
A separate report is submitted in the private part of the agenda in respect of this item, as it contains details of financial information required to be kept private in accordance with Schedule 12A of the Local Government Act 1972. The grounds for privacy are that it refers to the identity, financial and business affairs of an organisation and the amount of expenditure proposed to be incurred by the Council under a particular contract for the supply of goods or services. The public interest in maintaining the exemption under Schedule 12A outweighs the public interest in disclosing the information.

Cabinet

11 April 2017

Name of Cabinet Member:

Cabinet Member for Community Development – Councillor L Bigham

Director Approving Submission of the report:

Deputy Chief Executive (Place)

Ward(s) affected:

All

Title:

Culture Coventry Trust - Financial Performance and Support Arrangements

Is this a key decision?

Yes, as it has the potential to affect all wards within the City and could have financial impact in excess of £1m

Executive Summary:

The UK's cultural sector has seen a reported reduction in budgets by over £1bn since 2010. This reduction has created significant pressures within the sector, with the reported closure of over 45 museums across this period. Nationally, cultural organisations are actively increasing their commercial activities whilst reviewing and restructuring their medium term financial strategies in order to meet these ongoing challenges.

Culture Coventry Trust ('The Trust') contacted the Council in November 2016 seeking financial assistance regarding its forecast deficit financial positions for 2016/17 and 2017/18 onwards. Financial pressures over the last 2-3 years – including through the period of extension and development of the Coventry Transport Museum and restoration of the Old Grammar School – mean that the Trust was required to utilise its cash reserves and therefore now needs assistance whilst it establishes and implements its plans for the future.

The Trust is seeking to establish a robust Medium Term Business Plan, but in order to do that, it currently requires financial support from the Council in the form of cash flow loans and deferral of the repayment of other monies owed.

Recommendations:

Cabinet is asked to:

- (1) Approve the deferral of monies owed by the Trust to the City Council in respect of the Transport Museum extension project, until April 2018
- (2) Endorse the cost reduction measures proposed by the Trust, subject to on-going monitoring by City Council Officers
- (3) Approve the funding by the Council of the one off redundancy costs of the Trust's management restructure through the provision of additional one-off grant funding
- (4) Approve in principle (subject to scrutiny by Council Officers) the provision of a loan(s) from the Council to the Trust to be repaid at a commercial rate for the following:
 - to enable the Trust to pay their next three years West Midlands Pension Fund contribution in advance;
 - for drawdown during 2017/18 financial year to enable the Trust undertake cost reduction and income generation initiatives to achieve a sustainable financial position
- (5) Subject to approval of recommendation (4) above, approve as required, the issue of a letter of comfort to the Trust confirming that the Council will provide financial assistance during 2017/18 to enable it to carry out its cost reduction and income generation initiatives to achieve a sustainable financial position
- (6) Delegate authority to the Deputy Chief Executive (Place) and the Council's Section 151 Officer to undertake the financial due diligence, negotiate and finalise the detailed terms of the loan arrangement and if satisfied as to their terms (and such other matters as deemed relevant) effect the completion of the appropriate loan agreement

List of Appendices included:

None

Other useful background papers:

None

Has it been or will it be considered by Scrutiny?

No

Has it been or will it be considered by any other Council Committee, Advisory Panel or other body?

No

Will this report go to Council?

No

Report title: **Culture Coventry Trust - Financial Performance and Support arrangements**

1. Context (or background)

- 1.1. The UK's cultural sector has seen a reported reduction in budgets by over £1bn since 2010. This reduction has created significant pressures within the sector, with the reported closure of over 45 museums across this period. Nationally, cultural organisations are actively increasing their commercial activities whilst reviewing and restructuring their medium term financial strategies in order to meet these ongoing challenges.
- 1.2. Culture Coventry Trust contacted the Council in November 2016 seeking financial assistance regarding its forecast deficit financial position for 16/17. Additionally, following the completion of the Coventry Transport Museum (CTM) extension project, restoration of the Old Grammar School and the finalisation of all grant claims, the Trust still owes the Council monies in the form of cash flow loan for the development. The Trust consider their in-year deficit to be primarily as a result of lower than anticipated visitor numbers through the development period and in the time following the completion of the development, whilst the audience base has still been extending.
- 1.3. The Trust have additional liabilities which will take effect from 2017/18. This broadly consists of additional pension fund contributions and additional storage costs as a result of the need to vacate their Sandy Lane storage facilities and move to new premises.
- 1.4. Following the merger of the cultural trusts (Coventry Heritage and Arts Trust and Coventry Transport Museum), and a couple of difficult years – including through the period of extension and development of the Coventry Transport Museum and restoration of the Old Grammar School – the Trust was required to utilise its cash reserves, the result of which is the inability currently to resolve their in-year and ongoing deficits without assistance. Reserves are integral to any organisation's successful business plan to ensure short term financial problems can be managed, so need to be reinstated as soon as they can be afforded.
- 1.5. A savings target of £0.5m from current levels of Council grant support was approved by Council Members in February 2015 to take effect from April 2017. This target was assumed to be achievable from a combination of cost reductions and income generation to be implemented from April 2017. Together with their predicted deficit, the Trust therefore needs to identify significant savings and/or additional income in order to be able to sustain the current levels of service.
- 1.6. The Trust requires a Medium Term Business Plan which needs to address all of these issues, however, it is not in a position to achieve this without financial assistance.
- 1.7. In order to help address their 2016/17 financial difficulties, the Trust have implemented a series of cost saving initiatives and has looked to identify potential income growth. Given the relatively short period of time to take management action before the end of March 2017, there were no further actions available to the Trust that would have benefitted their 2016/17 revenue position.
- 1.8. The Trust are not in a position to repay monies loaned to it by the Council in the form of a cash flow facility during the time of extension and development of the Coventry Transport Museum and restoration of the Old Grammar School. This loan facility enabled the Trust to operate whilst waiting for large ERDF and HLF Grant payments to be received.

- 1.9. The Trust are not insolvent as their cash position is still in credit. However this takes account of both deferred spend, and grant monies paid to the Trust against which future payments are committed. A positive cash position has been maintained for the remainder of 16/17, and the Trust will be able to honour immediate operational costs such as salaries, however that cannot be sustained throughout 2017/18 without financial assistance.
- 1.10. Section 2 below considers options available to both the Trust and the Council to contribute to resolving the Trusts financial difficulties

2. Options considered and recommended proposal

- 2.1. Working with Council Officers the Trust have started to consider a number of both short and medium term opportunities to mitigate the pressures faced. These options and their associated implications are discussed below:

2.2. Short Term Opportunities

- 2.2.1 Management Restructure Savings – The Trust have begun consultation on a review of their senior management structure. This will involve the deletion of senior posts and once implemented, will generate significant full year savings. The effective implementation date is June 2017, which for 2017/18 will generate a part-year saving, off set by redundancy and pension strain costs. The Trust have sought assistance from the Council to fund this liability.

- 2.2.2 Pension payment in advance – The Trust have an option to pay the next three years pension liability up front in order to a) receive a discount on the cost and b) facilitate the re-profiling of the pension cost against revenue, with lower amounts in 2017/18 and 2018/19, and a higher compensating cost in 2019/20. This arrangement would buy the Trust time to put other arrangements in place by 2019/20. However, as previously stated, the Trust does not have the finances to enable them to make the advance payment without assistance, so this arrangement would require a commercial loan from the Council, repayable over the 3 year period.

2.3. Medium Term Opportunities

- 2.3.1 Staffing Costs - The Trusts largest cost like most organisations is the cost of employing staff and the on costs that go with that. The Trust have committed to reviewing these costs to determine what alternative options and organisation benefits exist. This is however unlikely to yield any short term financial benefit.

- 2.3.2 Income Generation Opportunities – The Trust already generate income from sales and entry to certain events. The Trust are further considering how they may commercialise their offer more effectively, particularly to benefit from the potential increased profile, opportunities and wider impacts of Coventry bidding for the UK City of Culture 2021 title.

2.4. Option 1 – Reject the request from the Trust for Financial Support (Not recommended)

- 2.5. This option is not recommended as the Trust would not be able to carry out the obligations of its Grant agreement or continue to deliver services to the public. The likelihood of this option is that during 2017/18, the Trust would become insolvent, despite any savings plans they have. The ultimate impact of this option would require the Council to step in to ensure services could be maintained.

2.6. Option 2 - Endorse the Trusts short and medium terms actions and approve their request for financial support (Recommended)

2.7. Whilst not ideal, this option is considered the most favourable as it gives a greater chance of a financially sustainable service, and continuation of the service provided to the public. The importance of this continuity is evident through the aspirations of the Coventry Cultural Strategy and the city's bid for the title of UK City of Culture 2021.

3. Results of consultation undertaken

3.1 The Trust have consulted their Board on the proposals within this document and are in support of them in order to enable them to sustain provision, continue to trade and remain solvent.

3.2 The Trust's auditors have been consulted on the short term arrangements regarding the pension fund discount and re-profiling of pension fund liability and are in support of these provisions.

3.3 The £0.5m MTFS saving was approved by Members following consultation on budget initiatives in the 2015/16 budget setting process

4. Timetable for implementing this decision

4.1 The Trust need to identify savings or generate income urgently to prevent further losses and to assist them to work towards a sustainable Medium Term Business Plan. Any delay would be likely to result in them becoming insolvent during 2017/18, which would be in breach of their Grant Aid Agreement, and means the Trust would be unable to sustain delivery of current services.

5. Comments from Director of Finance and Corporate Services

5.1 Financial implications

In February 2015, the Council approved as part of its MTFS to reduce the level of grant it pays to the Trust with effect from 1 April 2017 by £0.5m. This together with the Trust's current projected financial deficit position for 2017/18, and the need to reinstate some reserves, will require the Trust to restructure its finances to ensure they have a sustainable short to medium term plan.

The cost reductions and pension arrangements as described in section 2.2 of the report will mitigate a proportion of this pressure in 2017/18 and 2018/19, as would the deferral of the cash flow loan repayment.

The combined result of all proposals still leaves a significant cumulative pressure at the end of the next financial year (2017/18) which the Trust need to address, to enable them to operate from 2018/19 on a positive basis.

In order to achieve this, the Trust would require support with their short term cash position to ensure they continue to trade solvently. This could be achieved by way of a commercial short term cash flow (overdraft) facility from the Council which they could draw down on at the point required.

Additionally, the Council may be required to provide a letter of comfort to the Trust's auditors for their 2016/17 and 2017/18 accounts to demonstrate that the Council is willing to cashflow the Trust until such time as it can operate independently.

In all cases of support, it is expected that the Trust would repay all of the loaned monies over time, on a commercial basis, to ensure state aid compliance.

5.2 Legal implications

5.2.1 There are various statutory powers available to the Council when considering to make a grant and/or investment, they are:

- The Council has a specific power to invest under Section 12 of the Local Government Act 2003; and
- The Council also has a general power to make investments/and or a grant under the powers of general competence contained in Section 1 of the Localism Act 2011.

5.2.2 The loan and grant proposals contained in this report satisfies the purposes of the Localism Act 2011.

5.3 State Aid risk

5.3.1 Article 107 (1) of the Treaty on the Functioning of the European Union ("**Treaty**") states: *"...any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market."*

5.3.2 The Treaty does not define in any more detail what constitutes state aid. However, the term has been interpreted to include the provision of grants, loans on favourable terms, the transfer of assets at less than the market rate, and tax advantages. Not all state aid is unlawful, and it is possible to justify some types of financial assistance under pre - approved mechanisms.

5.3.3 It is possible that a third party (and/or European Commission) who has not received state aid could bring legal proceedings in the UK courts for damages. Such a claim could, for example, be brought by a competitor who feels it has suffered loss because it has not been given aid.

5.3.4 A recipient can be ordered to repay all aid received over a ten-year period if the European Commission finds it has been provided unlawfully. It is no defence that repayment may force the recipient into insolvency.

5.3.5 Market Economy Investor Principle ("MEIP") can provide an appropriate mechanism to potentially justify aid to any third party following the Council's loan. A Loan does not automatically constitute state aid if the Council carries out prior due diligence that demonstrates that investments are likely to generate sufficiently high returns and that a private prudent investor would have made the same investment. (i.e the Council can invest in the proposal in return for an appropriate commercial return which would satisfy the expectations of a private prudent investor).

5.3.6 The risk of state aid is not dependent upon whether the financial return is actually ever achieved by the Council, as whether state aid exists or not is assessed at the time of the funding advanced, but there must be a realistic prospect of the financial return being achieved by the Council.

5.3.7 Accordingly the Council will be inserting relevant provisions within the loan documents and undertaking a detailed state aid analysis in order to mitigate the risk of a state aid challenge.

6. Other implications

6.1 How will this contribute to achievement of the Council's key objectives / corporate priorities (corporate plan/scorecard) / organisational blueprint / Local Area Agreement (or Coventry Sustainable Community Strategy)?

The recommended proposal will contribute to the Council's core aims of:

- ***Making the most of our assets*** – The services provided by the Trust directly support access for residents and visitors to the city to the Council's collections and the broad range of cultural assets interpreted and exhibited through the work of the Coventry Transport Museum, Herbert Art Gallery and Museum, Lunt Roman Fort and Old Grammar School. Many of these cultural buildings have seen significant capital investment, and sustaining public access to the Council's collections is central to the aspirations of the city's new cultural strategy.
- ***Improving educational outcomes*** - Coventry has a strong cultural education offer within the city, provided not only by schools and education services but also through universities, colleges and arts business. The Trust has an established role to play in creating, connecting and signposting cultural, education sector and community opportunities. The museums and services provided through the Trust promotes opportunities for all generations to learn from and develop through experiences of culture and the arts in the city.
- ***Healthier, independent lives*** – Cultural assets and services play a vital role in addressing social challenges, reducing isolation and improving outcomes for individuals and communities (Local Government Association). A review of medical literature undertaken in 2004 cited nearly 400 papers showing the beneficial impact of the arts on a wide range of health outcomes (Staricoff, 2004), whilst also contributing more generally to physical and mental wellbeing.
- ***Ensuring that children and young people achieve and make a positive contribution*** – The Warwick Commission on the Future of Cultural Value (2015) noted that “the extraordinary cultural and creative talents that we share contribute to the well-being of our society, our economic success, our national identity and to the UK's global influence.” The Commission noted that not enough was being done to realise the creative potential of individuals, despite the workforce in this sector growing over four-times faster than the UK's workforce as a whole. Through its volunteer and workforce capacity, the Trust has an established role in generating and supporting opportunities within the local cultural sector and economy.
- ***Developing a more equal city with cohesive communities and neighbourhoods and supporting active communities and empowered citizens*** – Coventry's diverse population is acknowledged as one of Coventry's cultural strengths. Through arts and cultural activity, the heritage, cultures, abilities and participation of all the city's diverse communities can encouraged in the cultural life of the city. The Trust has a key role to play in connecting to a broad and diverse audience and participant base in the city.
- ***Raising the profile of Coventry through promoting Coventry as a visitor destination and centre*** - Goal 5 (Economic growth) of the Coventry Cultural Strategy identifies Coventry as a culturally vibrant, attractive and prosperous city and sets the ambition that as a cultural city we work to enrich the lives and environment for all residents. The strategy aims to address the need of the city to improve the way it promotes itself as a major tourist destination for the West Midlands and as a result, through a better articulated tourism offer, successfully attract more visitors increase

spend and secure and sustain new businesses and investment. As a large cultural organisation in the city and the managers of key cultural assets, the Trust has a central role to play in the city achieving this goal.

6.2 How is risk being managed?

Council Officers will monitor the Trust to ensure that it is delivering against both its regular annual Key Performance Indicators and also implementing and investigating the various initiatives described in this report. Relevant Cabinet Members will be kept informed of progress.

6.3 What is the impact on the organisation?

The Council is a founding partner in Coventry's bid to be UK City of Culture 2021. The Trust plays a central role in the cultural life of the city through the management of key cultural assets and buildings. .

6.4 Equalities / EIA

An Equality and Consultation Analysis has been undertaken in relation to the Coventry Cultural Strategy 2017-27. As the proposal is to support and facilitate the sustainability of the Trust's current activities and reach, no negative impact on protected groups or concerning the three aims of general duty is anticipated.

6.5 Implications for (or impact on) the environment

This proposal is not expected to have any environmental impact.

6.6 Implications for partner organisations?

The Coventry Cultural Strategy 2017- 2027 is a document developed through consultation with a range of stakeholders and proposes a partnership approach to delivering the strategy.

Culture Coventry is a large cultural agency in the city, managing key assets. The Trust is a Major Partner Museum receiving regular funding from Arts Council England and is the lead agency for the Cultural Destinations funded programme for the city. The securing of a sustainable business plan for the Trust will, in the medium to longer term, make it less vulnerable to fluctuations in its business and less reliant on public funding. It will further have a positive impact for national and local partner organisations as they plan for future collaborations, exhibitions and performances across the range of work of the Trust.

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