



Report to:	Sutton Shareholdings Board	Date:	22 February 2017
Report title:	Task and Finish Group: Review of LBS Companies - Governance Arrangements		
Report from:	Jessica Crowe, Monitoring Officer		
Ward/Areas affected:	Borough Wide		
Chair of Committee/Lead Member:	Councillor Simon Wales, Chair		
Author(s)/Contact Number(s):	Fiona Bywaters, Head of Committee and Management Support (Interim), 0208 770 5122		
Corporate Plan Priorities:	<ul style="list-style-type: none"> • An Open Council 		
Open/Exempt:	Open		
Signed:		Date:	08 February 2018

1. Summary

- 1.1 This report details the need for a Task and Finish Group to undertake a review of the governance arrangements of London Borough of Sutton companies where the Council is a shareholder. The Task and Finish Group will need to develop a draft Code of Practice for the governance of council interests in companies for approval by the Sutton Shareholdings Board.

2. Recommendations

The Sutton Shareholdings Board is recommended to:

- 2.1 Agree to establish a Task and Finish Group to review the governance arrangements of London Borough of Sutton companies where the Council is a shareholder and draft a Code of Practice for the governance of council interests in companies.
- 2.2 Agree that the Task and Finish Group will meet on 2 to 3 occasions between 23 February 2018 and 20 April 2018.
- 2.3 Agree that the Task and Finish Group reports its outcomes to a future meeting of the Sutton Shareholdings Board.

3. Background

- 3.1 The Council's innovative approach to establishing new delivery models pre-dates austerity. Sutton formed a unique community safety partnership in 2006, set up an Arms-Length Management Organisation in 2007 and began the development of a shared HR service in 2008/9. All of these projects helped save money and improve services. However, following the publication of a new policy direction, Putting Residents First, in 2012, our development of new delivery models increased significantly.
- 3.2 The Council now has over 20 shared arrangements (saving approximately £10m), with a number of public sector partners, and has seen other entities set up as the result of staff spin outs. As opportunities were identified to develop entirely new strands of activity for the Council, such as energy supply or house-building on a commercial basis, Council-owned companies have been established as the best vehicles for delivering these. An increase has also been seen in income generated by internal services trading with other agencies. This has been achieved by training staff specifically in project management techniques that facilitate new delivery models and through the agreement of the Strategy and Resources Committee in October 2014 to a staff offer to support employees seeking to deliver their services in different ways. Additional funding has also been secured to support this approach at reduced cost to the authority, through the Mutual Support Programme (Cabinet Office) and the Transformation Challenge Award (Department for Communities and Local Government).
- 3.3 Having taken an iterative approach to facilitate innovation and seize opportunities as they arise, the time is now right to take stock of the Council's overall approach to and governance of new delivery models. The proposed task and finish group is to look specifically at the governance arrangements of any wholly or partly owned private limited companies formed by the Council. To date six such companies have been registered with Companies House.

4. Impacts and Implications

- 4.1 It is recognised that each company is a separate legal entity which needs to succeed on its own terms and be competitive within its market. However, each company must also succeed on the Council's terms, mindful of the expenditure of public money in their creation and the stewardship of public resources. In order for the companies to be commercially successful, an appropriate balance needs to be achieved between these demands.
- 4.2 As the majority of the companies are now operational, work has recently been undertaken by Officers to review the options for the ongoing governance of the Council's interests in these companies and how best to monitor their performance and operation in the most efficient and effective way. It is recommended that the task and finish group continue this work with the aim of drafting a Code of Practice for the Governance of Council Interests in Companies, to be adopted by the Sutton Shareholdings Board.
- 4.3 The Code should serve as guidance to members, officers, company representatives and other interested parties in understanding the requirements of the Council when establishing a local authority company and how the associated governance arrangements are expected to work. It

would likely be formed of two parts: overarching guiding principles and a set of working expectations.

Guiding Principles

- 4.4 It is suggested that the meetings of the task and finish group are themed around the following proposed guiding principles:

Controls and Freedoms

- 4.5 A trading company must be afforded commercial freedoms to enable it to be successful, but it is appreciated that this should not be unfettered. Governance arrangements should seek to ensure that the company is provided with sufficient freedoms to achieve its objectives while the council, as shareholder, retains sufficient controls over strategy, key decisions and business activity to ensure that its investment is protected. It is important that the appropriate social and financial returns on investment are obtained and that trading activities are conducted in accordance with the Council's values.

Relationship, Integrity and Accountability

- 4.6 While trading companies can operate on an equal footing with their competitors, it is important that the Council, as shareholder, can carry out its functions as an investor, as a trustee of public funds and as a local authority committed to the proper exercise of its functions. Comprehensive governance arrangements should seek to ensure that the Sutton Shareholdings Board can:

- Make investment decisions based upon a complete and accurate consideration of business plans; and
- Evaluate social and financial benefits and returns on the public investment.

- 4.7 These arrangements must also take into account mechanisms of scrutiny available under the Council Constitution, whether that be by consideration at the Scrutiny or Audit and Governance Committee or by requisition to Full Council.

- 4.8 The companies should be able to provide the Sutton Shareholdings Board with comprehensive financial and business reporting against their business plans and be open to an appropriate level of scrutiny, without fear of commercial confidentiality being breached. This places obligations on Members of the Sutton Shareholdings Board to operate as shareholders in the interests of the company as well as the Council.

Understanding of Role

- 4.9 A trading company is a separate legal entity from the local authority and subject to the Companies Acts. Its directors and officers derive their authority from the articles of association and company law. They are answerable to the company and must act in the company's interests. Local authority members and officers must be aware of potential conflicts of interest when carrying out their roles for the authority, or when acting as a director of a trading company.

The success and good governance of the company depends upon those involved understanding their role and responsibilities, both collectively and individually.

- 4.10 Governance arrangements should seek to ensure that there is sufficient induction and training available to members acting in the role of shareholder representative as well as officers of the Council acting as company directors. Development must focus on legal duties, the stewardship of assets, provisions of any governing document, the external environment and the structure of the organisation. The organisation of a member development session on the role of the shareholder will be taken into account when developing the core induction programme in 2018, following the local elections.

Working Expectations

- 4.11 The working expectations to be covered in the Code are wide-ranging in their implementation of the guiding principles. The task and finish group may wish to cover the following topics, among others, when meeting:

- Separation of Strategic Direction and Contract Management: At present, contract and client management arrangements vary among the LBS companies. Where senior council officers are appointed as company directors, particularly where a relationship of reverse accountability to the Council exists, this could lead to a potential conflict of interest were the client in some way dissatisfied with contract performance.
- Appointment of Directors: What are the Council's expectations in the recruitment and conduct of directors? In 2015, the Sutton Shareholdings Board was recommended to appoint further expert non-executive directors to both Opportunity Sutton Limited and its subsidiaries as the business developed and evolved. Two years later, as commercial activity increases further, the group may wish to consider whether the need for further NED appointments be reviewed across all Council companies.
- Procurement: The group may wish to seek specialist legal advice as to the Teckal implications of changing company governance arrangements, as well as the implications of LATCs using the London Tenders Portal and any access to wider local authority framework contracts or arrangements. The group might wish to consider the interaction of the Council's contract standing orders with LATC internal governance mechanisms.
- Provision of Support Services: The authority as shareholder needs to be assured that there are effective and robust support services in place in certain areas. This is to satisfy itself that sufficient standards of operational and corporate governance compliance and effective financial management within the company are adhered to.
- Interaction of local authority governance requirements: In considering the Shareholdings Board's terms of reference, the group may wish to revisit the issue of composition of the board and whether it may benefit from co-opted expert members. An appropriate mechanism might also be considered for shareholder decision-making outside the committee cycle due to the difference in pace between commercial and committee decision-making.

- The advantages and disadvantages of adopting a group approach: Where local authorities have created commercial vehicles as and when required in response to different needs, there comes a point at which it may be wise to rationalise these arrangements.

5. Impacts and Implications

Financial

- 5.1 There are no direct financial implications as a result of this report as the proposed review will be carried out within existing resources but it is important to be mindful of the following:-
- 5.2 All companies retain a financial risk linked to their performance. Being a public sector owned business does not alter this risk and it should be therefore be recognised that, as with any commercial activity, there is an opportunity to make a financial gain or loss. Good governance is a key element to ensuring the success of a company and mitigate financial risk.
- 5.3 The adoption of a more commercial approach provides the authority an opportunity to generate additional savings/revenue to support the delivery of public services as part of its programme to manage the reduction in financial resources available.

Legal

- 5.4 There are no specific legal implications arising out of this report though the following comments are made in relation to its contents:
- 5.5 As the Local Authority Trading Companies are separate legal entities which are independent, this needs be recognised and maintained in the language used and governance arrangements between Council and Company.
- 5.6 With regards conflicts of interest these may be potential or actual conflicts and the nature of the conflict will dictate as to the action to be taken by those finding themselves in that position.
- 5.7 When considering a group approach with regards the existing companies, such an approach does has its advantages, especially in relation to VAT grouping. A group approach will enable a consistent approach in the relationship between the Council as shareholder and all the companies it has created. However, as there are “Teckal” companies (Regulation 12(1) of the Public Contract Regulations 2015) that may be part of a proposed group, attention will have to be paid with regards the Reserved Matters contained in a shareholders agreement between the Council and the parent company to ensure that the control element required to take advantage of the Teckal exemption is preserved.
- 5.8 Generally, with regards companies that are “Teckal” compliant, any changes to governance arrangements will need to ensure this does not impact on the exemption, especially in relation to the control test contained in Regulation 12(1)(a).



6. Appendices and Background Documents

Appendix letter	Title
None	

Background documents
None

Audit Trail		
Version	Final	Date: 08 February 2018
Consultation with other officers		
Finance		
Legal		
Equality Impact Assessment required?	No	N/A