Notice is hereby given that pursuant to Section 24 and Schedule 7 of the Local Audit and Accountability Act 2014 (“the Act”), KPMG, the external auditor for Northampton Borough Council (“the Council”) at the relevant time, has issued a report in the public interest (“PIR”) regarding the Council’s loans to Northampton Town Football Club (accounts for the year ended 31 March 2016**).**

In accordance with the requirements of the Act, anytime between 10am and 4pm on weekdays any person may inspect the report and make a copy of it, or any part of it, at the Council’s offices at The Guildhall, St Giles Street, Northampton NN1 1DE. Due to the Coronavirus pandemic individual full copies of the report will be made available for collection from the One Stop Shop or sent out by post on request by emailing legalservices.nbc@northampton.gov.uk

If you wish to view the report in person then please contact Judy Goodman (Practice Manager) on 01604 837409 before attending the One Stop Shop and please satisfy yourself that you are complying with the latest Coronavirus rules. Arrangements will be made if allowable under lockdown rules for the report to be safely provided to you. Alternatively, the report is available at the website address above.

Dated on 27th January 2021.

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Northampton Borough Council: Report in the public interest regarding the Council's loans to Northampton Town Football Club (accounts for the year ended 31 March 2016)

Summary

A. We are issuing this report in the public interest under section 24 and Schedule 7 of the Local Audit and Accountability Act 2014 (the "Act"). We have discretion whether to make a report in the public interest where we consider that there is a matter that should be considered by the audited body or brought to the attention of the public.

B. Northampton Borough Council ("NBC" or the "Council") is required under the Act to publish the report as soon as practicable, consider it at a meeting within one month, decide what action it will take in response and publish a summary of that decision.

C. This public interest report concerns NBC's loan to Northampton Town Football Club ("NTFC") and reports on significant failures of corporate governance and items of account that are, in KPMG's view as the Appointed Auditor to NBC, contrary to law. This matter was brought to our attention by officers of the Council in November 2015, and we subsequently received an objection to the Council's Statutory Accounts for 2015/16 during the period that they were open for inspection. We investigated the issues raised and within our remit and this report sets out our findings in relation to the process that the Council went through in making the loan and also in how they managed the loan once it was made.

D. NBC's relationship with Northampton's sporting clubs (including NTFC) has been mixed over the years (and since 2008), with well-publicised claims from NTFC that the Council was not doing enough to support them. A scheme to redevelop NTFC's stadium site (Sixfields) was put forward by NTFC and supported by the Council's Leader. The scheme was intended to expand the East and West stands, create a range of new facilities, including a conference centre, a 100-room hotel, a gym, and up to 300 new homes and offices.

E. On 17 July 2013, NBC's Cabinet made an in principle decision to loan monies to NTFC to pay for improvements to the Sixfields stadium and to build a hotel next to the stadium. The Council would also buy land from the Homes & Communities Agency ("HCA") adjacent to the Sixfields stadium and enter into a Joint Venture Agreement with a private company, the HCA, and NTFC, for the development of that land. The Cabinet delegated authority to the then Chief Executive (David Kennedy), in consultation with the then Director of Finance/Section 151 Officer (Glenn Hammons) and the then Leader of the Council (David Mackintosh) to make the loans, subject to five conditions which were set out in the Cabinet report (and are summarised at paragraph 8 of this report). These five conditions included that there was sufficient tangible security offered by NTFC to the Council, and that there were robust contractual arrangements in place between NTFC

and a financially sufficient third party in relation to the proposed hotel development. The Cabinet also delegated authority to the then Director of Regeneration, Enterprise & Planning (Steve Boyes) to enter into a conditional sale of land, subject to three conditions which were set out in the Cabinet report (and are summarised at paragraph 8 of this report). These conditions included that the Council is not exposed to any risk of financial loss or liability from its participation within the JV agreement.

F. Three loan agreements were prepared and funding was provided to NTFC between September 2013 and August 2014. Further details of the arrangements surrounding the loan are set out in the 'Background' section of this report.

G. In late 2014 the works to improve the East stand at the stadium ceased following a dispute between NTFC and the developers (1st Land Limited) which resulted in the building contractors (Buckingham Group Contracting Limited) not being paid. The dispute was resolved when a new contract was signed with a new developer, County Developments Northampton Limited ("CDNL"), and work recommenced on the stadium in early 2015, but in the spring of 2015 work ceased on the stadium again when CDNL did not pay the building contractors. At this time loan repayments to the Council started to be late, but repayments were made until early autumn 2015 when all loan repayments from NTFC to the Council stopped. Consequently, the loan agreement was cancelled by the Council and the development company, CDNL was put into liquidation by the contractor, Buckingham Group Contracting Limited. During this period NTFC was placed under the threat of a winding up petition from HMRC which could have resulted in NTFC going into administration or liquidation. A Memorandum of Understanding between the Council and the new owners of NTFC was agreed in November 2015 to collaborate and work together to ensure the continued survival of NTFC. The Council then impaired the loan within its 2015/16 Financial Statements.

H. Our investigation into these matters has led to us making the following key findings in this report (this list is not exhaustive and full details of our findings are set out in the report):

   a. There were worrying gaps in the Council's knowledge at the time of making the decision in principle. For example, there was no formal financial business case submitted by NTFC until after this decision on 17 July 2013. Certain matters would have, in KPMG's view, been better addressed prior to the 'in principle' decision (in particular whether the stadium improvements were actually needed);

   b. This project was championed by the former Leader and, other than points raised by three non-Cabinet members attending the Cabinet meeting on 17 July 2013 (noted in the report), it appears to have been agreed without having been subject to any robust challenge by his fellow Cabinet members;

c. The agreement at the in principle stage included that the £5m proceeds of sale of the development would be used by the Council to offset the debt owed by NTFC. In our view that was inappropriate and there seems to have been no or insufficient benefit or any discernible rational reason to NBC to reduce NTFC's debt in this way. Furthermore, although the sale did not in the event go ahead, if the £5m had been applied as outlined in the 17 July 2013 report it would have, in our view, run a high risk of constituting unlawful State Aid to NTFC;

d. Although professional advice was obtained before making the loans, a report by PWC (NBC's internal auditor) found that "there was insufficient time available to ensure that all matters identified were adequately addressed and resolved before signing the agreements." This included advice in relation to State Aid. In our view the Council did not ensure that it followed the correct steps to ensure that the loans were lawful and did not represent State Aid;

e. The then Chief Executive authorised loans totalling £13.5m which was in excess of the "up to £12m" quoted in the Cabinet paper of 17 July 2013. The Council advanced a further £1.5m for the stadium in April 2014 with inadequate due diligence undertaken as to why the extra money was needed nor what the previous £4.5m loaned until that point had actually been spent on. Officers had sought legal advice which determined that although the background in the Cabinet report referred to "up to 12m", since the recorded decision did not reference a specific figure, additional Cabinet approval was not required and entering into facility agreements for up to £13.5m was in line with the existing decision. In KPMG's view this advice was incorrect and the delegation as to amount was subject to the overall limit quoted in the report and it is unreasonable to interpret this as being given authority to approve any size loan. We have concluded that in our view this decision went beyond the delegated authority and was therefore unlawful;

f. NBC has confirmed that a full assessment of the income projections was undertaken as part of agreeing the original loan in September 2013, and that the business plan was subject to regular review in meetings between the Council and NTFC. However the results of the review were not reported to any Committee (due to the delegated authority in place). In KPMG's view, the results of the income projection review should in all the circumstances have been reported back to Cabinet;

g. The Council was prepared to enter into a conditional agreement to sell land to a company (CDNL) that was proposed by NTFC without going through any competitive procurement process. NTFC and CDNL had directors on common, which is a further issue with regard to legality and financial and corporate governance which we would have expected the Council to have picked up on and considered the implications;

h. There was inadequate due diligence undertaken by the Director of Finance/Section 151 Officer, including an inadequate assessment of whether the work would generate assets capable of being refinanced by NTFC in order to repay the loans to the Council and of the financial viability of NTFC. The Section 151 Officer has provided an explanation of this and given his view that the due diligence undertaken was sufficient taking into account the circumstances at the time. In KPMG's view, nevertheless, taking into account the significance of the project and the amounts loaned (which were known at the time), there was inadequate assessment of whether the financial projections put forward by NTFC were reasonable, and inadequate assessment in advance of the loan of the security put forward by NTFC. The Section 151 Officer at this time, Glenn Hammons, was formally appointed to the role on 15 July 2013, two days before the Cabinet's in principle decision to approve the loan. In practice he had been engaging with the Council in relation to the Cabinet report from early July 2013 and as such had a reasonably informed knowledge of the proposal before it went to Cabinet and was decided upon. We deal with this issue in more detail at paragraph 50 of the report;

i. The officers with delegated authority entered into the loan agreements without ensuring that all of the conditions on their delegated authority were met:

    i. Whilst one of the conditions required of the Chief Executive was satisfied and two conditions could be deemed as being partially satisfied, two were in our view definitely not satisfied: we have concluded (and subsequent independent reviews, reports and events have borne out), that the security provided by NTFC was neither sufficient nor tangible; and, there was no robust contractual arrangement in place between NTFC and a financially sufficient third party. In KPMG's view, failure to meet these conditions rendered the decisions taken further to the delegated powers unlawful;

    ii. Of the three conditions placed on the Director of Regeneration, Enterprise and Planning, we believe that two were satisfied but one was not, namely that the Council should not be exposed to any risk of financial loss or liability from its participation within the JV agreement.

As a result of the JV partner (CDNL) being liquidated, the Council incurred significant cost in ensuring that it still has control of the land and it has meant that the land has not been developed. In KPMG's view, the Director of Regeneration, Enterprise and Planning should have been able to foresee the risk of the Council being exposed to financial loss or liability and should have mitigated that risk accordingly. In KPMG's view, failure to meet this condition rendered the decisions taken further to the delegated power unlawful.

I. In summary, we have identified what in our view are serious failings in the Council's arrangements when deciding to and subsequently making the loan to NTFC. The Council has accepted in discussions with us that its arrangements fell short of the required standard in a number of respects, and it has commissioned a complete review of governance arrangements in order to address the shortcomings. In addition, NBC's internal auditors, PWC, carried out a review of these matters in 2016 and produced a report in November 2016 entitled "Review of policies and procedures relating to the provision of loan finance to Northampton Town Football Club". However, we have decided that acting proportionately, we should issue this public interest report to ensure that the matter is brought to the attention of the Council and the public setting our detailed views on these matters.

J. In conclusion, this whole episode demonstrates poor decision making based on inadequate reports leading to public money being lost, and demonstrates the need for careful thought, structure, independent advice and monitoring in making such decisions on a transaction which was significant and unusual. There was a near complete lack of an approved business case, appropriate independent advice and documented risk management and proper governance process followed. Documents presented to Members for decision making purposes and records of decisions taken by officers were deficient.

K. Whilst carrying out our review, we identified areas for improvement in the Council's arrangements. Our recommendations to address these areas are set out in Appendix B to this report. We note that the Council has taken some steps to address a number of these areas already, but we include all recommendations in this report for completeness.

Background

Our Work

1. This matter was brought to our attention as the Appointed Auditor, by officers of the Council in November 2015 and we subsequently received an objection to the Statutory Accounts for 2015/16 during the period that these were open for inspection.

2. We therefore investigated the issues raised and within our remit and this report sets out our findings in relation to the process that the Council went through in making the loan (Stage 1) and also in how they managed the loan once it was made (Stage 2). What happened to the money once it arrived in NTFC is primarily a matter for the Police. Thus, we need to stress that:

   (a) We have not investigated what happened to the loan money once it was received by NTFC.

   (b) It is also a matter for the Police to consider whether any action should be taken against current or former officers or members; and

   (c) We have not reviewed the way in which the Council has sought to recover its money.

3. In thematic terms our work can be summarised as being a review of the Council's stewardship of public money, and to achieve that by:

   (a) looking at the decision to accept and enter into the transaction in accordance with the Council's policies;

   (b) reviewing the loan agreement;

   (c) reviewing the governance over the decision and subsequent action;

   (d) reviewing the risk management over the transaction;

   (e) reviewing and considering the performance management arrangements for the transaction;

   (f) critically assessing the management information with regards to the transaction;

   (g) reviewing the financial controls over the transaction; and

   (h) considering the project management over the transaction.

Background facts

4. The Sixfields site has been both a development opportunity and challenge for the Council for a number of years; it is a useful size and close to the Town centre but has contaminated land (the site was previously used for landfill) and there are issues around whether retail development would move business away from the town centre.

5. Northampton has an impressive sporting pedigree, with First-Class Cricket, Premiership Rugby Union and a professional football club. The Council's relationship with these clubs, especially the football club (NTFC) has been mixed over the years (and since 2008), with well-publicised claims from NTFC that the Council was not doing enough to support them.

6. The scheme to redevelop Sixfields was put forward by NTFC and supported by the then Council Leader as set out in the manifesto for the election at that time. The scheme proposed to expand the East and West stands, create a range of new facilities, including a conference centre, a 100-room hotel, a gym, up to 300 new homes and offices. As such the scheme proposed by NTFC had a number of attractions to NBC; it was intended to increase the stadium's capacity and add conferencing and hotel facilities which would generate sufficient revenue to finance the development and put NTFC's finances on a more solid footing. It would also secure the development of the Sixfields site which is in the Northampton Waterside Enterprise Zone.

7. On 17 July 2013, the Cabinet of NBC took what was in effect an in principle decision to loan monies to NTFC to pay for improvements to its Sixfields football stadium and to build a hotel, which built on a 2011 Conservative election manifesto pledge – "*A Conservative administration will actively support development plans for retail and commercial opportunities that will provide our sports clubs with funding for the development of their teams and facilities."*

8. The Cabinet delegated authority to the then Chief Executive (David Kennedy), in consultation with the then Director of Finance/Section 151 Officer[1] (Glenn Hammons) and the then Leader of the Council (David Mackintosh) to make the loans, subject to

[1] Section 151 of the Local Government Act 1972 requires every local authority to make arrangements for the proper administration of their financial affairs and requires one officer to be nominated to take responsibility for the administration of those affairs. As such the Section 151 officer has a number of statutory duties, including the duty to report any unlawful financial activity involving the authority (past, present or proposed) or failure to set or keep to a balanced budget. In addition, the Section 151 officer is usually the local authority's treasurer and must be a qualified accountant belonging to one of the recognised chartered accountancy bodies. The Section 151 officer has a number of statutory powers in order to allow this role to be carried out, such as the right to insist that the local authority makes sufficient financial provision for the cost of internal audit.

five conditions as set out in para 3.2.1. of the 17 July 2013 Cabinet report. In summary, these conditions were:

(a) That there would be no net initial or later costs to the Council of setting up, administering and servicing any borrowing it makes in order to provide loan finance to the clubs;

(b) That there is sufficient tangible security offered by the clubs to the Council from the time of taking the loan until full repayment is made (it was noted that *"in the case of NTFC this may be via legal charges on a combination of assets or other appropriate arrangements"*);

(c) That the length of the loan its repayment are linked to the timing of additional revenue generated from the expansion, with the principle that any money loaned should be repaid in the shortest possible time;

(d) That the income projections from additional revenue generated as a result of the expansion is sufficient to service debt owed to the Council; and

(e) In the case of the hotel development, that there are robust contractual arrangements in place between NTFC and a financially sufficient third party concerning certainty of minimum levels of income.

The Council further delegated authority to the then Director of Regeneration, Enterprise & Planning (Steve Boyes) to enter into the conditional sale of land, subject to three conditions. In summary, these conditions were:

(a) That the Council is satisfied that the proposed comprehensive development scheme will be viable and generate positive value for the land owners;

(b) That the Council is not exposed to any risk of financial loss or liability from participation with the JV agreement; and

(c) That adequate arrangements are made to re-provide suitable athletics facilities at an appropriate location.

9. We were informed by the Council that LGSS[2] had the legal obligation to provide Section 151 services to the Council from 1 June 2013. However, the decision as to who to appoint to this role was a matter for the Council. The then Chief Executive wanted the

[2] LGSS is a public sector shared service scheme, which provides business support services to public sector organisations. LGSS provided services to NBC through a partnering and delegation agreement, including professional finance services. Individuals appointed to assist NBC through this agreement were not employees of NBC.

Council to formally approve the appointment, so he took a report to the Appointments and Appeals Committee on 25 June 2013 and to Full Council on 15 July 2013 to obtain formal approval of Glenn Hammons to this role.

10. Three loan agreements were prepared and funding provided to NTFC between September 2013 and August 2014. The Council also updated the Parking and Fair Licences during this period. In addition, the Council also prepared a contract with developers County Developments Northampton Limited ("CDNL") and NTFC for the Sale of Freehold Land with Vacant Possession Conditional on Planning Permission for Land at Sixfields Northampton, and a Counterpart Lease with CDNL relating to Land at Sixfields Northampton. A key part of this contract was the relocation of the athletics facilities and the availability of alternative facilities during the development stages, as the local Athletics Club used the facilities available on the land leased by NTFC. Also, in April 2014 an Agreement for Sale and Purchase of Land at Sixfields Northampton was made between the Homes and Communities Agency and the Council. The purpose of these additional contracts, leases and licences that the Council entered into was for the development of residential and commercial properties around Sixfields on land owned by the Council and the Homes and Communities Agency. The Council believed that receipts from this development and additional revenues arising from the improved facilities at the stadium would repay the loan.

11. However, in late 2014 the works to improve the East stand at the stadium ceased following a dispute between NTFC and the developers (1st Land Limited) resulting in the building contractors (Buckingham Group Contracting Limited) not being paid. The dispute was resolved when a new contract was signed with a new developer, CDNL, and work recommenced on the stadium in early 2015, but in the spring of 2015 work ceased on the stadium again when CDNL did not pay the building contractors. It was noted that CDNL was owned and run by two of the NTFC directors.

12. At this time loan repayments to the Council started to be late, but repayments were made until early autumn 2015 when all loan repayments from NTFC to the Council stopped. Consequently, the loan agreement was cancelled by the Council and the development company, CDNL was put into liquidation by the contractor, Buckingham Group Contracting Limited. During this period NTFC was placed under the threat of a winding up petition from HMRC which could have resulted in NTFC going into administration or liquidation. A Memorandum of Understanding between the Council and the new owners of NTFC was agreed in November 2015 to collaborate and work together to ensure the continued survival of NTFC.

13. The Council then decided to impair the loan within its 2015/16 Financial Statements and this was agreed by cabinet on 24 November 2015.

14. NTFC was then sold to a new buyer and a Memorandum of Understanding was put in place with the new owner.

15. The Council confirmed in the 2015/16 Statutory Accounts that "reviews and investigations with regards to the loan and the land development at Sixfields are ongoing and encompass: an Internal Audit review by NBC's Internal Auditors PwC into the Council's processes and procedures, to be reported to NBC's Audit Committee; an External Audit review by NBC's External Auditors KMPG *(sic)*; and a Police Investigation into any potential criminal activity behind the previous owners of NTFC and associated companies."

An explanation of the project and the loan values

16. A summary of how the above proposal was intended to proceed (as documented in the paper to Cabinet on 17 July 2013) follows below:

    (a) The Council would incur no net initial or later costs for setting up, administering and servicing any borrowing it in turn makes, whether via the Public Works Loans Board (PWLB), or from any other external source (the Council ultimately decided to borrow from the PWLB);

    (b) The Council would make an overall loan of up to £12m (later increased to £13.5m – see (c) below) to NTFC in order that they could rebuild the East Stand to increase capacity and add conference facilities and build a hotel next to the Stadium;

    (c) Following the approval by the Cabinet in July 2013, the specific breakdown of loan amounts were as follows: a First Facility Agreement of £7.5m (for the Stadium); a Second Facility of £1.5m (additional monies for the Stadium); and a Final Third Facility of £4.5m (for the Hotel);

    (d) NTFC would make payments (mostly interest, but some capital) to the Council from the additional revenue generated by these developments;

    (e) The Council would buy land from the Homes & Communities Agency ("HCA") that was adjacent to the Sixfields Stadium and the athletics track (which the Council already owned);

    (f) The Council would enter into a Joint Venture Agreement with a private company, HCA (as necessary) and NTFC for the development of that land forming part of Sixfields Stadium, together with other adjoining HCA land, on the basis that an agreement relating to a disposal at nominal initial value of the freehold interest to the private party concerned may be required to be completed prior to the commencement of physical development. The private company was later agreed as CDNL, which would build houses and retail properties on the site and sell them for profit;

(g) That subject to the legal considerations (including State Aid), that the net value generated for the Council from any Joint Venture Agreement that may be entered into, may be used in whole or part to reduce any levels of debt owed by NTFC to the Council. Following approval by Cabinet, it was agreed thatCDNL would re-pay the Council £5m (later increased to £6.5m) payable over the sales period of the development, as individual properties or land (both residential and commercial) were disposed of for value by freehold transfer or grant of a lease at a premium. The Council would use the £5m receipt from CDNL to reduce the amount of the loan outstanding from NTFC;

(h) As part of the agreement with CDNL following approval by the Cabinet, it was agreed that in addition to the repayment amount from CDNL (on behalf of NTFC) to reduce the loan, there would additionally be an "overage agreement" (i.e. when the sales revenues of the development exceeded an agreed value of £110m, then the Council would be entitled to receive half of the difference between the sum of £110m and the actual realised gross sales revenues, with these sums paid on completion of each property disposal);

(i) NTFC would, at some stage in the future, refinance the loan (i.e. borrow from another source) and repay the remaining loan balance to the Council;

(j) In the event, £10.25m is the amount that was actually drawn by NTFC under the three loan agreements; and

(k) £10.22m is the amount that was outstanding at the time the Council impaired the loans (as reported in the 2015/16 Financial Statements).

17. The original Cabinet report included reference to loan finance of "*up to £12m*"; however, the subsequent loan facility agreements entered into eventually totalled £13.5m.

Stage 1 - Making the loans

18. Whilst there was no form of initial loan request from NTFC provided to us by the Council, the development of Sixfields has been subject to discussion at Executive and Cabinet for a number of years. Examples of the previous papers presented to Cabinet were recorded within the decision-making paper to Cabinet on 17 July 2013. These two papers from 28 January 2008 and 11 July 2012, considered formally changes to the lease agreement with NTFC to allow for the development of a hotel and latterly

the development of land at Sixfields, whereby the paper presented to Cabinet on 11 July 2012 at 3.1.4 stated "NTFC wish to expand and improve Sixfields Stadium and the Council supports this aspiration." NBC confirmed that ongoing discussions had been held with NTFC in the years before the paper was delivered to Cabinet. Neither of these previous papers were included in the pack for decision making at the 17 July 2013 Cabinet meeting.

19. Additionally, in the paper presented to the Cabinet meeting on 17 July 2013, there was no reference to a previous paper which had also been presented to Cabinet on 5 August 2009. This 5 August 2009 paper, included an earlier proposal from NTFC and an unnamed development partner, requesting that the HCA and NBC transfer the freehold value of the Sixfields Stadium and land around the stadium for development. Proceeds from the residential and commercial development would then be used to build a new athletics track within Northampton, with remaining proceeds being shared between NTFC, HCA and NBC. The proposal also requested that NBC and HCA would then re-invest its share of the final proceeds into the re-development of the football stadium. HCA had stated any potential support to NTFC would be on the proviso that there would have to be clearly demonstrable community benefits and it was more appropriate for the Council to decide on what these would be. The Cabinet supported the Council entering into a development agreement with the HCA, NTFC and a development partner, on the basis that:

(a) there would be no conflict with preserving and enhancing the commercial vitality of the Town Centre;

(b) that the stadium itself continues to be used for Association Football and other uses described under the existing lease; and

(c) that replacement athletics facilities are built to UK Athletics Competition Standard for track and field, within Northampton prior to any redevelopment of the existing facilities.

The Cabinet at the time supported the principle that the Council should transfer its freehold interest of the Sixfields Stadium only in part, prior to physical development taking place on that land, but only in circumstances where the Council was first satisfied that there would be sufficient legal safeguards and financial guarantees to protect the Council's position. The Cabinet supported in principle NTFC's aspirations to improve the facilities at Sixfields Community Stadium and noted the request for the Council to invest, however the Cabinet agreed to resolve not to "*fetter its discretion as to how it might spend any proceeds arising from its participation in any development agreement*."

20. The key power for the Council to make the loan was the general power of competence under section 1 of the Localism Act 2011.

21. There was no formal financial business case submitted by NTFC until after the loans were agreed in principle by the Council's Cabinet on 17 July 2013. This meant there were worrying gaps in the Council's knowledge at that stage. Whilst capable of being cured by officers at the delegated decision making stage (Stage 2 in this report – see below), certain matters – in particular whether the Stadium improvements were actually needed and the financial sustainability of NTFC - would have been, in KPMG's view, better addressed by Council and the Director of Finance (S151 Officer) prior to the 'in principle' decision. Publicly available information from Companies House would have indicated that there were serious questions about the financial stability of NTFC (see further below).

22. Thus, NTFC's average attendance in each of the previous five years was around 4,500 and the capacity of the stadium was 7,500. Yet the Council never questioned whether there was really a need for a stadium that per the loan application seated 10,000 people, i.e. NTFC were asking for an additional 2,500 seats. Similarly, at that stage there was, in KPMG's view, inadequate critical review or challenge about whether there was demand for conference facilities or a hotel and/or the impact that additional provision might have on existing facilities elsewhere, with no clear partner agreements such as an agreed hotel developer for the site.

23. Furthermore, inadequate due diligence was undertaken by the then Director of Finance (S151 Officer). NTFC had received the lowest possible credit rating, had net liabilities of £7.5m and was only able to continue trading because of the assurances provided by the Directors. NTFC's external auditors had included an Emphasis of matter, drawing attention to note 1 in the NTFC financial statements, whereby the Company Directors believed that it was appropriate to prepare the financial statements on a going concern basis, due to their continuing support. These are matters that the Council should have known about.

24. NBC confirmed that the Stadium loan was a key element of the whole deal to redevelop the wider area. The report to Cabinet on 17 July 2013, noted that "the expansion of the stadia and ancillary facilities of both clubs would provide an important short term and longer-term boost to the local economy, with the Northampton Waterside Enterprise Zone. It would help to generate new employment and stimulate and sustain wider economic activity in the Town."

25. From the papers presented to the 17 July 2013 Cabinet meeting however no supporting business case was provided for members with a breakdown of the finances, or justification for the additional seating to be provided. This issue had also been

identified within the Internal Auditors report "Review of policies and procedures relating to the provision of loan finance to Northampton Town Football Club", November 2016, which stated the following:

> *'The recommendation to Cabinet should have contained a detailed analysis of the financial implications and associated sensitivity analyses of the business plan prepared by the Council. Instead, the cabinet paper prepared and presented in July 2013 identifies that "NTFC have indicated they would like to have an agreed facility with the Council for loan finance of up to £12million to support these stadium and hotel / conference centre plans".*

26. There are no further, specific details about the form of this loan or potential repayment options in the 17 July 2013 report. The paper includes a high-level summary of the implications, including: resources, risk, legal and equality considerations. The legal considerations indicate that the Council has the powers to make a loan of this nature but does not analyse the actual exercise of the powers in the circumstances. Approval from the Cabinet was, as noted, a decision 'in principle' and relied on the officers with delegated powers exercising them in accordance with the conditions set out in the report. As noted above, whilst officers could consider these issues under delegated powers, it would, in KPMG's view given the significance to the Council, have been better had the full details been set out at this stage.

27. One further matter at this in principle stage was of particular concern. The agreement was to provide that the £5m proceeds of sale of the development would be used by the Council to offset the debt owed by NTFC. This was, in KPMG's view, inappropriate. A Principal Lawyer, at LGSS Law noted in an email on 4 July 2013 to the Corporate Asset Manager (copying in the Monitoring Officer) that in the 17 July 2013 Cabinet report, *"Para 2.5 … reads as a tacit acknowledgement that the loan will not be repaid in full and is in effect a gift."*. As the sale did not, in the event, go ahead, no money was applied to reduce the debt and so no state resources were used for NTFC's benefit. As such no State Aid issues arose. However, if it **had** been applied as outlined in the 17 July 2013 report and the decision gone ahead, it would, in KPMG's view, have run a high risk of constituting unlawful State Aid to NTFC. There seems to have been no or insufficient benefit or any discernible rational reason to NBC (and the public purse in general) to reduce NTFC's debt in this way. NTFC had already/was about to benefit from a significant favourable loan and NBC had yet to reap the supposed benefits. This would quite simply have been the application of public funds to pay off the loan of a private company – see Appendix A for our further findings and analysis on State Aid.

28. Capita Asset Services prepared a report, at the request of NBC, dated 12 September 2013 (first provided to the Council on 16 September 2013) on the loan to NTFC, two days before the facility agreement for the stadium loan of £7.5m was signed. This

report was watermarked draft and we have not seen an updated or final version. This report concentrated on legal, including State Aid considerations and soft loan and capital accounting implications associated with the financial assistance. Capita Asset Services included a disclaimer, stating that they were not instructed to complete any work on securitisation/collateral or risk and due diligence associated with the proposed loan to NTFC. The Capita Asset Services report included a number of recommendations for NBC to consider prior to signing the facility agreement. NBC have provided an email trail evidencing a conference call with Capita and confirmed in response to a question placed by us that LGSS Law and LGSS Finance had reviewed the contents of the Capita Asset Services draft report. Emails seen by the internal auditors as part of their work entitled "Review of policies and procedures relating to the provision of loan finance to Northampton Town Football Club", November 2016, noted that correspondence on financial, legal and statutory duties in preparing for the facility agreements with due regard to taxpayers money had been undertaken between the Director of Finance/Section 151 Officer, Principal Lawyer for Property, Planning and Highways (LGSS Legal), Legal Contracts and Procurement Advisor (LGSS Legal) and Corporate Asset Manager, Monitoring Officer, Leader of the Council, Chief Executive and Director of Regeneration, Enterprise and Planning. However, as the draft Capita Asset Services report was only received two days before the facility agreement was signed, the internal auditors confirmed that "whilst appropriate professional advice was sought there was insufficient time available to ensure that all matters identified were adequately addressed and resolved before signing the agreements."

29. In the draft report prepared by Capita Asset Services it was stated that "Based on our interpretation of the State Aid requirements, the Authority needs to ensure that any loan provided to NTFC has a rate of interest in excess of the threshold set by the European Commission to be State Aid compliant." Capita Asset Services also provided the following in respect of their advice on State Aid:

> *"If State Aid is deemed to be an issue, the Authority would need to justify the rate it is charging on loan(s) provided to NTFC.*
>
> *……………………………………………*
>
> *To provide a view on applicable margins, we would need additional information about the credit rating of NTFC. But on the assumption that the entity has no credit history and the Authority used a Balance Sheet approach to assess the credit quality, it indicates the margin would not be lower than 400bps.*
>
> *Adding the minimum margin of 400 basis points for a company with no credit history gives a reference rate of 4.99% for the loan."*

30. Following the advice received, those with delegated powers to enter into the loan agreement with NTFC, took the decision to enter into the loan facility at the PWLB interest rate, with the draft loan agreement stating that the interest rate will be confirmed on the loan term sheet applicable to each advance, with no margin applied to the Authority's borrowing cost in respect of the credit risk associated with making the advance. As such, in our view, the Council did not ensure that it followed the correct steps to ensure that the loans were lawful and did not represent State Aid. We set out our further comments and analysis on State Aid in Appendix A.

Stage 2 - Managing the loans

31. The Cabinet approved the loans to NTFC in principle on 17 July 2013, giving delegated authority to the then Chief Executive, in consultation with the Director of Finance/ Section 151 Officer, to approve the amounts and terms of any loan finance arrangements subject to certain conditions. As explained below, not all the conditions were met, yet the agreements were still entered into, which in our view calls into question the legality of the decision-making of the officers further to their delegated powers.

32. The Cabinet also approved the recommendation to enter into a joint venture agreement for the development subject to certain conditions. The Director of Regeneration, Enterprise & Planning was given delegated authority to enter into legal arrangements subject to certain pre-conditions. These pre-conditions were not fully met, yet still the Council entered into the arrangements. In the event, the land involved was not transferred from the Council, but that was despite the Council's actions rather than because of them.

33. Following the approval in principle, NTFC developed a number of business and financial models of the redevelopment of the Sixfields Stadium and for a hotel on the Sixfields site. The earliest version of these models was not received by the Council until August 2013, the month after Cabinet approval.

34. Each variation of the business and financial model was reviewed by the then Director of Finance/Section 151 Officer and LGSS Finance. The Council confirmed to us that the NTFC business plans were assessed via face to face meetings with the Director of Finance/Section 151 Officer and Chief Executive at NTFC. Updated business plans were provided afterwards via email and the Council confirmed that the Director of Finance/Section 151 Officer and a colleague from LGSS Finance challenged each iteration of the business plan and agreed it with NTFC.

35. There was, in KPMG's view, inadequate assessment by the then Director of Finance /S151 Officer of whether the work would generate assets that would be capable of being refinanced by NTFC at a later stage in order to repay the loans to the Council.

36. The then Chief Executive authorised loans totalling £13.5m which was in excess of the £12m quoted in the paper that was approved in principle by Cabinet. The Council advanced a further £1.5m for the stadium in April 2014 with inadequate due diligence undertaken by the then Director of Finance/Section 151 Officer as to why this extra money was needed nor what the previous £4.5m that had been loaned to NTFC up to that point had actually been spent on. The Director of Finance/Section 151 Officer fell short, in KPMG's view, of his duty to protect the financial interests of the Council (and its taxpayers/residents).

37. As stated, in the original 17 July 2013 Cabinet report, reference was made to loan finance of "up to £12m". Officers sought legal advice from LGSS which determined that although the background in the report referred to "up to £12m", since the recorded decision did not reference a specific figure additional Cabinet approval was not required and entering into facility agreements for up to £13.5m was in line with the existing decision. In KPMG's view this advice was incorrect, the decision went beyond the delegated authority and was therefore unlawful. Legality aside, it would in any event have been good practice and for the purposes of transparency and openness to obtain further Cabinet approval for the additional monies intended to be lent as this was a significant sum in excess of the £12m mentioned in the 17 July 2013 report.

38. The minutes of the Cabinet meeting on the 17 July 2013 moreover clearly identify that three opposition non-Cabinet Members who attended the Cabinet meeting raised concerns about the approval in principle. However, their concerns were noted as observations and there was no record of the matter being "called in" to the Overview and Scrutiny Committee despite two of the three non-Cabinet Members who raised concerns noting that the matter should be considered by the Committee. No information has been provided which identifies whether these concerns were investigated and then adequately resolved.

39. NBC confirmed that the due diligence undertaken included an assessment of an updated Business Plan and a development appraisal of the land. In addition, NBC confirmed that they had completed a full set of Dunn and Bradstreet searches in respect of the additional sum requested, on 26 March 2014. However, as noted above, in KPMG's view the checks would ideally have been undertaken before the Cabinet decision in principle. From the evidence reviewed, we could not confirm that even post that decision, the Dunn and Bradstreet reports had been subject to detailed discussion or consideration, despite one of the checks flagging a high risk of business failure.

40. NBC confirmed that a full assessment of the income projections was undertaken as part of agreeing the original stadium loan in September 2013. NBC also confirmed that the additional £1.5m loan was covered by the income projections within NTFC's business plan. NBC confirmed that the business plan was subject to a regular review in

meetings held between the Council and NTFC. The updated business plan was assessed by NBC's Director of Finance/Section 151 Officer and the LGSS Finance team. Evidence of meetings held, iterations of the business plan and emails covering the additional £1.5m were provided. The results of the review of the income projections was not however reported to any Committee, as Cabinet had delegated the authority to the Chief Executive, in consultation with the Section 151 Officer and the Leader of the Council, to approve the amounts and terms of any loan finance arrangements. In our view, the results of the income projection review should in all the circumstances have been reported back to Cabinet.

41. Loan security was to be provided from the proceeds arising from the Development Agreement. NBC commissioned an independent CBRE Viability Validation Report which was received on 12 September 2014. This was not reported to any Committee, given the delegated authority in place. Whilst not strictly required, in our view, as a matter of good corporate governance and the significance of the project overall to the authority's finances, this should have at some point been reported back to Cabinet.

Other areas of note

42. The Council was prepared to enter into a conditional agreement to sell land that was projected to generate £110m once it was developed, to a company (CDNL) that was proposed by NTFC, without going through any competitive procurement process. An issue considered below is how this could have been appropriate given the Council's duty under section 123 Local Government Act 1972.

43. There was clear self-interest for NTFC to propose the development company CDNL as they had Directors in common. This is a further issue with regard to legality and financial and corporate governance, which we would have expected the Council to have picked up on and considered the implications.

44. However, the Council continued to advance money to NTFC even when it was obvious that something was seriously wrong. Quite apart from the lack of progress on site, NTFC submitted a revised planning application on 1 August 2014 which significantly reduced the scale of the stadium expansion.

45. The project was championed by the former Leader and, other than the points raised by three non-Cabinet Members attending Cabinet meeting and noted at paragraph 38 above, it appears to have been agreed without having been subject to any robust challenge by his fellow Cabinet Members. None of the other Cabinet Members were even aware that the Paper they approved contained a provision where it was intended that £5m of Council Taxpayers' money loaned to NTFC was not going to be paid back. We were told by some of the officers and Members we interviewed as part of our review that there had been pressure to complete the deal (mainly from the Leader).

46. We have separated our further findings and then conclusions into **Financial, Legal**, **Regeneration** and **Governance** issues.

Financial issues

47. We have carefully reviewed the evidence as to the due diligence undertaken and sought the view of former officers. Mr Hammons, the former section 151 Officer has provided an explanation of this and given his view that it was sufficient taking into account the circumstances at the time. He has further rightly noted that under the terms of the delegated powers, his role in this particular respect was defined by the level of consultation undertaken with him by the Chief Executive.

48. In KPMG's view, nevertheless, taking into account the significance of the project and the amounts loaned (which were known at the time) there was:

- inadequate assessment by the then Director of Finance (S151 Officer) of whether the financial projections put forward by NTFC were reasonable;

- inadequate assessment in advance of the loan by the then Director of Finance (S151 Officer) of the security over the loan put forward by NTFC. The Council took a charge on the land on which the stadium is built, but:

  - The Council owned the freehold over the land anyway;

  - The land was and is effectively worthless as long as it was and is used for its current purpose, and it would be very difficult to redevelop the site for alternative use; and

  - as proved when NTFC defaulted on the loan, it was highly improbable that the Council would have been able to realise any value from this security.

49. We were informed by the Council that LGSS had the legal obligation to provide Section 151 services from 1 June 2013. However, the decision as to who to appoint to this role was a matter for the Council. The Chief Executive wanted the Council to formally approve the appointment, so he reported to the Appointments and Appeals Committee on 25 June 2013 and to full Council on 15 July 2013 and obtained formal approval of Glenn Hammons to this role. It is therefore unclear who was the Section 151 officer in the lead up to the Cabinet decision on 17 July 2013 until the appointment of Mr Hammons on 15 July 2013.

50. Mr Hammons therefore became the Section 151 two days before the Cabinet approval in principle was obtained. Mr Hammons has told us that he did not receive a detailed handover from his predecessor Section 151 Officer and was not apprised of any

detailed background in relation to this loan. However, Mr Hammons had been engaging with the Council in relation to the Cabinet report from early July 2013 prior to his formal appointment (including commenting on draft versions of the report and making changes which were included in the final version). By the time he commenced his role as Section 151 Officer it is clear from the documents that he was reasonably well informed. In KPMG's view, even though newly in post given the reasonable knowledge base he already had, he should have ensured either that he obtained in the two days before approval by Cabinet, a sufficient understanding to carry out his senior finance role or he should have sought to defer the decision. Mr Hammons has told us that he was satisfied at the time that he had performed his role effectively in line with his statutory obligations and did not consider that a delay was required.

Legal issues

51. The Council had available to it power under the Part 1 of the Localism Act 2011, namely the General Power of Competence.

52. The main legal advice as to whether the exercise of the power was lawful in the circumstances, was received from LGSS Law on 17 September 2013, the day before the first loan agreement was signed and four days after the Conditional Sale of Land was signed. The provision of loan finance to NTFC to support stadium expansion formally commenced on 18 September 2013 with a facility agreement for £7.5m. This was subsequently followed with an additional facility agreement signed 14 April 2014 for £1.5m and a final facility agreement signed on 23 July 2014 for £4.5m to support the hotel redevelopment. This all came to a total of £13.5m.

53. The external advice also contained advice that it was necessary for the Council to charge NTFC a rate of interest that was higher than that at which the Council borrowed the money, in order to ensure that the loan did not constitute State Aid. In the event, the Council loaned the money at exactly the same rate (i.e. 2.5%) that it had borrowed it from the PWLB, for the stadium development. In respect of the £4.5m Hotel facility agreement made on 23 July 2014, this was at an assumed interest rate of 4.1%. See Appendix A for KPMG's views on State Aid.

54. As part of the project, the Council was to enter into an arrangement with a third party to sell a piece of land adjacent to the stadium (this is described more fully under Regeneration, below). The intention was that part of the receipt from the third party would be used to reduce the amount to be repaid by NTFC. At the outset this was intended to be £5m, which in our view, was a decision that, on public law and State Aid grounds (had the sale gone ahead), would have run a high risk of being unlawful.

55. We have summarised above the conditions set for the exercise of delegated authority in the Background section of this document (at paragraph 8). These are the conditions

by which, in effect, any decision taken under the delegated powers would had they been satisfied, been lawful.

56. Whilst one of the conditions required of the Chief Executive was satisfied and two conditions could be deemed as being partially satisfied; two were in our view definitely not satisfied. Specifically, these were:

That there was sufficient tangible security. We have concluded, and subsequent independent reviews, reports and events have borne out, that the security provided by NTFC was neither sufficient nor tangible; and

That there were robust contractual arrangements between NTFC and a financially sufficient third party (i.e. a hotel chain). There was no such arrangement.

57. The Council cannot demonstrate that it fully, properly and formally evaluated and considered whether the five conditions placed with the CEO had been met before proceeding to make the loan payments to NTFC. In the event, failure to meet the two conditions mentioned above, for the exercise of delegated authority, in our view, rendered the decisions taken by the officers further to the delegated powers unlawful.

58. Of the three conditions placed on the Director of Regeneration Enterprise & Planning, in KPMG's view two were satisfied but one was not – namely and specifically "*that the Council should not be exposed to any risk of financial loss or liability from its participation within the JV agreement.*" As a result of the JV partner (the developer, CDNL) being liquidated, the Council has incurred significant cost in ensuring that it still has control of the land and it has meant that the land has not been developed (which means that the Council has still not realised any financial benefit from the development). In KPMG's view, the Director of Regeneration Enterprise & Planning should have been able to foresee the risk of the Council being exposed to financial loss or liability, and should have mitigated that risk accordingly. Thus, again failure to meet a condition for the exercise of delegated authority, in our view, rendered the decisions taken by that officer further to the delegated powers unlawful.

59. Whilst Cabinet in principle approved the decision to loan up to £12m to NTFC, the Council subsequently entered into loan agreements totalling £13.5m. This happened because NTFC reported to the Council that costs for the stadium development were higher than anticipated and that they needed additional finance. The Council's officers (and especially the then Section 151 Officer) and Cabinet made inadequate attempts to validate this assertion or any impact it might have on the project overall, and instead went ahead and loaned an additional £1.5m to NTFC. It is KPMG's view that although the Cabinet delegated authority to the Chief Executive to "*approve the amounts and terms of any loan…*" this was subject to the overall limit of up to £12m quoted in the report and in our view it is unreasonable to interpret this as being given authority to

approve any size loan. £1.5m extra is a significant increase (a 12.5% increase) and the reasonable course of action should have been to update the Cabinet on the decision as soon as practicable and the extension should have been subject to due governance and Cabinet should have been asked to approve this additional amount. So, in this respect, and notwithstanding the legal advice obtained from LGSS Law (see paragraph 37 above), and the fact that the Council actually lent less than the original £12m stated (i.e. £10.25m), we have concluded that in KPMG's view the Chief Executive exceeded his authority. This, in KPMG's view, rendered the decision to loan the additional funds unlawful.

Regeneration and Planning issues

Conditional sale of land

60. As part of the project, the Council entered into a conditional agreement to sell a large parcel of land adjacent to the Sixfields Stadium to a company (CDNL) which would develop the land for housing. The land comprised two areas: one which had always been owned by the Council (mostly the Athletics track – which NTFC had a long leasehold interest in) and one which the Council purchased from the Homes and Communities Agency (for £1) for the purpose of this project. If it had worked as intended, CDNL would have paid the Council an initial £5m from the proceeds of sale, which the Council would then have applied to reduce the loan balance outstanding from NTFC, with further "overage" payments of 50% of the sales value, if this were to exceed £110m. The officers of the Council believed at the time that this reduction (the £5m) was necessary and normal in such deals to ensure the agreement was financially acceptable to NTFC. We can see no such need for the Council to make such a payment on what was already a very favourable loan to NTFC, and when in fact NTFC had not really been able to demonstrate that it was a viable going concern when it applied for the loan. NTFC's accounts for the years ending June 2009, 2010, 2011 and 2012 all included an emphasis of matter about the existence of a material uncertainty that cast doubt on the company's ability to continue as a going concern - something the Council's due diligence, such as it was, singularly failed to appropriately pick up, report and act upon.

61. The conditions in the agreement were principally related to achievement of a satisfactory planning permission and the timescale in which that was achieved. However, the sale did not proceed because the conditions were not met.

62. The process which councils must follow when they sell land assets are set out in the Local Government Act 1972 section 123. Under case law interpreting this provision, a council/local authority will only have complied with its duties to its residents and protecting the public purse if it has (i) taken proper advice; (ii) followed that advice for reasons that can be justified; and (iii) not followed advice that was so plainly

erroneous that in accepting it the local authority must have known, or at least ought to have known, that it was acting unreasonably. Principal among the requirements is that the Council must achieve best consideration (which can include non-monetary factors). The obvious way of doing this is to go through some kind of competitive process to identify the developer. In this case, the development company was proposed by the officers of NTFC and it would appear that at the time the Council's officers, using their delegated authority, accepted the recommendation without question. In the Cabinet Report of 17 July 2013, reference to 'a developer' was made, however CDNL or its relationship to the owners of NTFC was not. We consider this was inadequate, and the Council's view that this does not matter because the sale did not go through is irrelevant because the Council did enter into a conditional agreement to sell and all the conditions could have been met without resolving this fundamental problem.

63. The company with which the Council entered into the conditional sale agreement was CDNL, whose Directors included David Cardoza and Anthony Cardoza. David Cardoza and Anthony Cardoza were also Directors of NTFC (Barry Hancock, Andrew Clarke, David Jackson and David Linnell were also Directors of NTFC during the period when the loan was negotiated and made) and who therefore stood to gain both through the proceeds of the development (to CDNL) and the £5m from the Council that would be used to reduce the debt owed by NTFC.

Planning approvals

64. The Council continued to advance money to NTFC even when it became clear that something was already fundamentally wrong with this project. Notwithstanding the lack of progress on site, NTFC submitted a revised planning application on 1 August 2014 which significantly reduced the scale of the stadium expansion. By this stage the Council had already advanced £7.5m for the stadium development and it subsequently advanced a further £1.5m on 19 August 2014 despite knowing that the proposed development had changed fundamentally. NTFC's original planning application, submitted in November 2013, was to increase capacity by 2,347 seats and add a conference facility, but their revised application reduced that to just an additional 422 seats and no conference facility.

Governance issues

65. Whilst we have concluded that there were failings by Officers of the Council in their duties, we have also concluded that, in light of the lack of objections raised, most of the then Cabinet Members failed to provide adequate governance.

66. However, the in principle decision to approve the loan to NTFC was a Cabinet decision.

67. All of the then Cabinet Members mentioned above stated that they were not aware that the report they approved (see paragraph 45) contained a provision where it was intended that £5m of Council Taxpayers' loaned money to NTFC was not going to be paid back, and which the LGSS lawyer subsequently referred as "a gift to NTFC". Whilst in terms of their duties, officers should inform Members if there were significant, unlawful or questionable issues, for an issue as significant as this we would expect Members to be more proactive than they were, in asking questions.

68. With regard to the former Leader, it is clear that he drove forward a number of projects that have benefited the Town. In this case however, the outcomes for the Council were poor and the basis for driving this forward insufficient.

69. The Leader led the Council's side of discussions with NTFC and many of these discussions were not minuted and not attended by any other Council representative. This resulted in a series of phone calls, texts and emails (on some occasions from a personal email account) from the former Leader instructing officers to take actions as he negotiated the Council's position. For instance, the project was still being changed significantly by NTFC in the run-up to the Cabinet meeting on 17 July 2013. A draft version of the 17 July 2013 Cabinet report, which was dated 7 July 2013 states that the loan was to be for £10m to NTFC (and £2.5m to the Rugby Club), but this was then changed to up to £12m to NTFC following a meeting between the then Leader of the Council and NTFC (also the loan to the Rugby Club had doubled to £5m by the time the report was finalised). Following our various interviews of Council Members, officers, and review of reports, we have seen no clear evidence to explain why the amount increased or that the Council considered the impact of the increase on, for example, the viability of the project or the security required.

Conclusions

70. We have identified what in KPMG's view are serious failings in the Council's arrangements when deciding to and subsequently making the loan to NTFC. In coming to our view that we should, acting proportionately, issue a public interest report under Schedule 7 of the Act, we have taken into account the NAO's guidance, including the loan made in the context of the Council (for reference, audit materiality for 2015/16 was £2.7m), and the Council's acceptance in discussions with us that its arrangements in relation to the loan fell short of the required standard in a number of respects, and that it has commissioned a complete review of Governance Arrangements in order to address the shortcomings. Whilst the Council has provided written assurances that it would include our report in the public domain on the agenda of its Audit Committee and its Full Council meeting, we consider it should be brought to the attention of the Council and the public by our issuing a public interest report further to our formal statutory powers. As a result, not only does the report itself need

to be publicised but there then needs to be a full Council meeting at which it is considered, and the Council's response also published.

71. In conclusion, this whole episode demonstrates poor decision making based on inadequate reports leading to public money being lost, and demonstrates the need for careful thought, structure, independent advice and monitoring in making such decisions on a transaction which was significant and unusual. There was a near complete lack of an approved business case, appropriate independent advice and documented risk management and proper governance process followed. Documents presented to Members for decision making purposes and records of decisions taken by officers were deficient. This is further demonstrated by the significant time taken by the Council in retrospectively gathering and providing information and evidence to us, which in itself points to inadequate governance, poor risk and poor performance management. Similarly, the fact that thousands of emails and sources of evidence had to be provided to us to attempt to demonstrate proper governance procedures were followed demonstrates the lack of ownership and the lack of an adequate control of the process.

Recommendations

72. Whilst carrying out our review, we have identified areas for improvement in the Council's arrangements, particularly in relation to procedures and practices across the Council. The Council has taken some steps to address a number of these areas already, but we include all recommendations here for completeness. Our recommendations to address these areas are set out in Appendix B. As noted at the start of this report, the Council is required to consider this report at a public meeting within one month, decide what action to take in response and publish a summary of that decision.

KPMG LLP

KPMG LLP

Appendix A

State Aid Analysis

Summary

1. In our view, if all the positive statements in the 17 July 2013 Cabinet Report had been followed up and substantiated/corroborated, a number of State Aid issues would have fallen away e.g. adequate security over the loan (such as by way of legal charges on NTFC's assets); concrete understanding that the loan was repayable in full; and substantiated income projections from NTFC's revenues (due to expansion of their stadium provision etc.) to service the debt. There would also likely have been no failure of the loan arrangements and so no external scrutiny.

2. However, in our view these would still not overcome the legal assessment that the loan was either State Aid or so very close to it so as to warrant an in-depth assessment. The terms of the loan either required amendment to reflect what NTFC would have been able to secure in the commercial market and that it was, in fact, a repayable loan <u>or</u> a robust legal case made out that either the loan would have no distortive effect on intra-EU trade with a purely local impact. There was also the possibility of delaying the loan to ascertain if it could be structured in such a way to fit in with a future European Commission ("EC") exemption for sport infrastructure which was being consulted on at the time.

3. None of these possibilities were pursued despite red flags being raised, particularly about the preferential loan terms and the need for a more in-depth analysis of State Aid issues by LGSS during summer 2013. If NBC did have policy procedures in place to consider State Aid compliance, it seems that not nearly enough time was allocated to it on this occasion. The brief trail of legal advice ends almost as soon as it starts as the lawyers run up against an escalated timeframe to sign the loan agreement.

4. The only other route open to NBC in September 2013 would have been to seek approval from the EC that the loan arrangements constituted lawful State Aid. A case could certainly have been made out for this with a fully worked–up impact assessment regarding the wide benefits which would accrue to the area. This could have covered improved sporting/leisure facilities shared across professional and non-professional clubs and other local sports organisations; public health benefits from increased engagement in sports; regeneration of the Waterside Enterprise Zone; job creation; related sports and other tourism, and monitoring mechanisms for ensuring that the loan was applied for the purposes for which it would be given (and that NBC would be receiving some form of compensation and other tangible benefits such as increased asset values).

5. In our assessment of NBC's actions as set out above, there is an apparent dearth of detail that would be expected and required to make out any of these compliance routes above.

Detailed analysis

6. *Is there State Aid?*

6.1 Re: the initial loan:

6.1.1 There does not seem to have been a competitive process for the various works – this could have dealt with the possibility that the end developer was also benefitting from State resources (flowing down from the original loan to NTFC) and thus that there was State Aid at that level too which likely should have been identified and dealt with adequately. This was flagged by LGSS on 18 September 2013 and would have been a necessary process to avoid the threat of unlawful State Aid and, if the loan had been delayed, for it to benefit as structured from the sport infrastructure exemption introduced in June 2014.

6.1.2 Article 107(1) Treaty on the Functioning of the European Union (TFEU) sets out the criteria for the existence of State Aid which must then either comply with the State Aid rules (e.g. fit into an exemption or aid scheme as authorised by the EC) or be approved individually by the EC before any aid is given. The criteria are cumulative. We paraphrase the criteria in context below as they become relevant.

6.1.3 The loan is without doubt from State resources (a PWLB item sitting on NBC's balance sheet) and confers an economic benefit on NTFC. There are however a number of levels of potential benefit (NTFC, the developers, any concession holders/operators exploiting the funded infrastructure to generate revenue for end users) as the funds flow down. These entities are all involved in 'economic activities' under the State Aid rules. The EC is clear that "exploitation of a sport infrastructure used by a professional sport club" (*Hungary C (2011) 7287*) is economic activity and financing by the State is subject to State Aid controls.

6.1.4 Whether this is "aid" here (a pecuniary advantage of some sort) depends on the terms of the loan. If it was provided by NBC under normal market conditions for example, there would be no element of "aid". The Cabinet Report seems to confirm that the loan is to be repaid in the shortest time possible. However the PWLB interest rate is passed on to NTFC without any added margin and so is considered to be lower than what NTFC could have secured under normal market conditions and so is a preference (or "aid") to a specific organisation(s). Low(er) interest rates can be permissible under the State Aid rules where other terms are adjusted e.g. by reference to workers' wages but there is no indication of that here. Plus, we would not have expected 100% funding to be made available either but up to a percentage of the overall upgrade costs. Amendments to the loan agreement interest rate terms were made very close to signing of the agreement in September 2013 but these were, in our view, very much attempts to mitigate a problem should it arise and would not have been effective to avoid a risk of unlawful State Aid. The Council has also told us that the recitals to the facility agreements included that money will only be provided at PWLB rates if it is lawful to do so, and that the £5m proceeds would only be applied in part satisfaction of the amounts outstanding under the agreement subject to State Aid clearance. The Council's view is that the State Aid risk was therefore covered off in the agreements. However, the inclusion of this wording would not, in our view, render the loan lawful unless the Council did then analyse and ascertain whether it was lawful before providing the loan, which was not the case.

6.1.5 As mentioned above, all elements of State Aid need to be met before it can be determined that there is "State Aid". The key question (from our assessment) is the final criterion as to whether there is any potentially distortive effect on intra-EU trade. The threshold for this has been very low over the decades of State Aid case law (to ensure the efficacy of the regime) however there have been a few more recent cases where purely local "aid" has been held not to have a potentially distortive effect. We understand that NTFC does not (and has not generally) engaged in EU or other international tournaments. Therefore, with some modifications extolling the eventual public benefit and non-selective advantages of a burgeoning sports 'programme' to many sports clubs and organisations in the area (beyond football), NBC might have been able to make out a convincing case that the loan was not State Aid at all as there was no distortion of EU trade. (LGSS did refer to discounting 'aid' in this way in their brief advice note but it seems this option was not pursued.) With enough verifiable substance to this claim, NBC could have properly recorded its considerations and conclusions that the elements of State Aid were not met.

6.1.6 Beyond this, the appropriate consideration is the available exemptions or an individual application to the EC. Whilst sporting interests are promoted within TFEU generally for their social and educational function (Art.165), there are no State Aid sectoral guidelines for sport. LGSS did flag the possibility of a future exemption for investment in sport infrastructure which was being consulted on by the EC in 2013. This exemption was eventually introduced in June 2014 so some time <u>after</u> the loan agreement was signed and so could not have been relied upon ex ante by NBC in September 2013.

6.1.7 NBC could however have bided its time and ensured that the loan did fit within the exemption. However, the exemption is <u>not</u> for aid to individual clubs or non-sports related land development e.g. retail and hotels and so the purpose and scope of the loan and what it would eventually facilitate would have needed to have been expanded significantly. The criteria for the sports' infrastructure investment exemption require 20% usage and access by third parties, application of future receipts back to the State and, crucially, the running of a public procurement process to appoint any developer. There was apparently no subsequent follow-up by NBC (with LGSS for example) to even try to 'retrofit' with the new exemption.

6.1.8 The only other elements of previous exemptions which might have been considered in September 2013 were those relating to employment, training and regional aid. Successful arguments from case law relating to sport infrastructure could also have been considered as part of a direct application to the EC. Our view is that this latter route would have been very difficult to do successfully as the loan was clearly benefitting certain companies (not a non-discriminatory swathe of sporting organisations and clubs in Northampton) and eventual claimed public benefits seemed intangible and far off.

6.2 Re: the £5m applied to NTFC's debt:

6.2.1 The sale of the land adjacent to the Sixfields site did not actually go ahead and therefore no money was applied to reduce NTFC's debt. Thus, from a State Aid perspective no State resources have therefore been used for NTFC's benefit, so no State Aid issues, in the event, arise. The Council has said that this issue is therefore academic and that, as noted above at paragraph 6.1.4, the issue was adequately covered in the facility agreements by the inclusion of wording in the recitals that the £5m was subject to state aid clearance. However, we have seen no evidence to support the view that State Aid was a real concern for NBC.

6.2.2 If the £5m had been applied as outlined, in our view this on the face of it would have run a high risk of being unlawful aid as there seems to be no rational benefit to NBC (and the public purse in general) to reduce NTFC's debt in this way. NTFC was about to (or had already) benefitted from a significant favourable loan from NBC and NBC had yet to reap any of the supposed benefits. This would have been quite simply the application of public funds to pay off the loan of a private company.

6.2.3 Whilst also a moot point if the sale did not proceed, there is doubt that NBC was seeking best value for the land disposal (cf. the NBC Cabinet Report refers to "nominal initial value of the freehold interest"). A sale at an undervalue can also constitute unlawful State Aid to the recipient of the asset if it is purchasing at a lower cost than would be the case in a commercial transaction. Here we would have expected a competitive public auction process or independent financial valuation.

7. *What processes should NBC have followed to assure itself of the potential State Aid angle before the loan was made? What should have happened after?*

7.1 We would have expected to see a fully worked up business case (as is usual for applying for public funds/loans/grants etc.) and a detailed economic impact assessment (including some form of adequate benchmarking to limit any perceived advantages to NTFC). Finally we would have expected NBC to seek a targeted, independent legal opinion on the State Aid aspects including risk assessments of the various options for forms of the loan. Then we would have expected NBC to come up with a State Aid compliant solution.

7.2 In terms of post-loan monitoring, we would have expected to see a robust, frequent monitoring mechanism in place to keep tabs on compliance with the terms of the loan or cross-subsidisation. Given the value in this case dispensed at a local level, and the possibility that the loan might take over 10 years to pay back, we would expect significant monitoring by NBC lasting the entire duration of the loan facility. There is no apparent 'higher public authority' involvement in the arrangement of this loan. We would have expected this particularly if it had been determined this was State Aid with back-to-back monitoring at all levels of benefit (NTFC, the developers, any other corporate beneficiaries).

7.3 We would also expect there to be transparent, separate accounts; details of the loan on both NBC's and NTFC's websites and details as to planned usage for public benefit and not its exclusive use e.g. making the stadium available to local schools for sports purposes or to the local community more widely for non-sport purposes. Beneficiaries of State resources should be incentivised to make available realistic plans as to what they are using the funds towards, addressing real and well-researched needs.

Appendix B

Recommendations

Recommendation	Response
Recommendation 1 – Closing Cabinet Actions For the purposes of transparency and openness further approval should be sought from Cabinet for any additional monies, or any variations in the loan value that are subsequently agreed in respect of any loan decisions. In respect of concerns raised by Members, good governance practice would determine that these should be recorded as issues to be addressed by management. The outcome of these investigations should be supplied to Members at the following meeting to provide assurance that the concerns have been suitably addressed.	**Response and Due date for implementation**
Recommendation 2 – Completion of Delegated Conditions As part of good governance practice, the Cabinet should ensure that where conditions are placed on those with delegated powers, that there is a reporting mechanism in place whereby the results of the work undertaken by these individuals, including any results of further investigations, or decisions taken, is summarised in a report back to Cabinet to provide assurance that their requirements have been discharged.	**Response and Due date for implementation**
Recommendation 3 – Provision of Business Cases for External Loans Where Cabinet are required to make any future loan decisions, they should do so following receipt of a detailed business plan, which is accompanied by full due diligence, to support the decision-making process. This should include a clear and independent assessment of whether the work to be undertaken will cost the amount to be loaned. Additionally, any profiles of future income projections should also have been challenged and agreed, prior to being presented to Members.	**Response and Due date for implementation**

Recommendation	Response
Recommendation 4 – Depth of Due Diligence Reports to Cabinet for key decisions, should clearly include the results of the due diligence that has been undertaken by management, prior to the decision being undertaken. No activities of these significance should be delivered by senior officers in the name of Cabinet or Council, without the results of these activities being clearly reported to members. Where any future complex loan agreement includes the potential to receive monies back from say development or other activities associated with the loan agreement, this should be clearly reported to Cabinet or Council, to ensure that there is full disclosure of the arrangements to be put in place, thereby ensuring that the decision taken by Members is based on all available evidence concerning public funds. Any changes in the value or use of public funds should be reported back to Cabinet for transparency purposes.	**Response and Due date for implementation**
Recommendation 5 – Evidencing Decisions Taken Where legal or other professional advice is received, it would be both prudent and transparent for senior managers to produce a report containing the recommendations made by these advisers and how each recommendation has been assessed by the Council and how it has, or has not impacted on the final decision made. This report should sit above any supporting evidence via emails or minutes of meetings / conference calls.	**Response and Due date for implementation**

Recommendation	Response
Recommendation 6 – Reporting the Outcomes of Due Diligence The Council should prepare a summary report which concludes on the due diligence review undertaken into the finances, structure and ownership of any organisation it is intending on supporting with loan finance. The purpose of the report would be to discharge the duties of those given delegated authority and for transparency purposes the report should be presented to Cabinet. This should support the report prepared on any legal advice / recommendations that have been received.	**Response and Due date for implementation**
Recommendation 7 – Timeliness of Due Diligence Checks As part of entering into any key contract or business loan, the Council should undertake a thorough assessment of the personal / business interests of those charged with running the organisations, as well as completing due diligence on the finances of the organisation as a whole (see recommendation 6 above). These checks should be completed prior to any decision making and the results should be incorporated within the Council's business case. Where there are additional third parties, such as developers or contactors which will be employed by the loan recipient, the Council should include either its own due diligence on these additional organisations, or request the outcome of the loan recipient's due diligence, alongside the evidence of competitive tender to support a transparent approach to appointment.	**Response and Due date for implementation**
Recommendation 8 – Pressures within the sign off process The Council should ensure that officers are aware that if new information comes to light before or after a Member decision, that it may be appropriate to pause a process in order to seek further guidance.	**Response and Due date for implementation**

Recommendation	Response
Recommendation 9 – Overall Governance Process and link to Constitution The Council should review the procedures and guidance available to officers when considering the information to be provided to Cabinet and/or Committees in respect of loans made to third parties. This should include a clear stage by stage process, whereby evidence / reports should be prepared, reviewed and formally approved, and prior to moving to the next stage. Additionally, once the loan has been awarded there should be a transparent process for monitoring the recipient organisation and obtaining evidence to support that the loan is being used for the appropriate purpose. Periodic reports should be made to Council / Cabinet to summarise progress by the recipient. If at any point the recipient is not able to demonstrate progress, then no further payments should be made.	**Response and Due date for implementation**
Recommendation 10 – Sale of Land for Development Any future land sales should, other than in exceptional circumstances and where the law allows, be undertaken via means of a competitive process, in order that prospective parties are able to tender for the purchase, by submitting their plans for development. Each bid should be appropriately appraised, and consideration should be given to any relationships either with Council Members or related parties as part of the awarding process. The ultimate decision on who to award the sale to, should in a matter of this significance be undertaken by Cabinet following receipt of a formal tender evaluation process, which includes the results of the due diligence undertaken against each bid. When considering best value for the land, the Council may (in limited circumstances and subject to the particular facts) be able to take into account ethical considerations.	**Response and Due date for implementation**