

Report of the Chief Finance Officer and the Director of People
Portfolios of the Executive Members for Culture, Leisure & Communities
and for Economy & Planning

Make It York – Impact of Covid-19

Summary

1. Make It York (MIY) has formally approached the council for financial support to mitigate the impact of Covid-19 on the company. This paper proposes a series of actions to respond to MIY's request.

Recommendations

2. The Executive is asked to agree to:
 - a) Waive the requirement for MIY to make a revenue return to the council in 20/21 in respect of trading activity across the city centre
 - b) Defer the first two quarters rent due from MIY in 20/21 for use of premises on Museum Street and Silver Street offices
 - c) A loan facility from the council of £300k to be accessed by MIY only if necessary
 - d) Officers to provide a letter of guarantee to MIY with access to a maximum of £1m over the next 2 years should it be required.

Reason: to secure the future of Make It York.

Background - The impact of Covid-19

3. Whilst MIY was previously financially successful, meeting its budget targets and producing a £35k annual dividend for the council, the last two quarters have been extremely difficult for the company, as they have for millions of businesses across the country. MIY's revenues have been decimated and, although the company's board has reduced costs and cut all non-essential spend, these measures have not been sufficient to ensure the business's commercial viability.

4. A report to the council's Shareholder Committee on 5 November set out the company's current financial position and the forecast to March 2025, including details of projected income growth and cost reduction measures, together with associated risks. The report sought to strike a balance between taking the necessary measures to mitigate MIY's current financial position and maintaining sufficient capacity to deliver a meaningful and useful service. The Shareholder Committee asked the MD to do further work to strengthen the evidence base for the projections, to refine them, and to update them to reflect the effects of the current lock-down. That work is reflected in the current paper.
5. Having begun the year relatively cash rich, MIY is now coming to the point where its cash and reserves are almost exhausted, and the company is in a negative balance sheet position. If no action is taken, the following would result:

To March 2021:

- a) Profit and Loss: (£1,260k)
- b) Balance Sheet: (£1,145k)
- c) Year-end cash: (£420k)

To March 2022:

- d) Profit and Loss: (£135k)
- e) Balance Sheet: (£1,280k)
- f) Year-end cash: (£552k)

The Council's company

6. MIY's directors have a legal duty not to run an insolvent business. Unless the council intervenes to support MIY's financial position the directors would have to appoint a liquidator / insolvency practitioner without delay in order to wind up the company.
7. If MIY does not remain a going concern the consequences for the council and for the city will be severe. MIY is wholly owned by the council and, as the city's destination management and city marketing organisation, is charged with providing key functions relating to tourism, inward investment, business support, culture, events and city centre management. Key points to note are:
 - There would be major disruption to services if MIY were to be wound up. Notably, Visit York (VY) would immediately cease to function, severely limiting the city's post Covid-19 recovery

plans. The loss of VY would also cause significant damage to the long-term development and management of York's vital tourism economy and would have major repercussions within the sector at both local and national level.

- There would also be disruption to vital operational areas such as management of Shambles Market until such time as alternative management arrangements could be determined and put in place.
- Any requirement to bring services within the council would be complex and disruptive since MIY has its own terms and conditions, reflecting its commercial sector positioning, and any transfer would be subject to TUPE arrangements. Such a transfer would involve the council in very significant additional ongoing expenditure as staff transferred onto council terms and conditions.
- The MIY Teckal company model has been commercially successful for the council reducing the initial subsidy required by MIY from £554k p.a. in 2015 to £290k p.a. currently and facilitating investment in new products and services. This has been achieved through the entrepreneurialism facilitated by the company model leading to the development of new and increased income streams. The benefits of this commercial approach would clearly be lost if MIY were to be wound up.
- If MIY were to be wound up in December the company would leave significant debts. In particular, the company would not have sufficient cash to make the legally required redundancy payments that would be owing to staff. There would therefore be a real prospect of a large number of staff being made redundant without any compensation.
- As the company is wholly owned by the council there is no doubt that its creditors would look to the council for restitution.

Assumptions underlying MIY's projections

8. Profit and loss, balance sheets and year-end cash forecasts are attached as annexes to this paper. They are based on the following assumptions.

Cost reductions:

9. MIY has taken advantage of the government's furlough and furlough extension schemes with respect to VIC and city centre teams. Staff will return from furlough in December if lock-down ends. MIY also took advantage of the government's VAT and rates deferrals. The

other opportunity potentially available to MIY was a Coronavirus Business Interruption Loan; however, given that the company would require a facility of up to £750k for the next two years, and that the bank would require Directors' guarantees in respect of 20% of that, this was not a realistic option.

10. All operating costs have been scale back wherever possible: waste collection, heating, cleaning, security, consumables, etc. It would be possible to reduce costs further by keeping the VIC closed for the five remaining months of this financial year, saving £18,500. As a core MIY function, however, essential to the city's recovery, this is not recommended.
11. The MIY team have considered the scope to reduce property costs; however, the costs of moving and fit out will not currently deliver a saving. This will be monitored over the coming months and may become an option if realistic alternatives become available including an alternative use for the existing premises. The principal opportunity to save costs now is a programme of redundancy and the financial effects of this have been factored into the projections. Options for how these staffing reductions will impact are being considered alongside discussions between the board and the council with regard to MIY's future role.

Revenue projections:

12. Projections across the key areas of the business are as follows:

	Original budget 20/21	Revised budget 20/21	Projected budget 21/22	Projected budget 22/23
VY Membership	£325k	£180k	£249k	£249k
MIY Membership			£50k	£50k
VIC	£833k	£81k	£417k	£639k
Website advertising	£57k	£40k	£77k	£100k
York Pass	£693K	£161k	£350k	£519k
Publications	£299k	£100k	£250k	£250k
Shambles Market	£629k	£321k	£795k	£795k
Other City Centre	£160k	£0	£174k	£174k
Christmas	£875k	£0	£656k	£975k

13. The basis on which these various projections are made is shown in Annex 1. The projections take a prudent approach with regard to income streams that depend on customer footfall; however, reductions are balanced to some degree by new income streams to be delivered by employing new skills within the organisation, such as digital marketing expertise, which will deliver a more proactive approach to sales, including through targeting new organisations. Wherever applicable the projections are based on feedback from existing clients / partners.
14. The projections are of course subject to a range of variables including the ongoing impact of Covid-19. Depending on the length of the crisis, together with limitations on business operation, consumer demand, restrictions on travel, and the wider impact on the economy, the “actuals” may be worse than those forecast. Equally, they may be better. In preparing the forecasts, MIY’s accountants, Morrell Middleton, have sought to take a conservative approach albeit one informed by discussion with around 80 relevant sectoral businesses (drawn from the approximately 700 businesses that they support) with regard to levels of business confidence going forward. Ultimately, should MIY perform less well financially than forecast, it will be necessary to renegotiate elements of delivery through the service contract in order to allow MIY to reduce its costs further.
15. It should be noted that MIY’s accountants have projected that any further lock-down would see a loss of gross profit of circa £90k per month. If Christmas 2021 were to fall within a period of lockdown that gross loss of profit is likely to reach £1m.

Make It York’s ask of the council

16. To enable MIY to continue to operate and deliver its services while also allowing the business the opportunity to return to a positive balance sheet position during the 24/25 financial year, the board of MIY has requested the following from the council:
 - a) 20/21 revenue contribution from MIY to CYC in respect of trading in Shambles Market, the foot streets and Parliament Street to be written off. The rationale for this is that due to the COVID crisis MIY has not been able to utilize these assets (including over Christmas which, for accounting purposes makes up over 50% of the rent). The exception to this is Shambles Market, although that has had a significant period of closure and then rent-free occupation. The sum in question is £474k.

- b) Defer 20/21 rent on Museum Street and Silver Street offices. It is proposed that the first two quarters rent are deferred in line with other council tenants. A repayment plan is currently being negotiated with the company with respect to the sum owing.
- c) A loan facility from CYC of £300k to provide a degree of ongoing operational security. To be accessed only if necessary.
- d) A “parent company guarantee” from the council until such point as a positive Balance Sheet position is restored (currently forecast as during the 25/26 financial year). It is not intended that this should lead to expenditure on the part of the council; however, it will provide a guarantee that the council will cover MIY’s liabilities should the company fail. This is required for audit purposes to demonstrate that MIY is a going concern until the Balance Sheet position is restored.

17. The impact of the requested package in MIY’s financial position is forecast to be as follows:

Financial Year	Profit and Loss £’000	Balance Sheet £’000	Year-End Cash £’000
March 2021	(696)	(581)	144
March 2022	(135)	(716)	12
March 2023	194	(521)	222
March 2024	360	(161)	567
March 2025	338	177	885

18. The table above reflects that the company would return to profitability in 2022/23 and retained profit in surplus by 2024/25. There will be further options for cost reduction / income generation to bring this position into a positive position in advance of this date.

What MIY will deliver for the council

19. The current contract between MIY and the council comes to an end on 31 March 2021. Detailed discussions are taking place between the company and officers with regard to the key elements of the contract specification for the next period. Clearly, what MIY can deliver for the council is closely linked to the funding that is available to it. A report on the contract specification will be brought back to the Executive in February. This will also set the ongoing annual

funding to MIY by the council in respect of the service contract going forward.

Options

20. The Executive may:
 - a) Agree the financial support package requested by MIY
 - b) Decline to provide the requested support package

Analysis

21. Option a) offers the prospect of MIY returning to being a going concern as it was before Covid-19. With a lower cost base, a high quality and clearly focussed staff group, MIY will be in a strong position to “build back better”. It will allow for more detailed discussions to take place with the council over the shape of the contract from April 2021 and for options to be developed with regard to the priorities that MIY should address for the council. It will also allow for discussion to take place with regard to the ongoing level of the council’s financial support to MIY during the next contract period.
22. Option b) would result in the MIY directors, in line with their legal duty, ceasing to operate the company as an insolvent business and taking the necessary steps to wind it up. This would lead to the immediate cessation of the important functions that MIY provides, for example, its destination management role. This, in turn, would require the council to decide whether to provide any of MIY’s functions within the council. If so, relevant MIY staff would be subject to TUPE transfer. A winding up of the company would also mean that its financial deficit could not then be recovered and its liabilities would need to be addressed immediately. A large part of MIY’s debt is owed to the council but there are other creditors and they will inevitably look to the council, as MIY’s sole shareholder, to cover MIY’s debt.

Council Plan

23. The proposals in this report further the priorities in the Council Plan with regard to *well-paid jobs and an inclusive economy and safe communities and culture for all*.

Implications

24. **Financial:** The budgetary impact of the recommended position is a budget gap within the Economy and Place budget of £474k in 2020/21 as the planned rental payments will not be received. It is proposed that the cost of this is funded from the general Covid-19

support grant. This will be incorporated into the Monitor 3 update to Members in February 2021. The deferral of rents will result in a reduced rent commercial rent received in 2020/21 but will still be due in future years.

25. Should a cash loan be required by MIY there is capacity within the Venture Fund to provide funding over a short term position to assist with cash flow issues (one to two years).
26. Should Members decide to decline the support package under option B, the council would be required to assume responsibility for the Assets and liabilities of MIY. This would result in a net increase in liabilities on the council's balance sheet in the Statement of Accounts. The ongoing cost of running the services currently provided by MIY would also return to the Council and potentially result in increased net expenditure.
27. The Council would also have to consider TUPE legislation and the terms and conditions of MIY staff to bring them back in house which could potentially be a time consuming and costly process.
28. Should Members decide to provide a financial guarantee to MIY, additional disclosures and accounting adjustments would be made in the Council's Statement of Accounts in line with the CIPFA Code of Practice.
29. **Legal Implications:** The provision of support to MIY under Option A in the form of writing off the revenue contribution for the year 20/21, rent deferral, a potential loan and a parent company guarantee could amount to State aid under Art. 107(1) of the Treaty for the European Union. In order to be considered to be lawful State aid, the following will need to be put in place:
 - a) Writing off any debt(s) or amounts owed to the Council – any debts written off or re-negotiated by MIY and the Council must comply with the Market Economy Investor Principle, that is to say any deal entered into by MIY and the Council in respect of any existing debt(s) owed by MIY to the Council must be comparable to the behaviour of hypothetical private creditors that find themselves in a similar situation, and any terms offered by the Council to MIY should not be more generous than what the rest of the market is doing.
 - b) Rent deferrals – any rent deferrals again must comply with the Market Economy Investor Principle; in this context, they must be comparable to what hypothetical private sector landlords on the commercial property rental market are doing under comparable

circumstances, and again any terms offered by the Council to MIY should not be more generous than what the rest of the market is doing.

- c) Potential loan/guarantee – any loan or guarantee must also comply with the Market Investor Economy Principle. Any loans or guarantees negotiated between the Council and MIY must be benchmarked and offered on commercial terms that are compatible with those being currently being offered by other private sector loan providers and/or guarantors/sureties on the market generally.
30. Due to the COVID-19 pandemic, the European Commission implemented a State aid Temporary Framework to support the economy which (at the time of writing) was originally due to expire on 31 December 2020, but has now been extended until 30 June 2021 (subject to further review by the Commission). If it were not possible to apply the Market Investor Economy Principle to the rent deferrals or the loan/guarantee, it would be possible to still achieve lawful State aid by applying the provisions set out in the Framework. However, at the time of writing, the European Rules on State Aid (including the Temporary Framework) only apply to the UK until the end of the Brexit Transition Period (i.e. until 23:00 on 31 December 2020). After this time, it remains unclear, at this stage, what the rules will be going forward; e.g. as part of any trade deal agreed between the UK and EU, will current State Aid rules for the most part be kept in UK Domestic Law as “Retained EU Law,” but overseen by domestic oversight body (CMA), or will it be WTO subsidy rules if there is no deal? Therefore, if we intend to apply the provisions of the Temporary Framework then we need to do so by no later than 31 December 2020, subject to any updates and announcements from the UK Government on State Aid post-Transition Period.
 31. Option A will also require the negotiation and drafting of formal loan and/or guarantee agreements, as well as any other legal paperwork to formalise the waiver of the revenue contribution for 20/21 under MIY’s contract with the Council and any rent deferral under their existing leases with the Council, which will require the input of Legal Services.
 32. As per the Financial Implications above, if members choose to proceed with Option B above, and not provide the support package sought by MIY, this is likely to result in the Council assuming the assets and liabilities of MIY under a form of transfer agreement to be negotiated, as well as the formal termination of the existing contract and lease arrangements, and the removal of the company from the

Register at Companies House. In addition, Option B will also result in relevant transfers of staff from MIY to the Council under TUPE.

33. **Property Implications:** As the report sets out, MIY have agreed to pay all rental sums owed on the basis of a repayment plan to be negotiated.
34. There are no other implications arising from the report.

Risk Management

35. As identified in paragraph 12 above, the projections contained in this report are based on a number of assumptions and could change significantly. In particular, they could be negatively impacted by any worsening of the situation with regard to Covid-19, especially and further lock-down.
36. In compliance with the council's risk management strategy the main risks that have been identified are those which could lead to the inability to meet business objectives (Strategic) and to deliver services (Operational), leading to financial loss (Financial), damage to the council's image and reputation and failure to meet stakeholders' expectations (Governance).
37. Measured in terms of impact and likelihood, the risk score has been assessed at 16, placing the issue in the high category. This means that constant active monitoring, will be required together with an action plan and measures to reduce exposure.

Annexes

1. Income generation assumptions
2. Cashflow forecast to year end 20/21
3. Cashflow forecast to year end 21/22
4. Cashflow forecast to year end 22/23
5. Cashflow forecast to year end 23/24
6. Cashflow forecast to year end 24/25

Contact Details

Authors:	Chief Officers responsible for the report:
Charlie Croft Assistant Director (Communities and Culture) Patrick Looker Finance Manager	Amanda Hatton Director of People
Report Approved ✓ Date: 2 December 2021	
Specialist Implications Officers: Dan Moynihan Senior Solicitor – Contracts & Commercial Nick Collins Property Manager – Commercial	
Wards Affected:	All ✓

For further information please contact the author of the report