater and Victoria Square and the Town Centre was one where the local authority provided the financing and took all the risk.
223. For example, the original model for the Sheerwater Regeneration scheme involved a total investment plan of £372m financed through the sale of properties. Development was to be carried out by the council wholly owned development partner, Thameswey Developments Ltd, to avoid profit being paid to private developers to ensure that the affordable homes could be delivered and rents would be affordable. Thameswey Developments would access a revolving loan facility of £76m for eight years to provide working capital to cover the development financing costs, including the interest on the loans from the council. This revolving loan facility is funded through the council loans to Thameswey Developments and hence through Prudential Borrowing. Properties would then be sold either on the open market or for affordable homes, to the subsidiary company Thameswey Housing. The council would borrow up to £129m to finance share capital and a loan facility for Thameswey Housing Ltd to acquire those homes based on a 75%/25% debt/equity split. All the financing and development risk ultimately sat with the council.
224. The models for both Victoria Square and Sheerwater have changed significantly over time since the original business cases were agreed.
225. Some common features in the historic decision making for the investments included:
    - The reports were transparent in the financial implications and decisions. They were presented to Cabinet and Council meetings and as such did fulfil the requirements of the constitution.

- Financial assurance reliance was placed on externally prepared cashflow models as opposed to a financial investment model. The reports did not consider the return on investment or the VfM of the investment.
- There was no evidence of a full options appraisal. An appraisal of alternative options was limited which could have led members towards the decision of supporting the recommended approach.
- There was limited evidence of the use of external advisors to inform the decision. Advisors were used to prepare the cashflow model, prepare valuations and for Sheerwater external legal advice was sought for the CPO process.
- The reports did not include evidence of external legal and tax advice for the company structures to be established, for the consideration of state aid or evidence of the requirement to achieve best consideration in any asset transfers. Similarly, there was no evidence of the financing arrangements proposed.
- The reports did not outline any external financial appraisal to support scheme viability and the assessment of value for money.
- The risks of the local authority taking both the financing and development risk do not appear to be clearly highlighted or adequately assessed. The impact of the level of borrowing and the development and financial risk sitting solely with the council was not adequately considered.

226. In house capacity and skills were not strengthened to deal with investments of this magnitude. Whilst member oversight panels were put in place, the council lacked the project grip and commercial skills to manage these developments. Both projects experienced significant scope creep and cost pressures over time resulting in the debt requirement to be considerably higher than first envisaged in the initial reports.
227. The review team were informed that previous decision making was clustered around a few officers and members and while decisions were transparent and constitutional, there were gaps in the reports for the decision-makers. The potential acquisition of Victoria Square car park was described by interviewees as an example. Briefings to members covered issues of control and receiving income, but not the need to get working capital into VSWL. Thameswey was viewed as a delivery arm of the local authority rather than its own company, with little recognition of the need for a strong council client side (or the resources needed) to manage it.

Improvements to commercial governance

228. The council have recognised that historically company governance had not been robust enough. Steps have been and are continuing to be made to change this. A report to cabinet in July 2022 resulted in changes to company governance which was put in place by October 2022.

229. The EY medium term financial resilience assessment recommended:

Financial Strategy and Planning □ Prepare a response to the MRP consultation □ Structured review of policy and regulatory change □ Review revenue reserves	**Financial Governance** □ Challenge high-cost service expenditure □ Develop a financial resilience strategy □ Evaluate the reporting and business intelligence landscape
Financial Control □ Develop a shareholder centre of excellence that strengthens strategic finance □ Strengthen the contract register and commitment tracking □ Review the quality of financial capability and capacity	**Commercial Oversight of Investment Performance** □ Undertake an appropriate level of scrutiny on companies □ Develop an Asset Management Strategy □ Define Place Making strategic objectives and investment criteria.

230. Progress is being made on all of the above. The review of company governance is based on best practice from Local Partnerships and CIPFA. In July 2022 the Executive approved a number of new measures to improve company oversight and £150k funding to establish two new posts to support the arrangements which are:
    - The designation of the Leader of the Council as Shareholder Representative with responsibility for oversight of all shareholder decisions.
    - Shareholder Agreement – ensuring clarity on reserved matters and ensuring the requisite documents are in place: the Business Plan, Articles of Association, Shareholders Agreement, financial agreements and business plan.
    - Establishment of a Shareholder Advisory Group – a sub-committee of the Executive and ensure the necessary oversight is in place. Responsibilities include monitoring performance, returns on investment and risks and opportunities. SAG will have three separate meetings for Thameswey, Victoria Place and other company matters which are to be held quarterly. Membership will include Members of the Executive appointed by the Leader, the Chair of the Overview and Scrutiny Committee, a member from outside the Executive will attend. The Section 151 Officer and Monitoring Officer will act as advisors but this is not sufficient expertise.
    - Strengthening the role of scrutiny as the Scrutiny Chair will be able to take items to the Scrutiny Committee that warrant further attention.
    - Establishing a shareholder liaison service to provide support.
    - Changes to board membership to take councillors off company boards with membership being the Chief Executive, independent directors with appropriate expertise and other council officers as required.

231. Work has been ongoing for about 18 months and the council have estimated that there are a couple of years to go due to the sheer scale of the task. There are around 20 joint ventures and the Shareholder Group are reviewing them all. The Thameswey company structures are complex and need consolidating and the council has bought

several companies which need to be properly understood. The previous Chief Executive acted as shareholder. Record keeping was limited.

232. Progress includes:
- There are whole council briefings in advance of decisions.
- Directors have all had formal training. A conflict of interest process has been established. The CLO and CFO are on the client side and councillors have been taken from company boards.
- A directorships file has been set up.
- The new shareholder board and shareholder advisory group have started.
- The constitution is being reviewed.
- The recent Mazars internal audit report update to the Standards and Audit Committee in November 2022 has rated the 'Corporate Governance Arrangements' review substantial assurance.

233. There is limited capacity within Legal Services and Finance and not all the resources are in place. A new project officer has started and the Head of Service role is out to recruitment. An ex Section 151 officer from a core city is providing financial support to the Shareholder Advisory Group (SAG) which has been described as the de facto shareholder support. It is important that SAG has access to commercial finance and development, legal and property expertise to support decision making.

234. There are positive signs that the SAG is starting to have an impact. The Thameswey Business Plan was not initially endorsed by SAG who requested a revised one year business plan with a number of options to be reviewed. The Business Plan is being finalised for the end of May 2023. [Content redacted for commercial sensitivity.]

235. Managers in VSWL and Thameswey companies are starting to see changes being made. The Thameswey leadership team described how they now feel as though they are being held to account. They would welcome a true client function – if they are to be judged commercially, they need a formalized, contractual relationship and this increased rigour is welcomed.

236. The council needs to review the capacity in place to support this work. At present a lot of reliance is placed on external resources as there is insufficient commercial expertise to support SAG in its role. The finance team need a commercially aware accountant to support the option appraisal, monitoring and drawdown process. The finance team also need access to the correct commercial advice and support to help work through potential options for the future.

Future financial risk

237. Commercially the council is overstretched and remains reliant on further support to continue to pay down its loans. The CLT has put in place several initiatives and actions to get to grips with the current situation but yet to set out, in a structured overarching commercial strategy, what its ambitions are to maximise the assets that it now holds. Until this is in place the council remains open to commercial risks brought about by a piece-meal approach to challenges and opportunities the council now faces. Before confidence can be restored in the council's management of future financial risk there

must be a clear Commercial Strategy, more robust commercial risk assessment in all business cases put forward and Commercial expertise in the council.

Debt levels

238. As has been previously noted a sale of assets would be an inappropriate course to recommend and would be very detrimental to the council financial position. The council must therefore consider how it can best use its asset base to reduce its debt levels and maintain an overall balanced budget.
239. In summary, it is considered that the historic decisions made to invest heavily in the redevelopment of Victoria Place and the regeneration of Sheerwater were made with the intention to raise the profile of Woking in the highly competitive Surrey borders region. What has not been built into the business case for such major investments is consideration of the expertise and capacity of a small borough council to manage projects through to final maturity or exit.
240. It is clear that the council will need experienced commercial support to enable them to realise the full benefits of their investment. Other support can be provided by Crown Commercial Services whose frameworks for property management and car park management can be accessed quickly significantly reducing procurement times.
241. The recommendation to put in place a Strategic Oversight Panel will be guided by the strategy and will measure progress against milestone events. Until this is in place and the Council has a settled budget then it is too early to comment on future borrowing.

The commercial way forward

242. It is recommended that the council use a tried and tested model for commercial business planning that will aid them in taking a structured approach to developing their commercial strategy. In common use in central government is the VMOST model (Vision, Mission, Objectives, Strategies and Tactics). Alignment of commercial objectives with the overall vision for the council and a mission to maximise commercial benefits from its assets whilst reducing debt will be paramount for the future success of the council. Once the council is clear on the immediate commercial objectives, fully informed by expert advice on the planned use of its full property portfolio, then the commercial strategy(ies) to deliver objectives can be developed and implemented. Specific commercial risk assessments, set against potential rewards for the council must form an integral element of the strategy. This will allow members to consider any trade-offs that might be taken to increase reward/reduce risk against. Other investment properties should be considered for disposal on a case-by-case basis as discussed.
243. Many of the initiatives that can be appraised and followed will be influenced by commercial strategy and driven by the need to protect and improve the council's financial position. The review team has discussed with CLT members, a number of options that could be assessed for their viability and potential to reduce commercial risk for the council whilst contributing to reduction in debt levels and delivering promised schemes to its communities. The review team also appreciated the complexities of the current major investment projects in Victoria Place and

Sheerwater, however it is important that all initiatives are appraised to satisfy the need for continued long-term support.

244. In broad outline it is recommended that the council continue to appraise the following initiatives:
- The approach taken to car park management and ownership ensuring that the council protects its minimum income requirement from these assets.
- Using the council's investment property portfolio to generate short term capital receipts or to generate sustainable rental income.
- Reviewing the delivery model for Sheerwater and, where appropriate, bring forward the development of open market properties for sale.
- Consider the value of non-core services that could be wrapped into new partnering arrangements.

245. As stated previously, the review team recognise the complex nature of the current situation and are also cognisant of the pressure that is placed on the small team leading the programme to work through this challenge. We also are aware of the commercial and market expertise that will be needed to make the most of the opportunities that are now presented. It is therefore considered that procuring and engaging with new and effective private sector partners to complement the support provided by other organisations will be necessary.

Commercial next steps

246. The review team recommend that the council:
- Carry out appraisal of the initiatives outlined above.
- Set clear objectives for each initiative so that specific needs of the council are enshrined in any procurement process following appraisal.
- Carry out early engagement with the market to establish what can be achieved and what risks investors or suppliers will not tolerate.
- Develop a clear view on commercial risk apportionment and management.
- Develop a programme that can be delivered by the available resources or identifies where additional resource is required.
- Ensure at every stage that full and clear detail is presented to council, allowing fully informed decisions to be made and considering trade-offs that might have to be taken.

Part Two, 5 May 2023

Scope and purpose

1. Following the completion of the original review work and report, Woking Borough Council ("the Council") continued work to understand the extent of its financial challenges. In April, the Council provided further information to DLUHC setting out increasing risks to its financial position. [Content redacted for commercial sensitivity.] Given the seriousness of the developing situation with respect to the Council's investments, DLUHC commissioned a short extension to the review. The scope of the extended work is to provide the government with an assessment of the short- and longer-term decisions facing the Council; the sufficiency and adequacy of the Council's plans to mitigate immediate risk; and where the Council needs priority support to achieve the best outcome.

Executive summary

2. Since the original review, the Council has continued to undertake work to progress its understanding of its financial position. This includes an external review of the Council's lending and borrowing arrangements, impairments, and the position of its companies (the "investment review"). An external review of the Council's Minimum Revenue Provision (MRP) policy has also been completed. The multiple pieces of work are providing a clearer picture of the financial situation.
3. Although the issues are consistent with the findings from Part One of this review, the financial issues are more severe and immediate than initially thought. Despite the efforts of the current leadership team, it is clear that the Council cannot manage the scale of the challenge alone and needs urgent support to navigate through the decisions and actions needed in the coming weeks.
4. The external MRP review has indicated there could be a £40 million charge on the budget annually, rather than, according to the Council, a £11.9 million charge annually in 2021, rising to £23.4 million annually when averaged over a 50-year period, noted in the initial report. The Council were not making appropriate provision and will need to increase future charges to be compliant with the statutory duty. There may also be a historic underspend that the Council will need to correct; the exact value of this is still being determined. The Council are not able to absorb this additional cost.
5. Work undertaken by the investment review, and further legal advice the Council have taken, indicate that the Council's arrangement of borrowing from the Public Works Loan Board (PWLB) to lend to its companies for revenue purposes, some of which is paid back to the Council to meet the interest costs of those loans, is probably *ultra vires*. [Content redacted for commercial sensitivity.]
6. [Content redacted for commercial sensitivity.]
7. The scale of this issue is unprecedented. The Council has a net budget of £24m and core spending power of £14 million. The scale of the likely deficit relative to the size of the Council means that there is no realistic means by which the Council can return to financial sustainability on its own. [Content redacted for commercial sensitivity.]

8. Taking into account the findings of part 1 of the review, and the evidence that has come to light since, the complexity and scale of the task facing the Council cannot be understated. The new leadership of the Council is taking the right steps. However, it does not have the capacity or capability to address a challenge of this scale without additional support. Historically, record keeping has been poor and this hampers the Council's ability to understand their own position. Decisions made several years ago have put the Council in an untenable situation and resulted in the Council failing its best value duty. As set out, on the current trajectory the Council will not rectify these issues itself and will continue to fail its best value duty. The Council will require significant support, including statutory oversight.

Report findings

Companies and associated borrowing

9. [Content redacted for commercial sensitivity.]
10. [Content redacted for commercial sensitivity.]
11. [Content redacted for commercial sensitivity.]
12. [Content redacted for commercial sensitivity.] As a matter of urgency, the government needs to take action to make sure the Council is supported and that the appropriate expertise and capability is in place.

Overall financial position

13. [Content redacted for commercial sensitivity.]
14. The Council commissioned an external review of its MRP policy, which has now concluded. Part One of this review made clear that there was a risk the Council had been underpaying MRP, and this could result in a need to increase the charge in future. The MRP review has found that the underpayment is more than the £11 million, and that the Council will need to increase future payments by £40 million. In context, the Council's gross service expenditure is around £44 million. The Council may also need to make additional charges to address prior year underpayments from 2015/16 onwards, adding to the overall cost pressure; this is still to be determined.
15. The review team understands that the Council's total external borrowing is £1.8bn, most of which is from the PWLB. The original review details that most of this debt has been incurred by on-lending to its companies, to finance both capital spend and to provide the revolving loan facility (described in paragraph 5). The Council is currently using the loan repayments from its company to meet its own interest costs to the PWLB. Therefore, as well as incurring the impairment charge, the Council will also need to determine how it can meet its own debt liabilities, and the cost of meeting both the ongoing interest charge and increased MRP cost. The Council are currently working with an external partner to determine the modelling options in debt management.
16. In terms of future borrowing and capital spend, the Council is likely to require an estimated additional £250 – 300 million of borrowing this financial year. This will include the refinancing of c.£200 million of loans, and c.£25 million of contractual obligations carried by the Thameswey group (as described in paragraph 11). The significant office property estate owned by the Council needs fitting out and refurbishment in order to

maintain the revenue they are currently receiving. The Council predicts this to be a further cost of around £25-30 million to bring the office buildings up to standard; work on evaluating this cost is currently concluding within the Council. The exact timing of this borrowing need is not yet clear to the review team, but the Council may approach government within 2 to 3 months. Further work will be required to determine the exact borrowing need. [Content redacted for commercial sensitivity.]

17. The current revenue budget for the Council has a gap of c.£9.5 million in 2024/25, which could increase throughout the year. The Council does not currently have a costed maintenance programme for their current assets and this quantum will also need to be included in their future Medium Term Financial Plans (MTFP).

Nature and urgency of additional support required

18. The key priorities can be divided into three inter-related workstreams: handling the technical legacy of the borrowing and lending arrangements; effective management of the asset portfolio; and a wholesale review of the size and shape of the Council to quickly identify ways of cutting costs to bring the organisation's spending in line with its size. The details of these workstreams are outlined below.
    a. **Resolving the legacy issues on debt and lending arrangements.** The Council faces a legacy of technical issues including the revolving credit facility, the portfolio of assets and the ultra vires factor of the revolving loans. [Content redacted for commercial sensitivity.]
    b. **The Council need to develop and enact a strategy to achieve the best possible value for their property portfolio.** This may include maximising profit of the property portfolio which would include increasing capacity within the property team and seeking external opinions on how best to do this. The Council require help in the management of their asset stock, and this is probably best achieved if passed out of Council control. There are different options to achieve this, including partnering with development companies or central government.
    c. **Transformation of the Council to achieve savings and efficiencies.** The Council must prioritize service transformation to achieve cost savings and efficiencies commensurate with its size. This will require difficult decisions, including rationalising some 'County-level' services and developing exit strategies for other services. The Council needs to address issues with its treasury management and capital accounting systems, which require consolidation and additional specialist resource The Section 151 officer is working to position the Council to tackle these issues on a macro scale. However, the Council's limited experience with service transformation on the required scale highlights the need for expert support to manage this process effectively.

19. The Council will need government support. Senior Management recognises that the Council is in need of additional support and that it does not have the resource base to service the debt alone. The net revenue budget is £24 million, which leaves no room for the repayment of debt of this large a scale. There is no realistic route to the Council returning to financial sustainability alone. Finding a solution is urgent: there are concerns that the debt will increase further once a Section 114 is issued, and further

Section 114 notices may be required going forward. The Council will need to undertake significant service transformation and consider their future operating model.

20. In conclusion, as a result of past investment decisions, the Council has failed its best value duty leaving an unprecedented legacy for the current Leadership Team, which they have not been able to address to prevent financial failure. It is evident that the Council does not have the capacity and expertise to address the scale and complexity of these issues, and so it will continue to fail its best value duty. Resolving the issues and moving the Council back to a place of financial stability and value-for-money for the taxpayer will require significant support, including statutory oversight. There is a need for commercial and financial support including capital, legal and forensic accounting specialists. The Council will also need additional leadership capacity to help deliver this swiftly [content redacted for commercial sensitivity]. There are critical decisions that need to be taken in the next 2-3 months, for which immediate expert support is required.