

**EXPLANATORY MEMORANDUM TO  
THE LOCAL GOVERNMENT (BEST VALUE AUTHORITIES) (POWER TO  
TRADE) (ENGLAND) ORDER 2009**

**2009 No. 2393**

1. This explanatory memorandum has been prepared by Communities and Local Government and is laid before Parliament by Command of Her Majesty.

**2. Purpose of the instrument**

2.1 The Order replaces the Local Government (Best Value Authorities) (Power to Trade) (England) Order 2004 (SI 2004/1705) (“the 2004 Order”) and provides that all best value authorities in England that are English local authorities within the meaning of section 1(2) of the Local Government Act 1999 or fire and rescue authorities (“FRAs”) that are not also local authorities, are authorised to do for a commercial purpose anything which they are authorised to do for the purpose of carrying on any of their ordinary functions other than functions which they are required to carry out.

**3. Matters of special interest to the Joint Committee on Statutory Instruments**

3.1 None

**4. Legislative Context**

4.1 The power to trade is provided under section 95 of the Local Government Act 2003 (“the 2003 Act”). Under section 95 the Secretary of State may, by order, enable best value authorities<sup>1</sup> to do for a commercial purpose anything which they are authorised to do for the purpose of carrying on any of their ordinary functions subject to certain conditions. This is commonly known as the power to trade<sup>2</sup>. Section 95 provides that the power to trade only applies in respect of functions which the authority is not required to provide in relation to the person in question, it must be exercised through a company and it does not apply where another power enables the authority to trade in that respect.

4.2 The first Order made under this power was the 2004 Order, which provided for certain local authorities in England to exercise the power to trade, namely those authorities who were categorised in a sufficiently high category by order under section 99 of the 2003 Act (Comprehensive Performance Assessment (“CPA”))<sup>3</sup>. The 2004 Order was amended by the Local Government (Best Value Authorities) (Power to Trade) (Amendment) (England) Order 2006<sup>4</sup> to address the revised CPA

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<sup>1</sup> For the purposes of section 95 Best Value Authorities in England include local authorities (namely county councils, district councils, London borough councils, the Council of the Isles of Scilly, the Greater London Authority as it exercises its functions through the London Mayor) and fire and rescue authorities and the London Fire and Emergency Planning Authority.

<sup>2</sup> This can be distinguished from charging under section 93 of the 2003 Act which is limited to cost recovery.

<sup>3</sup> Local authorities were then categorised as ‘excellent’, ‘good’ or ‘fair’.

<sup>4</sup> S.I. 2006/3102

framework<sup>5</sup> introduced in 2005 which assessed performance for single and upper tier<sup>6</sup> local authorities according to ‘star’ categories<sup>7</sup>.

4.3 The 2004 Order set out additional conditions, under the power to do so in section 96 of the 2003 Act, on the exercise of the power to trade. These conditions include requiring an authority to recover the costs of any accommodation, services, staff, goods etc that it supplies to a company. An authority is required to prepare and approve a business case before trading.

4.4 The 2004 Order did not apply to FRAs (i.e. those local authorities acting in their capacity as a fire and rescue authority, combined fire and rescue authorities created by a scheme under section 2 of the Fire and Rescue Services Act 2004 (“the 2004 Act”) or a scheme under the Fire Services Act 1947 (“the 1947 Act”), continued by section 4 of the 2004 Act, or metropolitan county fire and civil defence authorities – subsequently renamed metropolitan county fire and rescue authorities or London Fire and Emergency Planning Authority).

4.5 The 2004 Order was amended by the Local Government (Best Value Authorities) (Power to Trade) (England) (Amendment) Order 2004 (“the amending Order”)<sup>8</sup> to enable those FRAs that had interpreted the 1947 Act as giving them a power to trade to continue to be able to do so, through a company. The 1947 Act was repealed by the 2004 Act. The trading power for FRAs provided in the 2004 Order (as amended) was originally limited in duration until 30th September 2007 and was not linked to CPA.

4.6 The 2004 Order was further amended in 2004 to add an additional category for one FRA<sup>9</sup> and in 2007 to reflect the merging of two FRAs into a combined FRA<sup>10</sup>. Following a consultation in 2007 the power was extended until 30th September 2009<sup>11</sup> - see paragraph 7.8 for more information.

## **5. Territorial Extent and Application**

5.1 This instrument applies in relation to England only.

## **6. European Convention on Human Rights**

As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

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<sup>5</sup><http://www.audit-commission.gov.uk/SiteCollectionDocuments/MethodologyAndTools/Guidance/CPATheHarderTest20087Aug08.pdf>

<sup>6</sup> London borough, unitaries, metropolitan district and county councils.

<sup>7</sup> This additionally awarded the freedoms to 4\*, 3\*, 2\*, 1\* rated local authorities.

<sup>8</sup> S.I. 2004/2307

<sup>9</sup> S.I. 2004/2573

<sup>10</sup> S.I. 2007/385

<sup>11</sup> S.I. 2007/2543

## 7. Policy background

### *Local Authorities*

7.1 The Local Authorities (Goods and Services) Act 1970 governs the way in which local authorities are allowed to ‘trade’ but this is only with other public bodies.

7.2 The Local Government White Paper “Strong Local Leadership – Quality Public Services” (2001)<sup>12</sup> announced a new Comprehensive Performance Assessment (CPA) framework to assess local authorities' delivery of national and local priorities. The White Paper promised that the highest performing local authorities would be given greater freedom and flexibilities including a power to trade in any service in which they have a strong performance on delivery.

7.3 Following this, the 2003 Act was passed and contained new powers for best value authorities to trade in function-related activities through a company and also provided for the regulation of these trading powers. The powers were introduced as part of a new package of freedoms and flexibilities following the introduction of CPA. Statutory guidance on the power is given in “General Power for Local Authorities to Trade in Function Related Activities Through a Company”<sup>13</sup>.

7.4 There was a consultation in January 2006, “Local Strategic Partnerships: Shaping their future”,<sup>14</sup> on how to handle the trading powers under CPA 2005. Responses to the consultation from the Local Government Association and a number of respondents supported an extension of the power to all authorities.

7.5 In 2007, the Lyons Inquiry<sup>15</sup> called for the power to trade to be extended to all local authorities.

7.6 The trading powers are currently available to local authorities which are high performers according to CPA. CPA is being replaced by the framework for Comprehensive Area Assessment (CAA), published on 10 February 2009<sup>16</sup>. CAA will provide an assessment of an area, and not of an individual council's performance. It will provide an overall performance rating, so is inappropriate as a transitional vehicle relevant to the continuation of the power to trade.

7.7 Currently 39 local authorities in England do not have access to the trading powers. Analysing the 2007/08 CLG Revenue Outturn data, the revenue spend of the authorities which do not have access to trading powers amounts to just over 1% of the total local authority revenue spend.

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<sup>12</sup> <http://www.communities.gov.uk/documents/localgovernment/pdf/144893.pdf>

<sup>13</sup> <http://www.communities.gov.uk/documents/localgovernment/pdf/133628.pdf>.

<sup>14</sup> <http://www.communities.gov.uk/documents/localgovernment/pdf/143024.pdf>

<sup>15</sup> <http://www.lyonsinquiry.org.uk/>

<sup>16</sup> <http://www.audit-commission.gov.uk/caa/framework.asp>

## *Fire and Rescue Authorities*

7.8 As stated in paragraphs 4.4 and 4.5, the 2004 Order did not originally apply to a local authority when acting in its capacity as a FRA, but was later extended to enable the power to trade to be exercised by certain FRAs. This was not linked to CPA performance. The trading power was available to 30 out of the 46 FRAs and was initially limited in duration until 30th September 2007.

7.9 On the basis and balance of the findings of a consultation carried out in 2007<sup>17</sup>, the temporary trading powers for those FRAs were extended until 30th September 2009. From the 35 responses received to the 2007 consultation 27 (77%) agreed to this option including support from FRAs and some suppliers. This ensured that the *status quo* was maintained, without any detriment to the taxpayer, until trading powers were reviewed in the light of the removal of the CPA.

7.10 If their power to trade ceased, the 30 FRAs in England would be deprived of existing income streams. This could have the effect of increasing the burden on taxpayers.

## *Making of the 2009 Order and Revocation of the 2004 Order*

7.11 In view of the number of amendments to the 2004 Order, it has been decided to make a new Order (“the 2009 Order”) that revokes the 2004 Order and the orders that have amended it. The Secretary of State makes the 2009 Order, under the power in section 95 of the 2003 Act, to authorise all best value local authorities and FRAs in England to trade in function-related activities through a company, subject to the conditions in section 95. The 2009 Order also imposes conditions, under the power in section 96 of the Act, on the exercise of any such trading power by a best value local authority or fire and rescue authority, undertaken through a company.

## **8. Consultation outcome**

8.1 The consultation paper “*Proposed changes to the delivery of Local Authorities’ and Fire & Rescue Authorities’ Freedoms and Flexibilities after the introduction of Comprehensive Area Assessment*”<sup>18</sup> was published on 6th May 2009. Amongst other matters, it sought views on the proposal to extend the trading powers to all English local authorities and FRAs.

8.2 The consultation paper, which included the initial Impact Assessments, was sent to all best value local authorities, FRAs, charities, lobby groups and businesses, including small & medium sized enterprises (SMEs).

8.3 The consultation asked 3 specific questions in relation to trading:

- Question 3: Do you agree that the power to trade should be extended to all local authorities?

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<sup>17</sup> [http://www.opsi.gov.uk/si/si2007/em/uksiem\\_20072543\\_en.pdf](http://www.opsi.gov.uk/si/si2007/em/uksiem_20072543_en.pdf)

<sup>18</sup> <http://www.communities.gov.uk/publications/localgovernment/freedomsflexibilitiescaa>

- Question 5: Should the power to trade be extended to permit all FRAs to trade in all of their services?
- Question 6: If there is no agreement on the above, should the current FRA Trading Order be extended indefinitely?

8.4 37 responses were received to the consultation with contributions from best value local authorities, FRAs, industry (including SMEs) and a charity. Not all respondents answered the specific questions in relation to trading. Where respondents gave general comments, any which were related to trading were also considered.

#### *Local Authorities' Power to Trade (Question 3)*

8.5 21 (57%) respondents supported the recommended option to extend the powers to trade to all local authorities (Question 4). 1 (3%) respondent from industry did not support this and 15 (40%) did not answer this question.

8.6 Reasons for support included:

- that it would enable the generation of income streams;
- absence could stifle innovation and prevent collaboration with partners;
- it should improve competition in the delivery of public services;
- it should encourage greater consistency and help diminish the 'postcode-lottery' of services that currently exists.

8.7 The respondent who did not support this option considered that some local authority companies would have a captive market, that they may use their local authority status to win business and that they can gain a competitive advantage over private providers.

8.8 The majority of responses to the consultation paper supported the extension of the power to trade to all best value local authorities. This approach, so respondents argued, will ensure that local authorities continue to have available the necessary power to improve services for their communities, provide enhanced competition in the public services market, and generate revenue to keep down council tax or invest in public services. With regard to the respondent who did not support the proposal, legal safeguards are in place which should prevent such abuses of the system as are mentioned in paragraph 8.7. The 2009 Order requires an authority to recover the costs of any services provided to the company. In addition, the companies through which local authorities are required to operate when exercising the power to trade are required to comply with competition law and procurement regulations<sup>19</sup>, and are subject to controls relating to state aid.

#### *Fire and Rescue Authorities' Power to Trade (Question 5)*

8.9 21 (57%) respondents supported the recommended option to extend the power to trade to all FRAs (Question 5). 3 (8%) respondents from industry did not support this and 13 (35%) did not answer this question.

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<sup>19</sup> The Public Contracts Regulations 2006 (S.I. 2006/5)

8.10 Reasons for support included:

- it will bring all FRAs into line with the trading powers available to local authorities;
- depriving FRAs of existing income streams only results in a greater burden on tax-payers which would hinder a more modernised service;
- it will stimulate a more entrepreneurial public sector and increase partnership working as well as maintaining maximum flexibility for future developments;
- it will enable FRAs to work with local partners to achieve potential efficiency savings e.g. shared services.

8.11 Reasons for opposition included:

- fundamentally wrong for a public sector emergency service to charge for its non-core activities;
- authorities that have a statutory duty as an enforcing agent should not also be allowed to provide an advice service;
- public perception of the Fire and Rescue Service gives them a brand advantage;
- unfair competition – taking work away from SMEs.

8.12 If there was no agreement on extending all powers to FRAs then Question 6 considered whether the existing limited FRA trading Order could be extended indefinitely instead. 13 (35%) respondents supported this, 6 (16%) respondents did not support this and 18 (49%) did not answer this question.

8.13 Where this was supported it was considered essential so that FRAs did not lose their income streams now or in the future. Some of these respondents considered that if this option went ahead that it should be time limited.

8.14 Respondents who did not support this option either considered that FRAs should have no access to trading powers or that they should have access to all trading powers (as per Q5).

### *Conclusion*

8.15 The majority of responses to the consultation paper supported the extension of the power to trade to all FRAs in England. This approach ensures that FRAs have the same access to trading powers as local authorities. FRAs would be able to generate revenue which they could either invest in fire safety programmes or use to keep down council tax. With regard to the respondents who did not support the proposal, FRAs are constrained in as much as any service provided on a commercial basis must be delivered through a company. It is up to FRAs to manage any potential conflict arising from giving advice and acting as an enforcing agent.

## **9. Guidance**

9.1 Statutory Guidance on the general power for local authorities to trade was published in July 2004<sup>20</sup> and an update addendum was published in 2007<sup>21</sup>. Guidance on the power for FRAs to trade was published in January 2007<sup>22</sup>. Consideration is being given to further updating the statutory guidance to reflect the changes brought about by the 2009 Order.

## **10. Impact**

10.1 The proposal may impact on the business, charity and voluntary sector as it is enabling authorities to engage in the public service markets. However, whilst the powers allow local authorities and FRAs to engage in activities which are also undertaken by the private sector, it should not be assumed that they will necessarily be displacing business from the private sector - trading activity could also create sub-contracting and partnering opportunities for small businesses with local authorities and FRAs. The trading powers may also be used to improve competition or to fill a gap in the market in the provision of services to the public.

10.2 The impact on the public sector is none.

10.3 Two Impact Assessments are attached to this memorandum.

## **11. Regulating small business**

11.1 The legislation does not apply to small business.

## **12. Monitoring & review**

12.1 The Department for Communities and Local Government will consider how the impact of the revised policy can be monitored and evaluated through its programme of local government research. Information on the costs and benefits of FRA trading will be assessed following the set up and running of any companies.

## **13. Contact**

Andrew Cornelius at the Department for Communities and Local Government - Tel: 020 7944 8766 or email: [andrew.cornelius@communities.gsi.gov.uk](mailto:andrew.cornelius@communities.gsi.gov.uk) can answer any queries regarding the instrument as it applies to local authorities.

Anna Wadsworth at the Department for Communities and Local Government - Tel: 020 7944 5672 or email: [anna.wadsworth@communities.gsi.gov.uk](mailto:anna.wadsworth@communities.gsi.gov.uk) can answer any queries regarding the instrument as it applies to fire and rescue authorities.

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<sup>20</sup> <http://www.communities.gov.uk/documents/localgovernment/pdf/133628.pdf>

<sup>21</sup> <http://www.communities.gov.uk/documents/localgovernment/pdf/323153.pdf>

<sup>22</sup> <http://www.communities.gov.uk/documents/fire/pdf/153140.pdf>

## Summary: Intervention & Options

<b>Department /Agency:</b> <b>Communities and Local Government</b>	<b>Title:</b> <b>Impact Assessment of local authorities' power to trade following the end of categorisation under CPA (Annex F)</b>	
<b>Stage:</b> Final	<b>Version:</b> 2	<b>Date:</b> 25 August 2009
<b>Related Publications:</b> Explanatory Memorandum to The Local Government (Best Value Authorities) (Power to Trade) (Amendment) (England) 2006 (S.I. No. 3102/2006)		

**Available to view or download at:**

[http://www.opsi.gov.uk/si/em2006/uksiem\\_20063102\\_en.pdf](http://www.opsi.gov.uk/si/em2006/uksiem_20063102_en.pdf)

**Contact for enquiries:** Andrew Cornelius

**Telephone:** 020 7944 8766

**What is the problem under consideration? Why is government intervention necessary?**

The power to trade is currently related to performance and is available to local authorities categorised under Comprehensive Performance Assessment (CPA) as "excellent", "good", "fair", "4 star", "3 star", "2 star" and "1 star". Assessment under CPA comes to an end in March 2009. Without action, whilst local authorities currently categorised as being eligible to trade will retain the power, the remaining authorities will not have access to the powers. There will also be uncertainty about how the Government intends to provide long-term access to the power to trade.

**What are the policy objectives and the intended effects?**

The intention is to provide local authorities with continued access to the trading powers. This will continue to enable local authorities to act to increase diversity and choice in public service delivery and to trade with the public and private sector where there is a strong business case to do so. Under the preferred option the power would be extended to just 39 authorities, evidence suggests that only a small percentage of these would make any significant use of the power. The combined revenue spending power of the additional 39 local authorities is 1% of the local authority total.

**What policy options have been considered? Please justify any preferred option.**

1. Do nothing; 2. Trading powers to better performers only; 3. Preserve existing authorities' power to trade; 4. Trading powers to all authorities (Preferred Option).

The preferred option provides opportunity for council's to generate revenue to invest in services, reduce council tax and seek collaborative opportunities with the private and voluntary sectors. The revenue spending power of the additional 39 authorities represents just over 1% of local authority market activity and prevents authorities already trading from losing access to revenue streams. This is supported by LGA & Lyons.

**When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?** The Department will consider how the impact of the policy can be monitored and evaluated through its research programme. Research is only likely to be carried out in 2010/11 at the earliest.



**Ministerial Sign-off** For final proposal/implementation stage Impact Assessments:

***I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.***

Signed by the responsible Minister:

Ian Austin

..... Date: 2<sup>nd</sup> September 2009

## Summary: Analysis & Evidence

**Policy Option: 2**

**Description: Trading powers to better performers only**

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups'	
	<b>One-off (Transition)</b>	<b>Yrs</b>		
	£	0		
	<b>Average Annual Cost</b> (excluding one-off)			
	£		<b>Total Cost (PV)</b>	£
Other <b>key non-monetised costs</b> by 'main affected groups' Authorities trading may distract resources from core services, although a strong business case should prevent this; some authorities may lose access to the trading powers where they previously had access to them leading to loss of revenue and decreased innovation and				

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups'	
	<b>One-off</b>	<b>Yrs</b>		
	£ 0	0		
	<b>Average Annual Benefit</b>			
	£		<b>Total Benefit (PV)</b>	£
Other <b>key non-monetised benefits</b> by 'main affected groups' Improvement in quality of services provided by some councils through enhanced competition; opportunities for councils to make profit from managing their extended freedoms efficiently; better usage of resources for tax payers.				

**Key Assumptions/Sensitivities/Risks** There are inherent risks in undertaking trading activities; however, there are safeguards in place to ensure that trading is undertaken with an appropriate level of consideration by an authority. Local authorities may only trade in function related activities and must prepare and approve a business case before trading.

Price Base Year	Time Period Years	<b>Net Benefit Range (NPV)</b> £	<b>NET BENEFIT (NPV Best estimate)</b> £	
What is the geographic coverage of the policy/option?		England		
On what date will the policy be implemented?		Autumn 2009		
Which organisation(s) will enforce the policy?		n/a		
What is the total annual cost of enforcement for these		£		
Does enforcement comply with Hampton principles?		Yes		
Will implementation go beyond minimum EU requirements?		No		
What is the value of the proposed offsetting measure per year?		£		
What is the value of changes in greenhouse gas emissions?		£		
Will the proposal have a significant impact on competition?		No		
Annual cost (£-£) per organisation (excluding one-off)		Micro	Small	Medium    Large

Are any of these organisations exempt?	Yes/No	Yes/No	N/A	N/A
<b>Impact on Admin Burdens Baseline</b> (2005 Prices)			(Increase - Decrease)	
Increase	£	Decrease	£	<b>Net</b> £

Key: Annual costs and benefits: (Net) Present Value

## Summary: Analysis & Evidence

**Policy Option:**  
3

**Description:** Preserve existing authorities power to trade

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' The proposal does not place any additional costs on local authorities
	<b>One-off</b> (Transition)	<b>Yrs</b>	
	£ 0	0	
	<b>Average Annual Cost</b> (excluding one-off)		
	£ 0		<b>Total Cost (PV)</b> <b>£ 0</b>
Other <b>key non-monetised costs</b> by 'main affected groups' Improving authorities without access to the trading powers would not gain access to the trading powers resulting in less scope for collaborative working with the private and voluntary sectors and authorities would not be able to realise the financial benefits of trading for a profit.			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups'
	<b>One-off</b>	<b>Yrs</b>	
	£ 0	0	
	<b>Average Annual Benefit</b>		
	£ 0		<b>Total Benefit (PV)</b> <b>£ 0</b>
Other <b>key non-monetised benefits</b> by 'main affected groups' Improvement in quality of services provided by some councils through enhanced competition; opportunities for some councils to make profit from managing their extended freedoms efficiently and better usage of resources for taxpayers. Less authorities would be subject to the			

**Key Assumptions/Sensitivities/Risks** There are inherent risks in undertaking trading activities; however, there are safeguards in place to ensure that trading is undertaken with an appropriate level of consideration by an authority. Local authorities may only trade in function related activities and must prepare and approve a business case before trading.

Price Base Year	Time Period Years	<b>Net Benefit Range (NPV)</b> £	<b>NET BENEFIT (NPV Best estimate)</b> £	
What is the geographic coverage of the policy/option?		England		
On what date will the policy be implemented?		Autumn 2009		
Which organisation(s) will enforce the policy?		n/a		
What is the total annual cost of enforcement for these		£ 0		
Does enforcement comply with Hampton principles?		Yes		
Will implementation go beyond minimum EU requirements?		No		
What is the value of the proposed offsetting measure per year?		£ 0		
What is the value of changes in greenhouse gas emissions?		£ 0		
Will the proposal have a significant impact on competition?		No		
Annual cost (£-£) per organisation (excluding one-off)		Micro	Small	Medium Large

Are any of these organisations exempt?	Yes/No	Yes/No	N/A	N/A
<b>Impact on Admin Burdens Baseline</b> (2005 Prices)			(Increase - Decrease)	
Increase	£	Decrease	£	<b>Net</b> £

Key: **Annual costs and benefits: Constant Price**

## Summary: Analysis & Evaluation

Policy Option: 4

Description: Trading powers to all authorities

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' There would be some costs in setting up a trading company and running costs for the operation, depending on the service being provided. The required business case should demonstrate how a commercial return is to be achieved and start-up costs should be scoped in that consideration.
	<b>One-off</b> (Transition)	<b>Yrs</b>	
	£ 50k	1	
	<b>Average Annual Cost</b> (excluding one-off)		
	£ 8m		<b>Total Cost (PV)</b> £ 67m
Other <b>key non-monetised costs</b> by 'main affected groups' Authorities trading may distract resources from core services, although a strong business case should prevent this, larger number of authorities subject to the risks inherent in undertaking trading activities (such as financial loss). There is also the possibility that private businesses operating in the same market may be affected by the competition offered by local authority trading companies			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups'  The benefits for a local authority company is the turnover as part of the business.
	<b>One-off</b>	<b>Yrs</b>	
	£ 0		
	<b>Average Annual Benefit</b>		
	£ 8.6m		<b>Total Benefit (PV)</b> £ 72m
Other <b>key non-monetised benefits</b> by 'main affected groups' Improvement in quality of services through enhanced competition, opportunity to generate revenue, and to seek collaborative and partnering opportunities with SMEs and the wider private and voluntary sectors. Revenue generated would enable authorities either to invest in public services or keep down Council Tax.			

**Key Assumptions/Sensitivities/Risks** There are inherent risks in undertaking trading activities; however, there are safeguards in place to ensure that trading is undertaken with an appropriate level of consideration by an authority. Local authorities may only trade in function related activities and must prepare and approve a business case before

Price Base Year 2008	Time Period Years 10	<b>Net Benefit Range (NPV)</b> £ 0 - 10m	<b>NET BENEFIT (NPV Best estimate)</b> £ 5m
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What is the geographic coverage of the policy/option?	England
On what date will the policy be implemented?	Autumn 2009
Which organisation(s) will enforce the policy?	n/a
What is the total annual cost of enforcement for these	£
Does enforcement comply with Hampton principles?	Yes
Will implementation go beyond minimum EU requirements?	N/A
What is the value of the proposed offsetting measure per year?	£
What is the value of changes in greenhouse gas emissions?	£

Will the proposal have a significant impact on competition?			No	
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	Yes/No	Yes/No	N/A	N/A
<b>Impact on Admin Burdens Baseline</b> (2005 Prices)			(Increase - Decrease)	
Increase    £		Decrease    £	<b>Net</b>	<b>£</b>

Key:

Annual costs and benefits: Constant Prices

(Net) Present Value

[Use this space (with a recommended maximum of 30 pages) to set out the evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Ensure that the information is organised in such a way as to explain clearly the summary information on the preceding pages of this form.]

### Trading Powers

1. The *Local Authorities (Goods and Services) Act 1970*<sup>23</sup> governs the way in which local authorities are allowed to 'trade' with other public bodies. It authorises local authorities to enter into agreements with public bodies for the provision of goods, materials, and administrative, professional and technical services, for the use of vehicles, plant and apparatus, and for the carrying out of maintenance. There is also a power for the Secretary of State to designate by order that any person(s) exercising functions of a public nature shall be a public body for the purposes of the Act.
2. The Local Government White Paper *Strong Local Leadership – Quality Public Services* (2001)<sup>24</sup> announced a new Comprehensive Performance Assessment (CPA) framework to assess local authorities' delivery of national and local priorities. The White Paper promised that the highest performing local authorities would be given greater freedom and flexibilities.
3. Section 95 of the *Local Government Act 2003* ("the 2003 Act")<sup>25</sup> authorises the Secretary of State, by order, to permit best value authorities to do for a commercial purpose anything which they are authorised to do for the purpose of carrying on any of their ordinary functions. This is commonly known as the power to trade. The power to trade is only able to be exercised through a local authority company (within the meaning of Part 5 of the *Local Government and Housing Act 1989*<sup>26</sup>). Trading under the power needs to be directed towards the achievement of Best Value in the related function. This means that local authorities cannot set up trading arms unrelated to core services or functions.
4. The power may not be used to authorise best value authorities to trade in a statutory service which they are already obliged to provide with a person to whom they are already obliged to provide it, or to use the new powers where there are existing trading powers.

### Trading Order

5. The *Local Government (Best Value Authorities) (Power to Trade)(England) Order 2004* ("the 2004 Order")<sup>27</sup> provides the power to trade to those local authorities who have been categorised, by order under section 99 of the 2003 Act, as having attained a certain level of performance namely those authorities who have been categorised by order under as "excellent", "good" or "fair".

### CPA Framework

6. The Audit Commission independently carry out assessments, which placed councils into one of five categories - excellent, good, fair, weak and poor. The Government's stated policy was that those authorities categorised as excellent, good and fair would have access to greater powers to trade. In December 2005 the Audit Commission published a revised CPA framework, *The Harder Test* ("CPA 2005")<sup>28</sup>, for England's 150 single tier and county councils. Under CPA *The Harder Test* framework,

<sup>23</sup> [http://www.opsi.gov.uk/acts/acts1970/pdf/ukpga\\_19700039\\_en.pdf](http://www.opsi.gov.uk/acts/acts1970/pdf/ukpga_19700039_en.pdf)

<sup>24</sup> <http://www.communities.gov.uk/documents/localgovernment/pdf/143810.pdf>

<sup>25</sup> [http://www.opsi.gov.uk/acts/acts2003/ukpga\\_20030026\\_en\\_1](http://www.opsi.gov.uk/acts/acts2003/ukpga_20030026_en_1)

<sup>26</sup> [http://www.opsi.gov.uk/acts/acts1989/Ukpga\\_19890042\\_en\\_1](http://www.opsi.gov.uk/acts/acts1989/Ukpga_19890042_en_1)

<sup>27</sup> <http://www.opsi.gov.uk/si/si2004/20041705.html>

<sup>28</sup> [http://www.audit-commission.gov.uk/localgov/audit/cpa/CPA\\_STCC/cpaarchive/Pages/cpaframework2005.aspx](http://www.audit-commission.gov.uk/localgov/audit/cpa/CPA_STCC/cpaarchive/Pages/cpaframework2005.aspx)



councils receive an overall performance category ranging from 0 to 4 stars, with 4 stars being the highest. District CPA has not been altered to incorporate *The Harder Test* framework and District councils (which are not single tier councils) are not brought within that that framework.

7. In January 2006, the then *Office of the Deputy Prime Minister* (ODPM) launched a consultation exercise seeking views on the handling of freedoms and flexibilities under CPA 2005, *Freedoms and Flexibilities*<sup>29</sup>. The Government's preferred option was to extend freedoms and flexibilities downwards across star categories. This would mean that the trading powers, currently available to excellent, good and fair authorities, would be given to 4 stars, 3 stars, 2 stars and 1 star authorities. Changes were not proposed for the freedoms and flexibilities of those District Councils (which are not single tier councils), and they retain the current categorisation labels of excellent to poor.

8. Following consultation, the *Local Government (Best Value Authorities) (Power to Trade) (Amendment) (England) Order 2006* ("the 2006 Order")<sup>30</sup> amended the 2004 Order by applying the power to trade to those local authorities categorised in an order under section 99 of the 2003 Act as "4 stars", "3 stars", "2 stars" and "1 star" as well as to those authorities categorised as "excellent", "good" or "fair".

### **Current Proposal**

9. It was proposed in a *Freedom & Flexibilities* Consultation Paper<sup>31</sup> to extend the power to trade commercially to all local authorities. The responses to the consultation on how to handle the trading powers under CPA 2005 received support from the LGA and a number of respondents to extend the power further to all authorities. The *Lyons Inquiry into Local Government*<sup>32</sup> also recommended that the power should be extended to all local authorities.

10. The terms of a new Trading Order will continue to place safeguards on the use of the power, for example, by requiring an authority to prepare and approve a business case before trading. This requirement ensures that authorities manage risks effectively. However, local authorities will need to continue to base firmly any proposed trading activity on the need to secure value for money for the taxpayer and to have regard to relevant good practice.

11. The recommended option provides an incentive for improvement. The benefits of the preferred option include improvement in quality of services provided by councils through enhanced competition. There would be opportunity for more councils to make profit from having access to trading powers and more councils able to seek collaborative opportunities with other sectors from having access to trading powers.

### **Previous RIAs**

12. Full Regulatory Impact Assessments were produced for the Local Government Bill 2003 and for the *Local Government (Power to Trade) (England) Order 2004* and the *Local Government (Best Value Authorities) (Power to Trade) (Amendment) (England) Order 2006*.

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<sup>29</sup> <http://www.communities.gov.uk/documents/localgovernment/pdf/143663.pdf>

<sup>30</sup> <http://www.opsi.gov.uk/si/si2006/20063102.htm>

<sup>31</sup> <http://www.communities.gov.uk/documents/localgovernment/pdf/1222822.pdf>

<sup>32</sup> <http://www.lyonsinquiry.org.uk/>

## Consultation

13. On 6 May 2009, the Department published the consultation document, Proposed changes to the delivery of Local Authorities' and Fire & Rescue Authorities' Freedoms and Flexibilities after the introduction of Comprehensive Area Assessment<sup>33</sup>. Amongst other things, the consultation asked:

- Question 3: Do you agree that the power to trade should be extended to all local authorities?

14. 37 responses were received to the consultation with contributions from local authorities, Fire & Rescue Authorities, private sector (including SMEs) and a charity. Not all respondents answered the specific questions in relation to local authority trading, however where there were general comments relating to local authority trading, these were also considered.

15. 21 respondents (57%) supported the recommended option to extend the powers to trade to all local authorities, 1 respondent (3%) did not support this and 15 respondents (40%) did not answer this question.

16. Reasons for support include:

- that it would enable the generation of income streams
- absence could stifle innovation and prevent collaboration with partners
- it should improve competition in the delivery of public services
- it should encourage greater consistency and help diminish the 'postcode-lottery' of services that currently exists

17. The respondent who did not support the proposal considered that some local authority companies would have a captive market, that they use their local authority status to win business, and that they can leverage a competitive advantage over private providers.

18. The majority of responses to the consultation paper supported the extension of the power to trade to all local authorities. This approach will ensure that local authorities continue to have available the necessary power to improve services for their communities, provide enhanced competition in the public services market, and to generate revenue to keep down council tax or invest in public services. With regard to the respondent who did not support the proposal, there are appropriate legal safeguards in place to protect from such abuses of the system. The 2004 Order requires an authority to recover the costs of any services provided to the company. In addition, local authorities are required to comply with competition law, state aid principles, as well as the procurement regulations which enforce rules on transparency, free movement of goods and non discrimination.

## Local Authority Coverage

19. The Government's approach to providing local authorities with access to the trading powers has been through its Freedoms and Flexible programme linked to CPA categorisation. This means that only those higher performing local authorities have had access to the power to trade. Subsequent trading orders have extended access to the trading powers to more CPA categories following CPA *The Harder Test*. Under the most recent categorisation order, the 349 higher performing local authorities have access to the trading powers, with 39 authorities currently restricted in their access to the trading powers. Whilst this means that 10% of local authorities do not have access to the trading powers, this figure is not necessarily representative when you look at the 'economic activity' of the authorities which do not have access to the powers. Using the 2007/08 CLG Revenue Outturn data<sup>34</sup>, the revenue spend of the authorities which do not have access to trading powers amounts to just over 1% of the total local authority revenue spend.

## Sectors and Groups Affected

20. The trading powers are enabling powers. It is expected that local authorities will seek to engage in trading activities only where the authority already has a strong track record of delivery in that service

<sup>33</sup> <http://www.communities.gov.uk/publications/localgovernment/freedomsflexibilitiescaa>

<sup>34</sup> <http://www.communities.gov.uk/publications/corporate/statistics/revenue200708provouturn>

area. The proposal to extend the trading power potentially affects a range of sectors, groups and markets. It is anticipated that the proposal would have a positive competitive effect on the private sector due to local authorities engaging in new activities and stimulating markets and increasing competition. The powers allow local authorities to engage in activities which were also undertaken by the private sector; however, it is not necessary to assume that local authorities will necessarily be displacing business from the private sector. Trading activity could also create sub-contracting and partnering opportunities with local authorities. The trading powers can be expected also to be used to improve competition and contestability or to fill a gap in the market in the provision of services to the public.

## Research on Use of Trading Powers

21. ODPM (now DCLG) commissioned a baseline evaluation of the use, awareness, and emerging impact of freedoms and flexibilities in local government. The Report was published as '*Evaluation of Freedoms and Flexibilities in Local Government: Baseline Study*' (DCLG, September 2006)<sup>35</sup>. In view of the relatively small size of the samples, caution should be used in drawing inferences about English local authorities as a whole. The Report found that:

- between 20% and 30% of respondents reported that their authorities were taking up trading and charging powers.
- 3% of authorities saying they had made significant use of the power.
- 18% of authorities said they had made some use of it
- 56% said they had made no use at all of the power.
- However, this low level of use does not seem to be caused by a low level of awareness of the powers now available.

22. Research by the Local Government Association (LGA) in November 2004, *Loosening the Reins*<sup>36</sup>, found:

- low level of use of the power with only 2% of councils using their new powers to trade,
- a further 18% intending to use the powers.
- 64% of authorities using, or planning to use, the power identified raising revenue as a key objective.

23. Research undertaken by INLOGOV (the Institute of Local Government Studies) for CLG in November 2007, *Local Authority Trading: Research Report*<sup>37</sup>, also found little evidence of authorities using or planning to use their increased power to trade, though upper tier authorities were more likely than districts to indicate a plan for marginal increases in trading activity. The Report found:

- 72% of local authorities surveyed trade, with an annual average income of £3m (this figure includes trading under other powers)
- 29% of authorities trade in 2003 Act powers
- Overall, 25% of local authorities aim to make surplus.
- Local authorities which did not trade cited the following as the main barriers to trading:
  - cultural barriers
  - non-trading authorities were more likely to perceive European regulations as restricting local authority trading than trading authorities

## Known take up of the powers

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<sup>35</sup> <http://www.communities.gov.uk/publications/localgovernment/evaluationfreedoms2>

<sup>36</sup> <http://www.wlga.gov.uk/download.php?id=144&l=1>

<sup>37</sup> <http://www.communities.gov.uk/publications/localgovernment/tradingresearchreport>

24. Whilst the research undertaken by INLOGOV suggests that 29% of local authorities trade in 2003 Act powers, we have been unable to establish more than 3 or 4 authorities actively trading in the market. Each of those authorities has on average 2 companies commercially trading.

### Services traded in

25. According to the INLOGOV research cited above, the most commonly traded local authority services are:

- grounds maintenance
- building cleaning/maintenance
- highways maintenance
- vehicle maintenance

26. This list should be considered with some caution as the trading research looked at all powers under which local authorities trade and these typically follow the traditional DSO/DLO (Direct Service/Direct Labour Organisation) which local authorities ran in the past. However, it is likely that where a local authority has a successful DSO/DLO, then that may be incorporated as a trading company. The services which we established know local authorities are trading in under the 2003 Act powers, and which form the basis of the cost-benefit analysis above are in the area of:

- Facilities management and small building works
- Temporary staff
- Transport services (in particular those which would otherwise require subsidy such as rural, evening and Sunday services)
- Property Consultancy services
- Waste management and recycling
- School & Venue catering
- Grounds & highways maintenance
- Environmental services

### Costs and benefits of setting up and operating a trading company

27. At the time of preparing the impact assessment, four local authority trading companies were known to the Department. All four were contacted in order to obtain relevant values to be used in estimating the costs and benefits arising from the creation of additional trading businesses. Key questions put to existing trading companies included turnover, gross profit, type of activity and start-up costs. The evidence gained in this exercise was used to inform the assumptions and calculations presented in the text box '**range of scenarios under option 4**' shown later in this document.

### Risk in the Context of Trading

28. Section 3 of the *Local Government Act 1999*<sup>38</sup> places a duty of Best Value on local authorities and other public bodies. This requires them to secure continuous improvement in the way in which they exercise their functions, having regard to a combination of economy, efficiency and effectiveness. Trading under the 2003 Act powers needs to contribute towards Best Value in the related function.

29. The trading power permits local authorities to act in an entrepreneurial manner and engage in commercial activities. There are inherent risks in undertaking such activities especially when taxpayer's money is being used to fund these ventures. However, there are safeguards in place to ensure that trading is undertaken with an appropriate level of consideration by a local authority. The trading power permits local authorities to trade in function related activities only (i.e. authorities need to have the power to engage in an activity before they can trade in it). This should minimise the risk as a local authority should not be engaging in activities in which they do not have any experience or expertise of

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<sup>38</sup> [http://www.opsi.gov.uk/acts/acts1999/ukpga\\_19990027\\_en\\_1](http://www.opsi.gov.uk/acts/acts1999/ukpga_19990027_en_1)

undertaking. A local authority must also prepare and approve, as appropriate within its governance arrangements, a business case before exercising the 2003 Act trading powers. This provides further safeguards for taxpayers' money by ensuring that there is a rationale and full consideration presented through the appropriate local authority executive arrangement before undertaking trading activities. In addition, a local authority has a duty ("the fiduciary duty") to ensure that arrangements must be made to ensure that taxpayer's money is spent appropriately. This duty has generally emerged from case law c/f *Roberts v. Hopwood* [1925] AC 578 and in *Bromley London Borough Council v Greater London Council* [1983] 1 AC 768. The fiduciary duty will apply to a local authority seeking to trade.

## **Options Analysis**

### ***Option 1 - 'Do nothing'***

Whilst the categorisation order remains in force, local authorities which are currently categorised as under that order as eligible to trade will continue to have access to the trading powers.

#### *Risks*

Diversity and choice in the delivery of public services would be restricted. Local authorities would be prevented from extending and improving the range of services they offer. The introduction of new players into the market would be restricted and Government policy in this area would be put into reverse.

Given that CPA will be formally coming to an end once Comprehensive Area Assessment reports later this year, the Do Nothing approach will create further uncertainty in local government about how Government intends to provide access to the power to trade. Continued linkage to categories which are no longer relevant is not a sustainable solution.

#### *Costs*

- Authorities that have begun to trade successfully would now have uncertainty in whether the power to trade will continue and may start winding up their current trading activities. This could:
  - place a greater burden on taxpayers where the company is trading at a profit and paying dividends to the local authority
  - mean that there would be less competition and diversity of services which could negatively impact on consumers and other businesses which current receive services from the company.
- There would be less scope for collaborative working with the private and voluntary sectors.

#### *Benefits*

- Any uncertainty created by not clarifying how the trading powers will be taken forward and therefore winding down their trading activity, would mean that the local authorities would no longer be subject to the inherent risks of undertaking trading activities (such as financial loss).

### ***Option 2 – 'Grant trading powers to better performers only'***

The successor assessment regime to CPA is CAA. However, there is no direct correlation between the CPA and CAA framework and CAA is an assessment of the area, and not of the individual council's performance. There is also no legislation to enable CAA to provide freedoms to local authorities. Therefore, this option is rejected.

### ***Option 3 – Preserve existing authorities power to trade***

As with Option 1, this means that to some degree, diversity and choice in the delivery of public services would be restricted but there would be certainty about how the Government intended to provide access to the trading powers. As there would be greater certainty around the trading powers than under Option 1, it is likely that more local authorities would undertake trading activities. This means that there could be a greater number of trading companies.

### *Costs*

- preventing authorities with improving performance from accessing the trading powers would not help stimulate innovation and collaboration between councils
- as there would be greater certainty around the trading powers than under Option 1, those authorities with the preserved power to trade would be more likely to undertake trading. This means that authorities would be subject to the risks of undertaking trading activities (such as financial loss).
- authorities without access to the trading powers would not have scope for collaborative working with the private and voluntary sectors.
- greater potential competition for private sector suppliers which could lead to local authority companies taking a greater share of the market.

### *Benefits*

- As there would be greater certainty around the trading powers than under Option 1, it is likely that more local authorities would undertake trading activities. This means that there could be a greater number of trading companies which could lead to:
  - improvements in quality of services provided by some councils.
  - greater competition and diversity in the delivery of services which would have a positive effect on consumers and businesses in receipt of services from the company.
  - increased income streams, potentially leading to a reduction in council tax burdens.

### ***Option 4 - Grant trading powers to all authorities (Preferred Option)***

#### *Risks*

When trading in their ordinary functions, authorities may be tempted to enter into areas of activity for which they are not best qualified and do not have the appropriate level of expertise rather than concentrating on improving delivery of their core functions. Whilst extending access to the trading powers to the 39 authorities is not without risk, there are safeguards in place to ensure that trading is undertaken with an appropriate level of consideration by a local authority (see paragraph 19 above).

#### *Costs*

- This option will provide greater opportunities for more trading companies. Resulting in:
  - start up and running costs for authorities choosing to trade
  - potential for local authorities to distract resources away from core public services, although a strong business case should seek to prevent this.
  - Larger number of authorities subject to the risks inherent in undertaking trading activities (such as financial loss).
  - greater potential competition for private sector suppliers which could lead to local authority companies taking a greater share of the market

## *Benefits*

- This option provides the greatest scope for opportunities under the trading powers as it is providing them to all local authorities. This means that as there will be more local authorities with the trading powers, it provides the greatest opportunity for the most trading companies. This could lead to:
  - greater competition and diversity in the delivery of services which would have a positive effect on consumers and businesses in receipt of services from the company.
  - increased income streams, potentially leading to a reduction in council tax burdens.
  - maximum scope for collaborative working with the private and voluntary sectors.
  - Improvement in quality of services provided by councils, through enhanced competition
  - More councils able to seek collaborative opportunities with other sectors from having access to trading powers

## **Monetised Costs & Benefits**

30. The proposal will extend the power to trade under the 2003 Act to a further 39 authorities. We know from research that 29% of authorities use the 2003 trading powers but that only 3% make significant use of the powers. This would suggest that 11 authorities might avail themselves of the powers and between one and two authorities would make any significant use of the power. Thirty-eight out of the 39 authorities that the power would be extended to are small, lower-tier authorities and it would seem unusual for these authorities to make significant use of these powers.

31. Whilst we do not know how many services an authority would choose to trade in, the research suggest a cautious approach and it seems unlikely that any of these authorities would trade in more than 1 or 2 functions, at least initially. There would be minimal costs in setting up a trading company and start-up costs for the operation (for example, preparing a business case is unlikely to exceed £10K). However the business case for an operation under the 2003 powers should demonstrate how a commercial return is to be achieved and set-up costs and start-up costs should be scoped in that document. The assumptions and calculations informing the Summary Analysis and Evidence are outlined in the textbox below.

#### **Range of scenarios under option 4**

*Potential uptake due to the extra 39 authorities having access to the trading powers*

##### Assumptions

The application of the power is discretionary and therefore there could be no trading company established as a result of the statutory change. However, given that 4 businesses are known to exist:

- It is assumed that **one additional trading company** is established as a result of the extension of the powers to the 39 local authorities currently excluded from the trading provisions.
- However, the number of additional local authority as a result of the statutory change is most likely to vary between 0 and a maximum of 2. These values are used in calculating the range of Present Values shown in the summary table above.
- The average turnover of a 'mature' local authority trading business is approximately £13.5m (based on average turnover of 3 example local authority companies – the fourth business with over £100m in turnover is treated as an outlier).
- The gross profit margin is approximately 8% (based on average gross profit of the 3 example local authority companies). The average operating cost of the additional trading business is obtained by subtracting the profit margin from the average estimated turnover. (Thus the operating cost of the mature business is calculated to be approximately £12.5m).
- Any new business created as a result of the change in the legislation results in a start-up trading business with a total initial turnover of £5m (and operating cost of £4.6m). Over a 10 year period this increases to the estimated £13.5m turnover of a 'mature' business (implying an annual average compound growth rate of approximately 12%).
- Based on evidence drawn from existing trading companies, the initial start-up cost is put at £50k.

##### Average Annual Totals and Present Values

Using the assumptions described above, it is calculated that:

- The mean annual turnover of one additional trading business is £8.6m over a 10 year period.
- The mean annual operating cost of one additional trading business is £8m over a 10 year period. (Based on the calculation that cost is equal to the difference between total revenue and the gross profit margin of 8%).
- The mean gross profit over the 10 year period is £0.6m
- The present value of the estimated cost of operating an additional trading business is £67m over the 10 year period. (i.e. using the base year estimate of £4.6m which grows to £12.5m in the final year).
- The present value of the estimated revenue achieved through operating an additional trading business is £72m over the 10 year period. (i.e. using the base year estimate of £5m which grows to £13.5m in the final year).
- The net present value of one additional trading company is £5m, however, given the assumption above that the expected outcome is likely to lie between 0 and 2 businesses created as a result of the statutory change, the net present value could vary between 0 and £10m.
- A discount value of 3.5% was used in the present value analysis.



## Recommended Option

32. Option 4 is the recommended Option. It provides the greatest flexibility while minimising the risks involved. The benefits of the preferred option include: improvement in quality of services through enhanced competition. There would be opportunity for more councils to generate revenue from having access to trading powers and more councils able to seek collaborative and partnering opportunities with SMEs and the wider private and voluntary sectors by having access to trading powers. Revenue generated would enable local authorities either to invest in public services or used to keep down council tax.

33. Evidence would suggest that of the 39 authorities that the power would be extended to, only a small percentage of those authorities would actually make any significant use of the power. The combined revenue spending power of the additional 39 local authorities is just over 1% of the total local authority revenue spend for 2007/08 and therefore represents a very minor potential increase in local authority market activity. The preferred option would prevent those authorities already undertaking trading activities from having to wind down those activities and losing access to revenue generated through trading. The LGA have pressed and the Lyons Inquiry recommended that trading powers should be extended to all authorities to remove any uncertainty about continued access.

## Small Firms' Impact Test

34. Whilst the trading powers mean that authorities are potentially trading in competition with the private sector, various safeguards have been built in. Safeguards include requiring authorities to adopt a genuinely risk-based approach, based on a sound business case prepared for the proposed trading activity. The arrangements secure that authorities are not able to distort markets through the provision of inappropriate subsidies to trading companies. In order to maintain a level playing field with local businesses, the new powers to trade will be subject to a requirement that it must take place through a corporate body formed by the authority. This means that surpluses on commercial operations under the new power will be subject to taxation in the same way as for other companies. Local authorities like other bodies are subject to and must abide by competition law and State Aid principles.

35. The statutory guidance on local authority trading, *General power for local authorities to trade in function related activities through a company*<sup>39</sup>, is clear that authorities should consider the requirements of competition law for any proposed charging and trading activities. The INLOGOV survey data suggests that 27 percent of trading authorities voluntarily undertook such assessments for trading preceding the 2003 Act. Case study evidence suggests that the impact of local authority trading on the business community can have positive effects. Some benefits identified were local opportunities for sub-contracting, and the delivery of back-office and transactional services to local community and not-for-profit sectors.

## Competition Assessment

36. A full Competition Assessment carried for the Regulatory Impact Assessment published to coincide with the introduction of the *Local Government Bill 2003*.

37. The underlying assumptions in the analysis have not changed since then. The trading powers were made available to local authorities in 2004 and the new Order merely makes some changes to the authorities covered following alterations to the CPA regime.

38. In summary the conclusions of the Competition Assessment were:

- the new powers could lead to increased contestability and/or increased competition in markets (especially those which are currently inefficient or less active)

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<sup>39</sup> <http://www.communities.gov.uk/publications/localgovernment/generalpower>

- greater levels of trading by local authorities could lead to efficiency gains through increased economies of scale, and so could benefit consumers through lower prices, better quality, or both
- there could however be a number of adverse effects arising from certain advantages that local authorities may possess, with consequent potential for the abuse of market power
  - conflicts of interest may arise for local authorities in cases where they both regulate markets and participate in them (for example where withholding planning consents would create barriers to entry)
  - the legislation could potentially facilitate collusion between local authorities, thereby adversely affecting private sector businesses, either through increased information asymmetry or affecting bidding outcomes
  - in terms of existing markets, local authorities may be able to exploit the benefits of an existing customer base and crowd out the private sector
  - the legislation may alter the competitive process through increased consolidation and the possible exclusion of small businesses from particular markets.

39. In relation to the bullet points above, it should be noted that:

- the power to trade will only be exercisable through a company structure, which will be subject to regulation in the same way as other commercial bodies (e.g. taxation). This will help ensure a level playing field with the private sector
- local authorities, like other bodies, are subject to and must abide by competition legislation. Trading by local authorities may be subject to the provisions in the Competition Act 1988 and/or Articles 81 and 82 of the EC Treaty (see paragraph 9.5).

40. The *Competition Act 1998*<sup>40</sup> introduced two prohibitions which reflect Articles 81 and 82 of the EC Treaty respectively. The Chapter I prohibition covers agreements between undertakings that have the object or effect of distorting competition in the United Kingdom, or a part of the United Kingdom. The Chapter II prohibition makes unlawful conduct by one or more undertakings which may amount to an abuse of a dominant position in a market in the United Kingdom.

41. Authorities should consider any proposed trading activities very carefully against the requirements of competition law, consulting their own lawyers as necessary. Trading by local authorities may be subject to the provisions in the *Competition Act 1998* and/or Articles 81 and 82 of the EC Treaty.

42. Whether or not a local authority may be considered an undertaking with respect to a particular activity (and therefore subject to competition rules), depends on whether the activity is 'an economic activity'. The new provisions do not make a significant difference in a local authorities' obligation to abide by competition rules.

43. In addition to the general consultation exercise for the 2003 Act, discussions were held with the Small Business Service and the Office of Fair Trading, CBI and other representative bodies for small businesses. The then ODPM also received and responded to written representations from the Federation of Small Businesses on their concerns with the charging and trading provisions in the Bill.

## Impact Assessments

### Equality assessment

44. The trading power is a non-prescriptive enabling power and should not in itself have an adverse impact on equalities. When making use of the trading powers, as part of their legal duty, local authorities should consider whether there are any equality considerations that need to be addressed.

<sup>40</sup> [http://www.opsi.gov.uk/acts/acts1998/ukpga\\_19980041\\_en\\_1](http://www.opsi.gov.uk/acts/acts1998/ukpga_19980041_en_1)

## Health impact assessment

45. The trading power is a non-prescriptive enabling power and should not in itself have an adverse impact on health issues. When making use of the trading powers local authorities should consider whether there are any adverse health impact considerations that need to be addressed.

## Rural considerations

46. The trading power is a non-prescriptive enabling power and should not in itself have an adverse impact on rural issues. When making use of the trading powers local authorities should consider whether there are any adverse rural considerations that need to be addressed.

## **New Burdens Assessment**

47. These are enabling powers and authorities are not obliged to use them. The trading power does not increase the cost of providing local authority services. Successful trading operations can be expected to generate revenue which can be used for further investment in services or for keeping council tax down.

## **Monitoring & Evaluation**

48. The Department will consider how the impact of the revised policy can be monitored and evaluated through its programme of local government research. Given the need to allow some time for the revised policy to take effect, such research is only likely to be carried out in the 2010/11 or later programmes.

## **Summary and Recommendations**

49. ***The recommendation is to extend the power to trade to all local authorities (Option 4 in this Impact Assessment), which the majority of responses to the consultation paper supported. This option provides the greatest flexibility while minimising the risks involved. The benefits include: improvement in quality of services provided by councils through enhanced competition, greater opportunity for more councils to generate revenue from having access to trading powers, and more councils able to seek collaborative and partnering opportunities with SMEs and the wider private and voluntary sectors. Revenue generated will enable local authorities either to invest in public services or used to keep down council tax.***

50. *Evidence would suggest that of the 39 authorities that the power would be extended to, only a small percentage of those authorities would actually make any significant use of the power. The combined revenue spending power of the additional 39 local authorities is just over 1 per cent of the total local authority revenue spend for 2007-08 and therefore represents a very minor potential increase in local authority market activity. The recommended option would prevent those authorities already undertaking trading activities from having to wind down those activities and losing access to revenue generated through trading. The proposal is supported by the local government sector.*

## Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

**Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.**

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Yes	Yes
Small Firms Impact Test	Yes	Yes
Legal Aid	No	No
Sustainable Development	No	No
Carbon Assessment	No	No
Other Environment	No	No
Health Impact Assessment	Yes	Yes
Race Equality	Yes	Yes
Disability Equality	No	No
Gender Equality	No	No
Human Rights	Yes	Yes
Rural Proofing	Yes	Yes

## Summary: Intervention & Options

<b>Department /Agency:</b> <b>Communities and Local Government</b>	<b>Title:</b> <b>Impact Assessment of providing Fire &amp; Rescue Authorities (FRAs) with powers to trade in any of their functions</b>	
<b>Stage:</b> Final	<b>Version:</b> 2	<b>Date:</b> 25 August 2009
<b>Related Publications:</b> Revision of Local Government (Best Value Authorities) (Power to Trade) (England) Order 2004 - Consultation Findings & Final Regulatory Impact Assessment		

**Available to view or download at:**

<http://www.communities.gov.uk/publications/fire/489630>

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**What is the problem under consideration? Why is government intervention necessary?**

The transitional Order for existing limited powers to trade, charging above cost recovery for the provision of specified services outside their core business, for Fire & Rescue Authorities (FRAs) in England ceases on 30 September 2009.

If powers are allowed to cease then FRAs would be deprived of income streams which could potentially be used to reduce the burden on taxpayers

**What are the policy objectives and the intended effects?**

We intend to propose making the power to trade available to all local authorities as part of the freedoms and flexibilities consultation. Currently only higher performing local authorities can trade in any of their ordinary functions which they are not already under a duty to provide. It is our proposal that FRAs in England have the same scope of access to trading powers as local authorities. We anticipate that there will be minimum effect as only a small number of FRAs are currently using the trading powers.

**What policy options have been considered? Please justify any preferred option.**

- a) to do nothing and let powers cease;
- b) extend existing specified FRA trading order until revoked; or
- c) provide FRAs with powers to trade in any services which they are not under a duty to provide.

On balance option c) is the preferred option since it provides the greatest opportunity for FRAs to access income generation and/or reduce the burden on taxpayers. Without the full trading powers FRAs would not have the same scope of access that local authorities do for trading. This would restrict competition and the potential for wider collaboration.

**When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?** Information on costs and benefits will be assessed following the set up and running of the company. Questionnaires and surveys to both suppliers and FRAs will be sent out on an annual basis to monitor the situation.

**Ministerial Sign-off** For final proposal/implementation stage Impact Assessments:

*I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.*

Signed by the responsible Minister:

Ian Austin

.....Date: 2<sup>nd</sup> September 2009

## Summary: Analysis & Evidence

<b>Policy Option: B</b>	<b>Description: Extend current specified FRA Trading Order until revoked</b>
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<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' Costs of running trading companies. Assumed 2 trading companies.
	<b>One-off</b> (Transition)	<b>Yrs</b>	
	£		
	<b>Average Annual Cost</b> (excluding one-off)		
	£ 1m	10	<b>Total Cost (PV)</b> <b>£ 8.6m</b>
Other <b>key non-monetised costs</b> by 'main affected groups' There will be costs incurred by FRAs in setting up trading companies. Potential negative impact on suppliers through increased competition in the market.			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups' Turnover for trading companies. Assumed 2 trading companies over 10 year period
	<b>One-off</b>	<b>Yrs</b>	
	£		
	<b>Average Annual Benefit</b> (excluding one-off)		
	£1.1m	10	<b>Total Benefit (PV)</b> <b>£9.5m</b>
Other <b>key non-monetised benefits</b> by 'main affected groups' Potential for FRAs to generate income which would be distributed back into their budgets to help fund other projects and/or reduce the burdens on taxpayers. Potential benefits to consumers from increased diversity and competition			

**Key Assumptions/Sensitivities/Risks** Those FRAs who trade will be subject to inherent risks in undertaking trading activities.

Price Base Year 2008	Time Period Years 10	<b>Net Benefit Range (NPV)</b> <b>£0.5m to £1.4m</b>	<b>NET BENEFIT (NPV Best estimate)</b> <b>£ 1m</b>
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What is the geographic coverage of the policy/option?			England		
On what date will the policy be implemented?			By 1 October 2009		
Which organisation(s) will enforce the policy?			No enforcement		
What is the total annual cost of enforcement for these organisations?			£ N/A		
Does enforcement comply with Hampton principles?			Yes/No		
Will implementation go beyond minimum EU requirements?			Yes/No		
What is the value of the proposed offsetting measure per year?			£ N/A		
What is the value of changes in greenhouse gas emissions?			£ N/A		
Will the proposal have a significant impact on competition?			Yes/No		
Annual cost (£-£) per organisation (excluding one-off)		Micro	Small	Medium	Large
Are any of these organisations exempt?		Yes/No	Yes/No	N/A	N/A

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)			(Increase - Decrease)		
Increase of	£	Decrease of	£	<b>Net Impact</b>	£

Key: Annual costs and benefits: (Net) Present

## Summary: Analysis & Evidence

**Policy Option:**  
C

**Description:** To provide FRAs with powers to trade in any services which they are not under a duty to provide

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' Costs of running trading companies. Assumed 3 trading companies.
	<b>One-off</b> (Transition)	<b>Yrs</b>	
	£		
	<b>Average Annual Cost</b> (excluding one-off)		
	£ 1.5m	10	<b>Total Cost (PV)</b> £ 12.9m
Other <b>key non-monetised costs</b> by 'main affected groups' There will be costs of setting up trading companies. Potential negative impact on suppliers through increased competition in the market.			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups' Turnover for trading companies. Assumed 3 trading companies over 10 year period
	<b>One-off</b>	<b>Yrs</b>	
	£		
	<b>Average Annual Benefit</b> (excluding one-off)		
	£ 1.7m	10	<b>Total Benefit (PV)</b> £ 14.3m
Other <b>key non-monetised benefits</b> by 'main affected groups' Wider potential than Option B for FRAs to generate income which would be distributed back into their budgets to help fund other projects and/or reduce the burdens on taxpayers. Potential benefits to consumers from increased diversity and competition			

**Key Assumptions/Sensitivities/Risks** This assumes that FRAs will have same powers as Local Authorities and that they will set up a trading company. Those FRAs who trade will be subject to inherent risks in undertaking trading activities. There is a risk is that FRA trading may impact on competing suppliers already in the market

Price Base Year 2008	Time Period Years 10	<b>Net Benefit Range (NPV)</b> £ 0.9m to £1.9m	<b>NET BENEFIT (NPV Best estimate)</b> £ 1.4m
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What is the geographic coverage of the policy/option?			England	
On what date will the policy be implemented?			By 1 <sup>st</sup> October 2009	
Which organisation(s) will enforce the policy?			No enforcement	
What is the total annual cost of enforcement for these organisations?			£ N/A	
Does enforcement comply with Hampton principles?			Yes/No	
Will implementation go beyond minimum EU requirements?			Yes/No	
What is the value of the proposed offsetting measure per year?			£ N/A	
What is the value of changes in greenhouse gas emissions?			£ N/A	
Will the proposal have a significant impact on competition?			Yes/No	
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	Yes/No	Yes/No	N/A	N/A

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)			(Increase - Decrease)	
Increase of	£	Decrease of	£	<b>Net Impact</b> £

Key: Annual costs and benefits: Constant Prices (Net) Present Value

[Use this space (with a recommended maximum of 30 pages) to set out the evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Ensure that the information is organised in such a way as to explain clearly the summary information on the preceding pages of this form.]

### Background/Context

1. The Local Government Act 2003 provides powers for the Secretary of State to make an order enabling best value authorities in England to trade in any of the ordinary functions through a company provided they are functions which they are not already obliged to provide.
2. These powers did not apply to local authorities when acting in their capacity as a Fire & Rescue Authority (FRA). An amending Trading Order, (Statutory Instrument 2004 No 2307) came into effect on 1<sup>st</sup> October 2004 to provide transitional provisions for only those FRAs in England that had interpreted the Fire Services Act 1947 as including a power to trade. It names the FRA and the specific service that the FRA was trading in on or before 1 April 2004.
3. The Trading Order was amended in 2004 (Statutory Instrument 2004 No 2573) in order to correct an error. It was subsequently amended in 2007 (Statutory Instrument 2007 No 385) to allow for the combination of two Fire & Rescue Authorities.
4. At present only those FRAs in England that had interpreted the Fire Services Act 1947 as including a power to trade have access to the limited trading powers. This covers 30 out of the 46 FRAs with access to limited trading powers which can include such services as:
  - Fire safety training other than training which is required to be provided as a statutory duty
  - Hiring out of equipment such as vehicles and workshops
  - Provision of audio-visual training materials, training and conference facilities
  - Training and provision of audio-visual training materials
  - Vehicle maintenance and repair
5. Only 2 FRAs have set up a trading company to date. The available evidence to date has indicated that existing trading powers have not been used widely by FRAs and there has been a limited appetite from FRAs to use extended powers. In the current economic climate this situation may change and would need to be monitored on a regular basis.
6. The FRA power to trade was originally intended to expire on 30 September 2007 when it was to have been linked to the Comprehensive Performance Assessment (CPA). Since CPA was due to cease in 2009 it would only have served a limited purpose to link FRA trading to this system and three options were considered through a consultation process in 2007.

Option A – Do nothing: this would cease the powers for FRAs to trade as from 30 September 2007.

Option B – Extend transitional powers until 2009: this would maintain the status quo by continuing the existing powers for specified FRAs to trade in certain powers until 30 September 2009. In 2009 the approach to trading powers for local authorities would be considered in the light of revised freedoms and flexibilities following the removal of CPA. This would include FRA Trading Powers. Any requests for new specified trading powers for a FRA before 2009 would have to be supported by a business case which would have to be approved by the Department.



Option C – Provide all FRAs with a power to trade in any of their functions. This would allow all FRAs to trade in any of their ordinary functions rather than limiting the power to specified activities. It would be similar to Option B in that it would be reviewed in the light of the changes to freedoms and flexibilities in 2009. A business case and risk analysis would be required to be prepared and approved by the authority to trade in functions case which would have to be approved by the Department.

7. 35 responses were received with 33 answering the questions posed in the consultation. From the 35 responses received:
  - 27 favoured Option B (77%) – this was supported by both FRAs and industry, 5 favoured Option C (14%) – only FRAs supported this option
  - 2 declined to give a preference for their option (6%)
  - 1 respondent supported Option A (3%)
8. Those respondents that favoured Option B saw it as the most practical solution in that it gave adequate time to both FRA and businesses to consider the impact of trading without FRAs losing a potential income stream.
9. Further comments to support Option B included:
  - It will enable evidence based decisions to be made
  - Maintains status quo
  - Allows time until new system of freedom and flexibilities is known in 2009
  - With the need for a business case to extend trading it gives a measure of control to FRA activities
10. One respondent noted that though their preferred choice was Option A they had actually supported Option B in the consultation since they recognised that ceasing trading powers immediately could have a negative impact on income streams and this could have a knock-on effect on the tax payer.
11. Four who preferred Option B stated that they would have equally supported Option C and that this option may have to be considered in the longer term once the new freedoms and flexibilities system is known.
12. Only FRAs (5) supported Option C since they believed it gave greater scope and promoted greater innovation in service delivery. One felt that FRAs were responsible public bodies which should be trusted to act responsibly.
13. One respondent believed that this option would not require the business case to be approved by a stakeholder forum but by the authority alone. This in their view would better embrace the concept of freedoms and flexibilities.
14. However respondents from industry had concerns that the powers in this option would preclude any element of control on the activities of FRAs.
15. The one respondent who favoured option A was opposed to the principle of trading by FRAs. The respondent had concerns about FRAs offering competing services in fire protection, consultancy and training services. They did note that if trading needed to continue that Option B would at least provide opportunity for safeguards to be put in place and give time to gain information on the likely take up by FRAs.

16. They believed that there were currently no mechanisms in place to ensure trading services from FRAs were being offered at market rates and that the public perceived FRAs as the experts in certain areas which could lead to an unfair advantage in the market. They believed that there was still potential conflict of roles with the FRAs acting as both the giver of advice and the enforcer.
17. FRAs have responded to these questions in the past in that they are taking steps to separate their roles and since they have to set up a trading company they are subject to competition law.
18. Concerns over Option A from other respondents were that such removal of powers would have a detrimental impact on potential income streams for FRAs and ultimately have a knock on impact on the tax payer. It was seen as impractical given the time it would take to wind down existing companies.
19. Two FRAs indicated that they currently did not use the trading powers and they did not indicate a preference for their option.
20. On the basis and balance of the findings of the consultation the transitional trading powers were extended until 30 September 2009 to maintain the status quo, without any detriment to the tax payer, until trading powers were reviewed in the light of the removal of the Comprehensive Performance Assessment (CPA).

## **2009 Consultation**

21. There was a 12 week consultation on Proposed changes to the delivery of Local Authorities' and Fire & Rescue Authorities' Freedoms and Flexibilities after the introduction of Comprehensive Area Assessment<sup>41</sup>. This was published on 6 May 2009, and amongst other questions sought views on the proposal to extend the trading powers to all Local Authorities and Fire & Rescue Authorities.
22. The consultation paper, which included the initial Impact Assessments, was sent to over 300 stakeholders including all Local Authorities, Fire & Rescue Authorities, charities and lobby groups, businesses and suppliers including Small & Medium sized Enterprises (SMEs). The consultation closed on 28 July 2009.
23. The consultation considered 2 specific questions in relation to FRA trading:
  - Question 5: Should the power to trade be extended to permit all Fire and Rescue Authorities to trade in all of their services?
  - Question 6: If there is no agreement on the above, should the current FRA Trading Order be extended indefinitely?
24. 37 responses were received to the consultation with contributions from Local Authorities, Fire & Rescue Authorities, Industry (including SMEs) and a charity. Not all respondents answered the specific questions in relation to FRA trading. Where respondents just gave general comments any which were related to FRA trading were also considered.
25. 21 (57%) respondents supported the recommended option to extend all the powers to trade to all FRAs (Question 5). 3 (8%) respondents did not support this and 13 (35%) did not answer this question. Support came from FRAs and Local Authorities. Industry were opposed to this.
26. Reasons for support included:

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<sup>41</sup> <http://www.communities.gov.uk/publications/localgovernment/freedomsflexibilitiescaa>

- will bring Fire and Rescue Authorities into line with the trading powers available to county services as part of a local authority, and into line with the family of local government bodies
- depriving Fire and Rescue Authorities of existing income streams could result in a greater burden on tax-payers which would hinder a more modernised service
- will stimulate a more entrepreneurial public sector and increase partnership working as well as maintaining maximum flexibility for future developments
- will enable Fire and Rescue Authorities to work with local partners to achieve potential efficiency savings e.g. shared services

27. Reasons for opposition included:

- fundamentally wrong for a public sector emergency service to charge for its non core activities
- authorities that provide an advice service should not also act as enforcing agent
- unfair competition – taking work away from SMEs.

28. Similar concerns have been raised in the past and our view was:

- FRAs would not neglect their statutory duties in favour of chargeable activities. To do so would put an authority at risk of intervention for failing to discharge its' statutory satisfactorily. There is no compulsion for FRAs to recover their costs and many chose not to do so
- Fire & Rescue Authorities (FRAs) are taking steps to separate their roles and it is up to them to manage this
- FRAs are constrained in that any service provided on a commercial basis (beyond simple cost recovery) is delivered through a company. This will make them subject to competition law

29. 13 (35%) respondents supported the extension of the existing limited Fire and Rescue Authority Trading Order if the extension of all powers could not be agreed (Question Six). 6 (16%) respondents did not support this and 18 (49%) did not answer this question.

30. Where this was supported it was considered essential so that FRAs did not lose their potential income streams now or in the future. Some of these respondents considered that if this option went ahead that it should be time limited.

31. Respondents who did not support this option either considered that FRAs should have no access to trading powers or that they should have access to the complete set of trading powers as proposed in Q5.

32. Though there was limited response from existing suppliers to the consultation the Small Firms Impact Test (see paras 65-70) demonstrated that 94% of firms contacted did not support the extension of trading powers.

33. The majority of responses to the consultation paper supported the extension of the power to trade to all Fire and Rescue Authorities in England. This approach ensures that Fire and Rescue Authorities have the same scope of access to trading powers as Local Authorities. There would be the opportunity for Fire and Rescue Authorities to generate revenue which they could either invest in fire safety programmes or use to keep down council tax. With

regards to the respondent who did not support the proposal, there are the necessary legal safeguards in place to protect from such abuses of the system. The 2004 Order requires an authority to recover the costs of any services provided to the company. Fire and Rescue Authorities are required to comply with competition law, state aid principles and also the procurement regulations which enforce rules on transparency, free movement of goods and non discrimination.

### **Policy objective**

34. To examine the options to replace the current transitory trading powers for Fire & Rescue Authorities under the Local Government (Best Value Authorities) (Power to Trade) (England (Amendment) Order 2004.

### **Policy Options**

35. Three options have been identified:

Option A: Do nothing and let powers cease;

Option B: Extend existing specified FRA trading order until revoked; or

Option C: Provide FRAs with powers to trade in any services which they are not under a duty to provide.

#### **Option A: Do nothing and let powers cease**

36. This would remove existing powers from FRAs.

#### **Option B: Extend existing specified FRA trading order until revoked**

37. This would maintain the existing powers for certain named FRAs to trade in specified powers. These powers would continue until revoked. Any requests for new specified trading powers for a FRA would have to be supported by a business case.

#### **Option C: Provide FRAs with powers to trade in any services which they are not under a duty to provide**

38. This would allow all FRAs to trade in any of their ordinary functions that they were not under a duty to provide rather than limiting the power to specified activities.

### **Costs and benefits**

#### *Sectors and groups affected*

39. Businesses (including Small and Medium sized Enterprises), consumers, public and voluntary sectors.

40. The powers allow FRAs to engage in activities which are also undertaken by the private sector; however, it is not necessary to assume that FRAs will necessarily be displacing business from the private sector. The trading powers may be used to improve competition and contestability or to fill a gap in the market in the provision of services to the public.

#### **Option A: Do nothing and let powers cease**

##### *Costs*

41. This option would mean that FRAs would be deprived of existing income streams and thereby possibly increase the burden on tax payers. Two FRAs are already trading and there would be resources (cost and time) involved in winding down existing schemes.
42. The costs of closing down a trading company are not known. There would also be costs of transferring staff and pensions back to the FRA. If transfer was not possible then there could be redundancy costs. Assets and stock would need to be disposed of and any outstanding loans covered.
43. There is only the possibility of New Burdens for Option (A) ceasing powers, since FRAs will not have the ability to generate income that they already now have. With Options (B) & (C) the choice of whether to trade or not is up to each individual FRA.
44. There are no anticipated costs for suppliers with this option though there may be an impact in the market due to diversity and choice of services currently offered being restricted and so a possible cost to consumers.

#### *Benefits*

45. Suppliers have the potential to increase their business in markets where FRAs were trading in competing services.
46. FRAs would not be subject to inherent risk in undertaking trading activities.

#### **Option B: Extend existing specified FRA trading order until revoked**

47. There are currently 2 trading companies. The cost and benefit analysis assumes that there will continue to be 2 trading companies over the 10 year assessment period.

#### *Costs relative to the do nothing option*

48. There would be costs in administering the trading company and preparing business cases if extension of powers was required. Our estimates of the costs of setting up a trading company are between £14,000-£16,000<sup>42</sup>. The set up costs provided do not include the cost of any capital equipment. This cost could potentially vary significantly between trading companies.
49. The analysis currently conservatively assumes that the average annual per company costs are half those of the existing trading company that has provided evidence. This company is seen as very effective. The company annual cost is around £1m and so the analysis uses an average annual per company cost of £0.5m. Using this cost assumption and the assumption of 2 trading companies the average annual cost is £1m (£0.5m \* 2) and the **total PV cost is £8.6m** over 10 years. The running costs of trading companies could vary significantly.
50. Suppliers have potential to lose income through FRAs offering competing services in market.

#### *Benefits relative to the do nothing option*

51. There is potential for FRAs to continue to generate income which would be distributed back into their budgets to help fund other projects and/or reduce the tax burden. Though there is little evidence to date the annual per trading company turnover generated so far has been around £1,148,000<sup>42</sup>. The analysis currently conservatively assumes that the average annual per company turnover is half those of the existing trading companies that have provided evidence. The analysis uses an average annual per company turnover of £0.57m.

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<sup>42</sup> Information from existing FRA trading companies

Given the above assumptions the average annual benefit is £1.15m ( $£0.57 * 2$ ) and the total discounted **PV benefit is £9.5m** (over 10 years).

52. The annual turnover may vary significantly between trading companies.

53. No known benefits for suppliers. This option will maintain existing arrangements. There will be a wider diversity and choice in the delivery of public services and so consumers are likely to gain relative to the do nothing scenario.

### **Option C: Provide FRAs with powers to trade in any services which they are not under a duty to provide**

54. The cost benefit analysis assumes that there will be 3 FRAs trading over the 10 year assessment period. Currently there are 30 FRAs with trading powers and 2 actually using those powers. Under option 3 there will be 46 with trading powers so if we assume the same proportion that gives us 3 trading companies.

#### *Costs relative to the do nothing option*

55. There will be the same costs of setting up and running trading companies as Option B (paras 48-49). With wider trading powers it may be more cost effective for FRAs to administer a trading company or join with another FRA or region to set this up.

56. As above the analysis currently conservatively assumes that the average annual per company costs are half those of the existing trading company that has provided evidence. So the analysis uses an average annual per company cost of £0.5m. Using this cost assumption and the assumption of 3 trading companies the annual cost is £1.5m ( $£0.5m * 3$ ) and the **total PV cost is £12.9m** over 10 years. This estimate is conservative regarding the number of trading companies in the future. There could potentially be many more. The running costs of trading companies could vary significantly.

#### *Benefits relative to the do nothing option*

57. Similar benefits to Option B (para 51) though with more FRAs having access to extended powers there would be a wider potential for FRAs to generate income which would be distributed back into their budget.

58. No known benefits for suppliers. There will be a wider diversity and choice in the delivery of public services and so consumers are likely to gain relative to the do nothing scenario.

59. As in option 2 the analysis currently conservatively assumes that the average annual per company turnover is half those of the existing trading companies that have provided evidence. The analysis uses an average annual per company turnover of £0.57m. Given the above assumptions the annual benefit is £1.7m ( $£0.57 * 3$ ) and the total discounted PV benefit is £14.3m (over 10 years). This estimate is conservative regarding the number of trading companies in the future. There could potentially be many more.

### **Sensitivity Analysis**

60. Table 1 below show the sensitivity of total benefits, costs and net benefits to the changes in the assumed number of trading companies under the different options. The net benefit ranges are included in the option 2 and 3 summary: analysis and evidence pages (pages 2 and 3).

Table 1 varying assumed number of trading companies relative to the do nothing

	Assumptions	PV Benefit range (over 10 yrs)	PV Cost range (over 10 yrs)	PV Net benefit range (over 10 yrs)
Option 2	1-3 trading companies more than the do nothing.	£4.8m to £14.3m	£4.3m to £12.9m	£0.5m to £1.4m
Option 3	2-4 trading companies more than the do nothing	£9.5m to £19m	£8.6m to £17.2m	£0.9m to £1.8m

61. As noted above the analysis currently conservatively assumes that the average annual costs per company and the average annual turnover per company are half those of the existing trading company that has provided evidence. This company is seen as very effective. Table 2 shows the results when it is assumed that their per company figures are used as the average figures in the analysis.

Table 2 varying assumed average annual cost and turnover

	Assumptions	PV Benefit (over 10 yrs)	PV Cost (over 10 yrs)
Option 2	Average annual turnover £1.1m  Average annual cost £1m	£19m	£17.2m
Option 3	Average annual turnover £1.1m  Average annual cost £1m	£28.6m	£25.8m

*Race equality assessment*

62. The trading power is a non-prescriptive enabling power and should not in itself have an adverse impact on race equality. FRAs are under a legal duty to eliminate race discrimination and to promote equality of opportunity and good race relations in carrying out their functions. When making use of the trading powers, as part of their legal duty, FRAs should consider whether there are any race equality considerations that need to be addressed.

*Health impact assessment*

63. The trading power is a non-prescriptive enabling power and should not in itself have an adverse impact on health issues. When making use of the trading powers FRAs should consider whether there are any adverse health impact considerations that need to be addressed.

## *Rural considerations*

64. The trading power is a non-prescriptive enabling power and should not in itself have an adverse impact on rural issues. When making use of the trading powers FRAs should consider whether there are any adverse rural considerations that need to be addressed.

### **Small Firms' Impact Test (SFIT)**

65. On the question of extending trading powers to FRAs, a Small Firms Impact Test (SFIT) was sent in May 2009 to over 300 businesses including SMEs. 34 responses were received from:

- 26 (76%) - organisations with 0-20 employees
- 3 (9%) - organisations with 21-49 employees
- 4 (12%) – organisations with 50-249 employees
- 1 (3%) – organisation with 500+ employees

66. Out of these responses the majority (94%) did not supporting the extension of FRA trading powers. The particular concerns were similar to the Industry responses to the consultation (para 27). There were also concerns that the market share would be reduced and that the public perception of the Fire and Rescue Service would give them a brand advantage. The respondents that supported extending FRA powers considered that they could improve their access to the Fire & Rescue Service market through this option.

67. The SFIT sought further evidence of the costs to businesses of current FRA trading and how these costs would be affected by extending FRA Trading Powers. It was noted that evidence of impact of existing trading was hard to come by however the majority considered that extending existing powers would have a negative impact on businesses in costs, prices being offered and potential redundancies.

68. Only 2 FRAs have set up a trading company so it is not possible to analyse whether they have had any specific impact on SMEs to date. Other factors such as the economic climate and a wide range of suppliers in the market may also have an impact on the market. In the past FRAs have shown little appetite to use their Trading Powers due the resources needed in setting up a trading company. This is unlikely to change in the immediate short term.

69. Whilst the trading powers mean that FRAs are potentially trading in competition with the private sector, various safeguards have been built in to the use of the powers. Safeguards include requiring authorities to adopt a genuinely risk-based approach, based on a sound business case prepared for the proposed trading activity and cleared by the authorities' executive.

70. The arrangements secure that FRAs are not able to distort markets through the provision of inappropriate subsidies to trading companies. In order to maintain a level playing field with local businesses, the powers to trade are subject to a requirement that trading must take place through a company within the meaning of Part V of the Local Government and Housing Act 1989. This means that surpluses on commercial operations under the power will be subject to taxation in the same way as other companies. FRAs like other bodies are subject to and must abide by competition law.

### **Competition Assessment**

71. A full Competition Assessment was carried out for the Regulatory Impact Assessment published to coincide with the introduction of the Local Government Bill 2003. The assessment concluded that such powers could lead to increased competition in the market



though it was difficult to deduce the effects of such competition. Though there were potential greater efficiency gains for authorities through economies of scale there were also a number of potential adverse effects such as possible abuse of market power and conflicts of interest.

72. Many of the issues raised above, in relation to a local authority's assistance to a company, transparency, state aid and competition law, are addressed in the Trading Guidance. Such considerations would apply equally to a FRA as to a local authority
73. In relation to FRA suppliers have been concerned about FRAs offering competing services in fire protection, consultancy and training services. It was felt that there were no current mechanisms in place to ensure such services were being offered at the market rate. The public perceive FRAs as the experts in certain areas and this could lead to an unfair advantage in the market. There were also issues over the potential conflict of role with FRAs acting as both the giver of advice and the enforcer.
74. In July 2006 the Chief Fire Officers' Association sent out a survey to all the FRAs in England. This asked for information on current and future trading activities. Information gained from this was inconclusive though some FRAs indicated that they were unlikely to carry on with trading activities in the future.
75. The power to trade is only exercisable through a company structure, which is subject to regulation in the same way as other commercial bodies (e.g. taxation). This helps ensure a level playing field with the private sector.

### **Enforcement, Sanctions and Monitoring**

76. The trading power is an enabling power therefore there are no non-compliance issues. There are no sanction requirements for the trading powers. Any sanctions for non-compliance with the legislative duties under the trading legislation, or under any other legislation, will be a matter for the courts if necessary.
77. Having in place a business plan is a requirement of the legislation governing FRA trading and the business plan has to be approved by the Authority. Any failure to comply with the requirement to have an adequate business plan in place would be a matter for the Court and authority's auditor.
78. Any FRA trading company would be required to submit its accounts to Companies House by the end of January of each financial year. Future questionnaires and surveys to both suppliers and FRAs will be sent out on an annual basis to monitor the situation.

### **Race, Disability and Gender Issues**

79. The policy options proposed are not expected to have a disproportionate impact on individuals based on their race, gender or any disability.

### **Summary and Recommendations**

80. The recommendation is to provide FRAs with powers to trade in any services which they are not under a duty to provide (Option C).
81. The majority of responses to the consultation paper supported the extension of the power to trade to all Fire and Rescue Authorities in England. This approach ensures that Fire and Rescue Authorities have the same scope of access to trading powers as Local Authorities. There would be greater opportunity for Fire and Rescue Authorities to generate revenue which they could either invest in fire safety programmes or use to keep down council tax.

82. Removing powers (Option A) could have a negative impact on income streams for FRAs which could have a knock-on impact on tax payers. Extending the limited FRA trading powers only (Option B) would leave 30 out of 46 FRAs with access to restricted powers. This would mean that FRAs would not be in line with other local authorities with regard to trading powers and potential generation of income.

## Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

**Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.**

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	No	No
Sustainable Development	No	No
Carbon Assessment	No	No
Other Environment	No	No
Health Impact Assessment	No	No
Race Equality	Yes	No
Disability Equality	Yes	No
Gender Equality	Yes	No
Human Rights	No	No
Rural Proofing	No	No