

STROUD DISTRICT COUNCIL
STRATEGY AND RESOURCES COMMITTEE

**AGENDA
ITEM NO**

11 APRIL 2019

6b

Strategy and Resources Committee, 11 April 2019 – Agenda Item 5

Report Title	SUPPORT FOR THE FOUNDATION OF AVON MUTUAL
Purpose of Report	To agree an allocation of £50k to support the foundation of Avon Mutual
Decision(s)	<p>The Committee RECOMMENDS to Council :</p> <p>a) to approve the use of £50k of the Business Rates Reserve for purchase of shares in Avon Mutual.</p> <p>b) to delegate authority to the Head of Finance in consultation with the Head of Legal to conclude the share purchase.</p>
Consultation and Feedback	<ul style="list-style-type: none"> • Member Presentation Evening
Financial Implications and Risk Assessment	<p>This proposal would allocate £50k of the Business Rates Pilot funding for 2018/19, currently estimated at £793k, for the purchase of founder shares in Avon Mutual.</p> <p>Although the Council will receive shares this funding is not recommended by officers solely as an investment for financial benefit. This is a result of the high risks from investing in the organisation at this early stage.</p> <p>This investment is not part of the Council's Treasury Management processes but a capital programme addition.</p> <p>This investment is outside of the Council's normal risk parameters and the decision should be made in the context of there being no guarantee of the success of organisation or return of the funding.</p> <p>For budgeting purposes members should regard this decision as effectively grant funding as it will reduce the balance of the business rates reserve.</p> <p>Andrew Cummings - Head of Finance & Section 151 Officer</p> <p>Email: andrew.cummings@stroud.gov.uk</p>

Legal Implications	<p>There are two factors to consider in relation to legal implications, namely the legal power the Council has to invest and secondly any state aid considerations.</p> <p>The Council has a power to invest for any purpose relevant to its functions by virtue of section 12 of the Local Government Act 2003. The Council also has a General Power of Competence to do anything that individuals generally may do by virtue of Section 1 Localism Act 2011.</p> <p>Legal officers have considered state aid implications and are satisfied that the proposal is compliant with state aid law.</p> <p>Patrick Arran – Interim Head of Legal Services & Monitoring Officer Email: patrick.arran@stroud.gov.uk</p>
Report Author	<p>Andrew Cummings – Head of Finance & Section 151 Officer Email: andrew.cummings@stroud.gov.uk</p>
Options	<p>The Committee may choose not to support the foundation of Avon Mutual and allocate the reserve elsewhere.</p>
Performance Management Follow Up	<p>2018/19 Outturn Report</p>
Background Papers	<p>Appendix A – Avon Mutual Presentation Appendix B – Assessment for Capital Programme</p>

1. Introduction and Background

- 1.1 On 18th October 2018 Stroud District Council agreed a motion in support of local wealth building. That is the process by which anchor institutions can use their policies and financial spending power to help grow their local economy. This motion included an acknowledgement that co-operatives and local banks were one of the four key strategies of local wealth building. Council resolved to create a plan by which the practical strategies of local wealth building can be used to achieve SDC's vision and corporate priorities.
- 1.2 On March 20th 2019, Jules Peck and Dena Brumpton of Avon Mutual, delivered a presentation to Members about the proposal to form South West Mutual – regional banking for inclusive growth. A copy of the presentation can be found at Appendix A. This appendix demonstrates how the bank would be set up, what services it will deliver and the overall benefit it will deliver for the region.
- 1.3 The Council is a member of the Gloucestershire Business Rates Pilot for 2018/19. The financial arrangements for that pilot result in additional one-off funding for the member authorities. The share for Stroud District Council is currently estimated at £793k as has been reported to this Committee. This

funding is to be added to the Business Rates reserve for allocation as projects are identified.

1.4 This Committee has previously set out the principles for the allocation of this funding. The proposal is that funding may be allocated to projects which support;

- Local Business
- Financial Sustainability of the Council
- Local Wealth Building
- A zero carbon district

2. AVON MUTUAL

2.1 Avon Mutual is an organisation which has been set up to seek a banking license to operate a high street bank for households, SMEs and other organisations within Bristol, Bath, North and North East Somerset, Gloucestershire, and Wiltshire. It is one of 18 regional co-operative banks being launched by the Community Savings Bank Association.

2.2 When established as a bank Avon Mutual will offer banking on the mutual model. It will be a mission led bank with a focus on promoting sustainable and equitable prosperity for the region. The mission is to build financial inclusion, significantly increase the proportion of bank lending going to the “real” economy and SMEs instead of the financial economy, build economic resilience and bring about a renaissance of customer service, relationship banking and trust.

2.3 Avon Mutual’s own summary of their objectives is

- Mission-led bank promoting sustainable and equitable prosperity for the region
- Owned by its customers and committed to honest, simple and transparent relationship banking
- Serving the financial needs of people of ordinary means, local community groups and SMEs
- Providing a full range of banking services from 9 staffed branches and 21 automated branches

2.4 To fund the initial phases of the process of establishing a bank, the new mutual is seeking £500,000 of initial funding, through the issuing of Founder Shares. This is to fund

- conducting detailed market research and business planning,
- continuing board recruitment,
- commencing pre-authorisation stage of banking licence application,
- Secure commitments from investors for the £20m of capital required to commence full banking operations.

2.5 The mutual has made considerable progress attracting first round support and it is believed that a number of other public authorities are also considering investing.

- 2.6 Making an investment at this early stage can be seen as a positive action in support of the Council's commitment to local wealth building and is in line with the principles agreed by this committee in relation to the allocation of the Business Rates pilot funding.
- 2.7 Investing at this early Founder Shares stage is a higher level of risk than investing later in the process. The mutual does not yet have a banking license and until one is obtained will not be able to trade. If the mutual is successful in receiving a banking licence and the bank starts trading, based on current projections, it is envisaged that dividends of an estimated 7.5% will be payable from around Year 5. This is a targeted dividend and is not guaranteed in any way.
- 2.8 The Mutual recognises that investing at the early stage is an additional risk so investors in founder shares will receive three times as many shares for their money as later investors to help compensate for that level of risk. As all of the Council's shares will each receive the 7.5% dividend if a bank is successfully established and becomes profitable, the potential rate of return to the Council could be around 20% per annum.

3. Proposal to invest in the mutual

- 3.1 It is proposed that the Council uses funds from the predicted business rate pilot to purchase shares to the value of £50k. These shares may provide a return in the long term if a bank is established and reaches profitability but this is of course not guaranteed. The business rates pilot represents funding for the Council to be put towards strategic priorities and therefore represents a significant opportunity to support projects such as this which would otherwise fall outside of the Council's base budget.
- 3.2 The final confirmed amounts to be received from the business rates pilot will not be known until some-time after the end of the financial year. However, with the end of the financial year being close, recent monitoring suggests that there would have to be a very significant fall in business rates income within the County for the gain from the pilot to be eliminated. The Council already has a business rates reserve from which this share purchase will be funded in the event of there being insufficient pilot gain.
- 3.3 The Mutual is following a clear process in their route to become a bank and have considerable banking expertise on their board. However, it should be recognised that this is an investment in a start-up organisation which does not yet have the appropriate license to operate in its chosen field. There is therefore a risk that the mutual will not achieve its stated objectives.
- 3.4 If the organisation were to be unsuccessful and a bank not be established it is very unlikely that any of the £50k contribution would be recoverable.
- 3.5 It is therefore not recommended to make an investment solely with a view to generating a financial return on that investment. As there is no guarantee of a return the £50k funding should be viewed, in budgetary terms, as akin to a grant

to support the aims and principles of the Mutual. It is also in recognition that its principles of providing co-operative banking to businesses including SMEs, and to individuals are in line with the Council's own priorities. As such, whilst the legal effect of the proposal is to invest in a company and a share purchase, it is effectively akin to a grant to support the local economy rather than an investment intended to deliver an economic return.

- 3.6 As it is a share purchase the £50k will be shown as an investment within the Council's financial statements in the published accounts. However, it is not regarded as such for budgeting purposes as it is fully funded from the business rates reserve as the return is not guaranteed. The accounting treatment for the purchase of shares is that it is treated as capital expenditure which will be funded from the Business Rates Reserve. The addition of the share purchase to the capital programme, to be funded from the Business rates reserve, requires Council approval.
- 3.7 The addition to the Capital Programme means that an assessment is required, in line with the principles of the recently adopted Capital Strategy. This has been completed and is shown at Appendix B. This demonstrates that the investment has been subject to the same form of appraisal as all other new capital projects would be.
- 3.8 Stroud District Council would be one of the first authorities in the area to commit funding to the Mutual if Council approve this funding. Other authorities have committed support to mutual banks in their area, particularly within Greater London. In Devon South Hams and West Devon District Councils have each awarded approximately £50k from their business rates pilot to the support the foundation of the "South West Mutual". This is the sister organisation of Avon Mutual within their area.
- 3.9 The proposal to use the Business Rates pilot pot to fund the investment is made as the share purchase would meet two of the principles for allocating the business rates pilot fund. These are supporting local business and local wealth building. Co-operative banks are a key element of local wealth building and a locally run co-operative bank, with a local branch network, is likely to be beneficial to individuals and small and medium entities within both the district and the wider economic area served by the bank.
- 3.10 "Helping to create a vibrant and sustainable economy that works for all" is a key part of the Council's Corporate Delivery Plan. The support of Avon Mutual and of co-operative banking in general is in line with this corporate Council priority.
- 3.11 If a banking license is obtained and Avon Mutual becomes a bank then further funding rounds will be needed. Those rounds will be to obtain the capital that is needed to on-lend to customers. If the Council wishes it may choose to make further investment at this point in order to generate a financial return. An investment of that nature would have to be subject to full investment appraisal due diligence as with any other bank lending.

4. The next steps for the Council

- 4.1 The purchase of the shares will be completed, subject to the approval of the delegated authority, by the Head of Finance in consultation with the Head of Legal Services.
- 4.2 The S151 Officer will conduct all necessary dealings with the bank and fulfil the role of shareholder within the organisation.
- 4.3 Progress of the bank towards achieving a license and later commercial progress will be reported to Strategy and Resources on at least an annual basis or earlier if requested by the Committee of urgent circumstances require.