

## Appendix 2

# Commercial Development Unit Outline

### Introduction

A sustained period of austerity measures has seen all local authorities operating in extremely challenging financial landscapes with grant income falling while demand for many services is rising. Nottinghamshire County Council has, like many other organisations, responded to the challenges by instituting a programme of cost cutting. But cost cutting in itself is unlikely to close the financial gap without significant reductions to service.

The need to cut costs can be reduced through income generation activity that creates a net surplus once the full costs have been taken into account. These surpluses can then be re-invested in services that benefit the residents of Nottinghamshire.

The aim of the Commercial Development Unit is to set up and support the services with the greatest potential to generate repeatable income that results in a surplus.

### The Model

The model is loosely based around the successful incubator model that has been developed by Essex County Council. This model would establish a corporate approach to the assessment of a service's potential to trade at a surplus by identifying the opportunity, any required investment and potential risk / return. It is important to note that this assessment would be carried out in partnership with the service rather than something that is done to it. It enables the service to take a commercially critical look at itself and the market it would be entering. It is designed to get the service into a commercial mind set and furnish it with the tools and specialist knowledge to make a full assessment of the market, competitors, pricing and how it would operate in this market. This allows the service to have full visibility of the required investment and potential return on investment by generating a net surplus.

The Unit involves a process where the intention is that the service will move through it to eventually become self-sufficient and self-standing. This would then allow other services to enter the process.

There are six stages in the process:

- **Stage One** – services either volunteer proposals or are selected as an area which has the potential to trade commercially
- **Stage Two** – The Commercial Development Unit provides an initial quick sense check to ensure there are no obvious barriers such as legal/regulatory/statutory issues. Once selected, the unit would plan out the resources needed for a pre-assessment phase
- **Stage Three** – The service enters the process at the pre-assessment phase which would last for three months. During these three months the service would be preparing for the assessment board where it would have to present a fully-costed

business case and balanced scorecard. This phase would involve the following elements:

- Coaching, support and account management
  - Masterclass training in commercial tools and methodology
  - Sector specific research and analysis
  - Expert support – finance, HR, marketing, legal
  - Development of balanced scorecard
  - Development of business plan
- **Stage Four** – The service goes through an assessment exercise where the business case and balanced scorecard is presented to a Commercial Development & Trading Board which would examine the detail, assess its viability and makes a decision about what proposal to make out of the following three:
    - The business plan and investment is approved and it moves on to the next stage of full incubation
    - It is felt that the business plan needs further work and more preparation time is needed before being re-assessed
    - The business plan is not viable and the service leaves the process
  - **Stage Five** – If the service and the required investment is approved to move forwards, it then enters the full 12-month development period, where the service continues to receive support as it goes to market and starts trading.
  - **Stage Six** – Once it is felt that the service is up and running and operating successfully it will no longer be in the Unit but will enter a performance monitoring phase. The Unit will assess how it is performing against its agreed outcomes and make suggestions for improvements. The service will continue to report back progress to the Commercial Development & Trading Board. After three years if the service is performing it will no longer be monitored within this process.

### **Commercial Development Unit**

The Commercial Development team will need a very specific skill set that includes the following:

- Strategic thinking and planning
- Commercial mind-set and experience
- Analytical and data driven
- Coaching and mentoring
- Relationship / account management
- Target and results focussed
- Detail orientated
- Planning skills
- Project management
- Understands the Council's values and corporate objectives

Importantly, the unit would need to possess the gravitas and respect from colleagues across the Council in order to operate effectively.

Alongside the key commercial skills, the team will need to pull in specialist advice in areas such as HR, legal, procurement and marketing, as well as sector specific advice and guidance.

It is anticipated that there will only be two specific roles within the team:

**Commercial Development Business Partner** – works with the service to provide coaching and mentoring throughout the process

**Market & Business Data Analysis Officer** – ensures the Service has all the data it needs and supports the Service in interpreting the data.

The above roles will be supported by both a Service Director & Group Manager.

The positioning of the unit within the structure is yet to be decided but it is likely to be influenced by the wider review of the senior management structure already announced by the Chief Executive.

### **Traded Services Board**

Effective governance will be a key component of success. Both the Commercial Development Unit and the individual services need to be held to account. But equally if they are to succeed they need governance that matches the needs of business in terms of speed and responsiveness.

The Board would assess the business case, risks and required investment of the traded service. It would then make a recommendation to the service committee or policy committee. The exact make-up of the Board would need to be decided but it is proposed that it could contain the following:

- Member representation
- Chief Executive
- Section 151 Finance Officer
- Monitoring Officer
- Scrutiny Officer
- Legal counsel

### **Training, Coaching and Mentoring**

One of the key aspects of the model is to empower services with the knowledge, skills and commercial focus to run their service as a successful commercial operation. This is achieved through a number of master classes that provide services with the tools to set out a robust business plan as well as the skills and knowledge to operate commercially. These are not standard training events, they are focused on the practical application of the subject matter in the context of which the service will be operating and will include:

- Marketing
- Sales
- People and change
- Process and structure
- Financial management

Additional training maybe required, but this is identified through both the master class and business planning process.

Whilst services are moving through the commercial development process they have weekly 1-1 progress reviews and surgeries. These meetings allow the Commercial Development Unit to monitor and gauge progress as well as ensuring internal resource is provided and any external coaching, training or advice is facilitated.

### **Commitment of service**

In order to justify the resource needed, the service needs to commit to the process and its demands from the outset. The first level of commitment is to produce a full business case and balance scorecard for presentation at the assessment phase. After approval the service has to commit to start operating and generating a set amount of income as well as other conditions specific to the Service. This could take the form of a performance contract.

The service must report on a monthly basis the current months trading / finance, and then forecast for the next quarter and the year.

If the service is not performing to the required level this could result in the investment being removed and the service being reshaped.

### **Incorporation, ownership & branding**

As a traded service it is not an essential requirement to become fully incorporated. Unless trading is dependant on a certain commercial vehicle, services will initially be encouraged to start trading as a fully owned in-house service. Traded companies should only be considered where the business case justifies it and once the service has shown that the surplus income set out in the business case is achievable.

As a part of the business case the service area should set out the need for its position on branding. Any move away from the authority's brand would need to be fully justified in the business case.

### **Business case and balance scorecard**

The business case and balance scorecard is a key outcome of the incubator process. It sets the scope of change needed; the case for investment, risk, potential return on investment and timescales. It is this that allows an informed decision to be made. It also sets out the plan, milestones and targets for the first 12 months.

The main business case will contain all the elements of the balance scorecard as seen below and covers areas that explore market size, competition, finance, delivery, timescales, leadership, change management, performance management. The balance scorecard will also help to identify the service's capability gaps which will then allow a plan to be developed in terms of addressing this area.

By adopting the approach outlined, the authority will understand at the outset any development needs before a service is able to trade commercially and competitively. A decision can then be taken if the scale of change is worth the possible return on investment via a surplus.

It also allows a fuller impact assessment on other internal services, such as legal, HR, finance, ICT and communications, and systems such as payroll and BMS. This will also assist support services in their planning as they will have an idea of the scale of change as delivery models change and more services consider commercial operations.

The balance scorecard is a strategic planning and management system that is used extensively in business to align business activities to the vision and strategy. It can also be used as a way to assess the needs of a service before it embarks on a route to increased commercialisation.

Balance scorecards come in many shapes and sizes but the following has been developed with the council services in mind and the type of areas that need to be assessed before any decision can be taken about investment.

Sales & Marketing		Systems & Processes	
Size of Market and sales potential	Market Access & Routes to Market	Extent of organisational change needed	Balance of NCC work and surplus generating
Competitive position	Brand Awareness	System & Process Change	Access needed to NCC systems & Processes
Staff Capability	Commercial Capability	Ongoing costs	Margin & Surplus Potential
Leadership & Management	Culture change required	Scalability	Current & Potential income streams
People & Change		Financial Management	

### Implementation Plan

In addition to the business plan a separate implementation plan will be devised that will set out the required internal resource required to take the service to market. This will allow support services such as finance, HR and IT to understand the requirement and commitment of resources required.

Any support service that is supporting the implementation and / or commercial operation will be compensated for the provision of its service.

### Costs and return on investment

There will need to be investment in the right service areas if the authority is going to generate surplus income. The Commercial Development Unit will enable services to fully understand their cost base and also those areas where there is the potential for return on investment. The running costs of the Unit would be recouped from the total surplus made from services that are helped by the Unit to operate more commercially.

The costs of the unit are projected to be in the region of £160,000 the costs will be relative to the number of services going through the development unit at any one time. The financial forecast has assumed three services going through the process at any one time. Based on this model the Unit will generate a surplus in year two. As more services enter the process and as more services that have left the Unit mature the amount of surplus will increase leading to long-term sustainable surplus growth.

An important factor in both the recovery of the Unit's operating costs and ability to generate a surplus is the size and potential of the service area. Financial modelling has shown that in order to achieve a return on investment that generates a worthwhile surplus and covers the Unit costs early in the lifecycle that only services that generate or have the potential to generate an income of £500,000 or more should be considered for the first five cohorts. Anything below this is unlikely to provide the required payback. This should not prevent those services that have high potential growth that are not currently generating this level of income entering the Unit.

The financial modelling and forecasting has been based on a number of principles and simplistic assumptions that have been uniformly applied:

- Income estimates have been taken from actual income (not including grant and academy income)
- Operating costs is estimated to be 90%-100% of the income
- Operating costs estimated to grow at a rate of 4% in year one and then reduce in years two and three
- Income estimated to grow by 5% year on year
- The CDU will cover its costs from the surplus
- Services for Schools does not include Catering, Cleaning or Landscaping
- Some services within Services for Schools will make a loss

There are a number of elements that would change the return such as a change in the operating cost or levels of growth, but as a forecast made with the above assumptions then the return would be:

Year	1	2	3	4	5
	-£145,620	£329,869	£577,641	£1,185,187	£2,061,508

Over five years the CDU and services operating commercially could generate up to £4 Million in surplus income.

### **Next Steps**

The most important part of this process is the gateway review element, as it is this that indicates the viability of the commercial service. It is proposed that a pilot is run that takes two service areas through the first three stages in order to deliver a full business case. This would then be reviewed as a proof of concept prior to seeking any further approval.

Using existing NCC staff along with support from staff at Essex County Council would allow the concept to be tested quickly without the need to recruit to the Unit. It would also help us

to set up many of the required processes and ensure they are fit for purpose in a quick and efficient manner.