

Slough Borough Council

Report To:	Cabinet Committee
Date:	12 September 2024
Subject:	James Elliman Homes Limited (JEH)– Update on governance and risks
Lead Member:	Councillor Wal Chahal Deputy Leader – Financial Oversight, Council Assets, Procurement and Revenues & Benefits
Chief Officer	Pat Hayes – Executive Director (Regeneration, Housing & Environment) Annabel Scholes - Executive Director Finance & Commercial
Contact Officer:	Vicki Palazon – Finance Consultant (FIP and Companies)
Ward(s):	All
Key Decision:	NO
Exempt:	NO
Decision Subject To Call In:	NO, noting report only
Appendices:	None

1. Summary and Recommendations

1.1. This report provides an update on the current position of James Elliman Homes Limited (“JEH”)

Recommendations:

1.2. Cabinet is recommended to:

- 1.2.1. Note the audited Statement of Accounts for 2022/23 were filed on 14 August 2024 (due 31 March 2024);
- 1.2.2. To note the issue of two special resolutions giving direction to the JEH board;
- 1.2.3. To note the planned next steps to improve governance of JEH, including management of risks;
- 1.2.4. To note the next steps to undertake a detailed options appraisal to consider the role and case for continuing with JEH.

Reasoning:

- 1.3. JEH is a company limited by shares wholly owned by the Council. The Council has provided a loan to allow JEH to purchase residential properties for the purpose of renting. JEH's sole activity is that of a housing provider. It is not a registered provider and therefore not a social housing landlord. JEH owns a stock of housing, providing required housing for local residents and is potentially a significant asset for the Borough.
- 1.4. The Council as Shareholder needs to consider its future strategy in the context of both the Council's finances and the broader homelessness pressures on Slough and therefore the options for the company that best meets the Council's strategic objectives and minimises financial risk exposure held within the company.
- 1.5. The company employs no staff directly and utilises the services of the Council through a Service Level Agreement to provide operational resource and back-office support including finance. The company at the time of writing does not have a fully functioning board and recognises the need to review its company secretary and financial support. This has contributed to the company struggling to comply with regulatory requirements to file audited accounts within the prescribed timescales for the two previous years, leading to Companies House taking action to compulsory strike off JEH on two occasions and issue penalties. Strike off action was averted following intervention by the Council to support the company.
- 1.6. Board directors have changed on multiple occasions, but there have been no executive directors and limited independent non-executive directors leading to a lack of capacity and expertise at board level. There is no clear policy to ensure conflict of interest does not arise.
- 1.7. The Council's housing management service has been providing all housing management services to JEH as JEH has no paid employees. The board has been unable to properly contract manage this arrangement to ensure that regulatory requirements are met, properties are maintained to a decent standard and rent arrears and voids are managed. These are key risks which the board need to manage and these are directly related to its ongoing financial viability.

Commissioner Review:

"Commissioners note the content of this report, special resolutions giving directions to JEH Board and expressly the associated financial and governance challenges for the Company and the Council.

Under the statutory directions the Council needs to consider the case for continuing with each subsidiary company of the Authority (except Slough Children First) and whether it has the organisational capacity to maintain adequate oversight. It is critical that whilst a resolution and clear plan is awaited, the shareholder representative needs to provide the Committee with the assurance around the approach being taken to the company's property portfolio or early warnings of alterations to the strategic direction. This should include the financial implication, highlight issues and opportunities around Company/Council governance, conflict of interest, and that the necessary steps are being taken to ensure that risks are managed effectively, and that public funding is used efficiently."

2. Report

Introduction

- 2.1. JEH was set up in 2017 with the primary objective of improving the supply of affordable housing for key workers and those within the lower bands of the Council's waiting lists who are unlikely to receive a Council property; as well as temporary accommodation for homeless families. .
- 2.2. The decision to establish JEH was informed by a business plan, prepared by Savills in November 2016, and agreed by Cabinet in December 2016. The business plan assumed that JEH would acquire properties over a five-year period and that properties would be rented at a mix of market rents (60% of properties) and Local Housing Allowance ("LHA") rent (40% of properties). A revised business plan is due to be received by the council in October for onward approval by members.

Current Situation

- 2.3. Despite the original plan for the focus of JEH to be on key worker and Band C clients in its first years of operation at least 121 families in temporary accommodation (TA) were placed into JEH properties. This has meant that at present about 80% of properties are being rented at LHA level or below so bringing in significantly less income than envisaged in the original plan.
- 2.4. All the properties are managed by the Council under a Service Level Agreement (SLA) with all tenancy management, property maintenance and general management undertaken by the Council. The charges levied should have covered the cost of staff time etc, but it appears charging was historically haphazard, and no detailed accounts were kept for the company. The JEH property portfolio includes 168 individual properties and 46 leased to the Council and used for Temporary Accommodation. Of the 168 circa 130 are currently housing tenants placed by SBC to discharge homelessness duty.
- 2.5. The freehold assets were valued as of 31 March 2022 at £50m (assuming vacant possession) and as of 31 March 2023 at £55m. All properties were acquired on the open market, not built, by SBC/JEH, and financed by the Council. During 2021/22, JEH's housing acquisition programme was stopped, and no further purchases have been made after this date.
- 2.6. The JEH stock is a mixture of second-hand street properties and some new build flats. Many of the homes were or are in poor condition and have required investment to ensure compliance with fire safety and other private sector housing standards. Much of this work has been carried out in 2023/24 following the reestablishment of a Housing Department and will continue in 2024/25.
- 2.7. Once a new business plan has been developed, further information will be shared in relation to the investment in properties to improve the condition.
- 2.8. Historically management of the properties has been poor with tenants being allowed to build up very large levels of rent arrears and most licences not being renewed or cancelled. Originally all tenants were on ASTs most of which have become rolling periodic tenancies.
- 2.9. Most tenants now therefore enjoy a level of security and would have to be evicted legally which may prove difficult if no fault eviction is outlawed.

3. Governance requirements

3.1. In 2021 Grant Thornton, the Council's external auditors, made several s.24 statutory recommendations. These were reported to Audit and Corporate Governance Committee in 2021 and updates were provided in Finance Action Plan reports to Cabinet. However there has been no stand alone reporting on JEH, an extract of the original recommendations and management response is below:

Area	Recommendation	Management Response/ Responsible Officer/ Due Date
Financial governance. Monitoring and controls relating to Group entities	<p>The Council should review and implement effective financial governance and monitoring arrangements for its group relationships to mitigate exposure to additional financial risk.</p> <ul style="list-style-type: none">As a commercial entity subject to separate legal, tax and accounting considerations, there should be clear separation financial transactions of Slough Council and James Elliman Homes, in a separate financial ledger, with clear and distinct financial controls and monitoring in place for both the Council and the company.The Council should review its overall approach to using council officers on the boards of its group companies and other similar organisations. This should be informed by a full understanding of the role of and legal requirements for company board members.When allocating roles on Council-owned organisations to individual officers, the Council should ensure that the scope for conflicts of interest is minimised, with a clear divide between those in such roles and those responsible for holding them to account or overseeing them.The Council should ensure it is actively and routinely monitoring the financial performance of its group entities to consider and protect any unintended financial exposure on the Council's financial position	<p>The Council has begun reviews of its management of third party organisations and will be implementing a series of changes which will include among other matters appointing appropriate Senior Responsible Officers to ensure that companies meet their objectives, put in place new arrangements for holding companies to account, reviewing how the companies meet the Council's objectives, a review of the work undertaken by the companies, developing a clear approach to testing value for money etc. This will include a clear separation of all financial transactions, a review of Council officers on all boards, a review of all financial performance information and actions for all boards and identification of any risks the Council is facing.</p> <p>The responsible officer for this work is the S151 officer.</p> <p>The work will be completed during 2021-22.</p>

3.2. The Government's commissioned governance review by Jim Taylor in 2021 highlighted concerns about company governance leading to a specific direction from the Secretary of State as follows:

3.3. Following the review by the Authority of their companies within six months consider the roles and case for continuing with each subsidiary company of the Authority (except Slough Children First). For those companies that it is agreed to continue, make sure that the Directors appointed by the Authority are appropriately skilled in either technical or company governance matters to make sure each Board functions effectively under the terms of an explicit shareholder agreement and a nominated shareholder representative. For those companies which it is determined not to continue with in this form, to establish a plan to internalise, close or sell as appropriate.

3.4. In 2022 the Council commissioned a review of JEH by Local Partnerships, an entity jointly owned by HM Treasury, the Local Government Association and the Welsh Government. This report was not formally accepted by the council although the issues raised will feed into the refresh of the options and development of the business plan.

Next Steps

3.5. JEH has clearly provided a valuable route by which the Council could discharge its duty to homeless applicants and a source of good value temporary accommodation. These clients having been removed from the housing register.

3.6. Having a housing company able to acquire assets outside of the Council could, if properly managed, be a useful resource in reducing Homelessness costs particularly

in the light of policy changes by the Government. However, there has been insufficient oversight and governance of JEH by the Council, roles and responsibilities not defined and no properly functioning board running JEH.

3.7. This immediately crystallised when Companies House issued a notice that JEH would be struck off due to a failure to file audited accounts for 2022/23. This is the second year in which JEH has failed to file its accounts with the statutory framework and JEH has had to seek two extensions this year.

3.8. To avoid JEH being struck off, the Executive Director of Regeneration, Housing and Environment as the Council's shareholder representative, having consulted with statutory governance officers, taken legal advice and consulted with key cabinet members, issued a letter of support and special resolutions to enable the company to continue to operate for the next 12 months, at the same time issuing directions to the board to improve governance. Even with this action, JEH's auditors have made a statement of material uncertainty in relation to the going concern basis for accounting.

3.9. Page 9 of the [filed company accounts](#) quotes the following auditor's statement:

"In auditing the financial statements, we have concluded that the director's use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

However, we draw your attention to Note 1.2 of the financial statements, which indicates that the company incurred a net loss of £1,010,517 (2022: £1,448,282) and net assets of £1,615,890 (2022: net liabilities £2,481,408), which includes a net property revaluation of £5,107,815 (2022: £nil).

As stated in Note 1.2. Slough Borough Council, the shareholders are supporting the company in developing a business plan for the medium term to enable the company to return to profitability. These events or conditions, along with other matters set forth in Note 1.2, indicate that a material uncertainty exists that may cast significant doubt on the company's ability to continue as a going concern. Our opinion is not modified in respect of this matter."

3.10. The above action has dealt with the immediate issue, however the board will need to undertake further work to improve governance and have been directed to do the following:

- (1) Submit a draft business plan for the accounting year 2024/25, with a view to the Council's Cabinet approval to this being sought by the end of November 2024 or a later date as agreed by the Council. The draft should be submitted by 18 October 2024 and should set out options for returning JEH to profitability, alongside risks and mitigations.
- (2) Undertake a skills audit of the board and identify any gaps in skills and knowledge, to allow the Council to consider making additional appointments to the Board. Such a skills audit should be submitted to the Council by 30 September 2024;
- (3) Submit evidence of a review of the services provided by the Council under the service level agreement and identify any risks or issues by 31 October 2024;
- (4) Submit minutes of JEH board meetings held in the last 6 months, together with management accounts by 30 September 2024;

- (5) Submit an up-to-date risk register with mitigating actions by 30 September 2024;
- (6) Submit evidence that conflicts of interest are being appropriately managed, including details of any conflict of interest protocol and declarations of interests by 30 September 2024;
- (7) Submit details of any further support required to run JEH effectively, including details of cost of such support if this is required to be externally sourced by 30 September 2024;
- (8) Submit details of all governance documentation and evidence of approval by the Board and by the Council as sole shareholder and/or service provider by 30 September 2024;

3.11. The Board will only be able to fulfil these directions if it is of a size and skill set to properly run a company of this type and size. Therefore the Council need to take the following steps:

- Recruit and appoint an executive director/chief executive who will be a direct employee of JEH – appointment is a decision of the Chief Executive or officer acting under their delegation, with appropriate commissioner oversight;
- Support JEH to commission specialist finance support, either by way of an independent non-executive director with a background in finance, a finance officer or a commissioned service;
- Review the arrangement for company secretariat support.
- Review the articles of association and other governance documents with a view to Cabinet Committee being asked to approve any amendments;
- Conduct an options appraisal informed by the recommendations made by Local Partnerships and to inform JEH's business plan;
- Consider the role of JEH as part of a wider review of the Council's housing and homelessness prevention strategies;
- Review the use of Homeless Prevention Grant as part of the wider review of housing services;

3.12. At present, it appears that most JEH tenants may have acquired housing rights, and it would not be possible to simply evict them to gain vacant possession. The TA discharge scheme being in effect an adhoc Temp to Perm scheme.

3.13. Given the large number of JEH residents who seem to have been placed there to discharge duty by SBC there is a real danger they will re-present and need to be rehoused if evicted from JEH properties.

3.14. This complicates any potential disposal of the stock and effectively limits the field of potential buyers to social landlords as majority of tenants will be unable to pay significantly more than LHA rent levels.

3.15. At the moment 8 JEH properties are void and being worked on by the Council's contractors and 7 are void and in a state to be relet but are being held pending discussions on what cause of action to take regarding reletting.

Current financial position

4. The profit and loss account for JEH shows the following performance:

£m	2020/21	2021/22	2022/23	2023/24
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	Actual	Actual	Actual	Draft Outturn
Turnover	2.30	2.46	2.55	2.71
Operating costs	(2.43)	(1.07)	(0.41)	(1.48)
Operating profit/(loss)	(0.13)	1.39	2.12	1.22
Depreciation	(1.02)	(1.14)	(1.0)	(1.0)
Interest payable to the Council	(1.47)	(1.56)	(1.55)	(1.55)
Net profit/(loss)	(2.62)	(1.31)	(0.43)	(1.33)

* The 2022/23 accounts have been prepared and are currently being audited at the time of writing this report.

4.1. In 2020/21 the Company reported an operating loss of £0.1m due to significant repair costs on incurred on properties.

4.2. In 2021/22 JEH reported an operating profit and is forecasting a similar level in 2022/23, However this surplus does not take account of interest payable to the Council in relation to the £51.7 million paid to the Company under various loan agreements to buy property. The forecast loss after interest payable in 2022/23 is £0.21m. This may be less than the costs avoided by the Council from using JEH properties for TA and discharge of duty. Historically rent collection from JEH tenants has been poor which has placed additional pressure on the Company's financial performance.

Future Strategy

5. Taking the earlier draft report undertaken by Local Partnerships in March 2022, the current position outlined in this report, the company business plan is due to be received by the council in October 2024 for onward approval. A refresh of options will be undertaken during Autumn.

Implications of the Recommendations

Financial implications

5.1. The financial position shown earlier in this report highlights that the company whilst generally maintains an operating profit, there is a net loss each year after accounting for interest and depreciation. The balance sheet as at 31 March 2023 has cumulative retained losses of £6.9m although equity in the company at the balance sheet date is £1.6m when accounting for the revaluation reserve. For the company to be sustainable in the future and provide a return on investment for the Council, a robust business plan is required that can be evidenced to provide assurance to the Council that the company has financial sustainability and recover cumulative retained losses.

5.2. The Council has provided a loan to the company of £51.7m which is repayable including interest by October 2028. Based on the latest set of accounts, there is sufficient assets to repay the loan and meet all liabilities providing that market value on disposal could be achieved. However, this is only one option on deciding the future strategy for the company and would need a full risk assessment to be completed to limit any financial exposure the Council may find itself subject to.

5.3. The company is also subject to late filing penalties for two successive years of filing statutory accounts late, this will need to be addressed to ensure there is a plan in place to deliver audited approved accounts within the filing deadline going forward.

Legal implications

6. JEH is a company limited by shares. The Council is the sole shareholder. The Council has provided financing to allow JEH to purchase properties. At present there are considerable risks that this financing will not be repaid and that interest charges are also not capable of being paid. JEH is currently loss making. Company directors have various statutory duties, including a duty to promote the success of the company for the benefit of its members as a whole, in this case the Council as sole shareholder. The directors must also exercise independent judgement. This means outside of reserved matters or written resolutions by the shareholder, they cannot be directed by the Council (either at officer or member level) to take certain decisions. The directors also owe a duty to exercise reasonable care, skill and diligence and avoid conflicts of interest. Relying solely on Council officers to act as directors makes it particularly difficult for the board as a whole and individual directors to fulfil their statutory duties.
7. The Council, as shareholder, should hold JEH to account, but it should not seek to take operational decisions on behalf of JEH. Doing this risks the Council (and individual officers and members) acting as shadow directors. Shadow directors are recognised by law as directors because of the influence and control they exercise over a company. Therefore the same legal duties would apply and any disqualifications or restriction orders applicable to directors could also apply to shadow directors. Several activities could lead to a view that an individual or legal entity is a shadow director including approving expenditures, securing loans or borrowings on behalf of the business, participating actively in board meetings and managing the business activities of the company.
8. The Council has commissioned and received a number of reviews and reports setting out improvements it needs to make to improve its company governance. The Council needs to ensure that recommendations have been implemented and keep its systems and processes under review to ensure it meets its best value duty. In addition the Council needs to learn from failures elsewhere. This includes the public interest reports by Grant Thornton in relation to Croydon Council's use of housing and development companies. Recommendations included need for cabinet reports to clearly set out legal powers and how the Council's interests are protected, regular review of financial business cases and financial rationale for investment arrangements, improved record keeping, including ensuring legal documents are properly executed and that any loan covenants are complied with, regular review of governance arrangements for subsidiaries including ensuring there is clarity and reporting back mechanism for nominated representatives and arrangements in place to consider inherent conflicts of interest for executive officers, ensuring clear terms of reference for officer and member bodies that oversee significant projects and capital/revenue expenditure.

Risk management implications

9. This report articulates a number of challenges the company faces in its current operational state and therefore the Council as Shareholder has issued two special resolutions as outlined in this report to address which will also mitigate risk.

10. JEH maintains a detailed risk register which is reviewed by the Board monthly. The Board has also been directed to submit an up to date risk register and the Council needs to ensure its own risks are properly considered and where appropriate, recorded in the Council's corporate risk register.

Environmental implications

11. There are no direct environmental implications because of the recommendations contained in this report.

Equality implications

12. There are no equality implications from this report. Any future business case should consider the impact on existing tenants and whether these tenants are more likely to have specific protected characteristics.

Procurement implications

13. Should the decision be to dispose of the stock, JEH will need to determine how best to select a Registered Provider or other purchaser.

Workforce implications

14. JEH has no directly employed staff. The Council provides staffing resources under an SLA.

Property implications

15. The properties are owned by JEH. Two hostels have been let to the Council under 30 year leases at annual rent of £1.