



LOCAL PARTNERSHIPS

Appendix 4(a)



LOCAL AUTHORITY COMPANY REVIEW GUIDANCE

A toolkit for undertaking strategic and governance reviews
of wholly or partly owned council commercial entities



1 FOREWORD



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Why is this guidance needed?

Being a director of a local authority controlled company requires officers and elected members appointed to those roles to operate in a completely different legal and philosophical framework to that they are used to inside their local authority.

It can lead to real conflicts between the duty owed to the company and the interests of your council. It can also lead to conflicts of interest on a personal level which makes holding some roles in a local authority unviable whilst continuing as a director. It is necessary to make different assumptions about how things operate and what issues you need to have demonstrated you took into account, and what had no influence.

When I first took over as the chair of a company, jointly owned by two London boroughs, I was surprised by the amount of time we spent considering cash flow, with profitability being a second order issue. I had never had such a conversation inside my authority because cash flow is never an issue.

Too often, this is not understood until problems arise, resulting in reputational and financial damage and in some cases, external intervention directly impacting on your authority.

In some of the examples I have seen, it is not very clear why a company structure was chosen for the activity in the first instance as the council involved was not prepared to allow its company to exercise any of the freedoms that the structure would allow. In other examples, there were no controls at all.

In the right circumstances, using a company structure can facilitate change or outcomes that would be very difficult to deliver in a timely way under the constraints of a council's constitution, but it needs to be clear why that is.

In the report of the rapid review of Nottingham City Council, which I led in 2020, it was recommended that guidance was commissioned to aid local authorities in this area. Following the approach set out in this guidance and toolkit will help us all avoid the obvious traps.

In this guidance document



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2 INTRODUCTION

2.1 Background

Many councils have established wholly or partly-owned companies, covering a diverse range of offerings. These include selling services to other public bodies, providing leisure or cultural facilities or establishing vehicles to manage or invest in revenue generating assets such as affordable housing or commercial property.

Some of these companies have been successful, generating a healthy return on investment and delivering recognised benefits and positive outcomes. Others have generated negative headlines for the wrong reasons.

Whether successful or not, many councils have seen the need to review their companies. In some cases, councils seek assurance that the governance structures and processes for managing risk are sufficiently robust. Other local authorities want assurance that the entities are meeting councils' expectations, delivering real benefits, and providing value for money.

This desire to review entities has recently escalated in part due to the COVID-19 pandemic which has revealed areas where councils are exposed to significant risk.

We have also witnessed several well-publicised issues with company governance at a number of councils, with the Government making direct interventions, rapid reviews and best value inspections, some of which are highlighted as case studies in Section 7.



...a tool to help councils ensure that they strike an appropriate balance between allowing a company the freedom to manage its activities and ensuring that it is accountable for its actions.

2.2 Purpose

As this guidance is primarily aimed at reviews of *existing* council owned companies, the first sections focus on the effectiveness and appropriateness of governance arrangements that are critical so that the companies may be held to account and to protect the interests of taxpayers.

Sections 3 and 4 of this guidance provide a best practice checklist of issues to consider while conducting governance reviews. Section 3 focuses on councils' governance arrangements for overseeing wholly or partly owned entities and holding them to account.

Section 4 focuses on the establishment of effective governance arrangements for the entities themselves.

Section 5 has been included for context, and sets out the questions and challenges that we believe are relevant to the decision-making processes for establishing wholly or partly owned entities; why is establishing a company the right approach and would an alternative delivery model be more appropriate? It provides guidance as well as questions and issues to address as part of the process to plan and approve the establishment of a commercial entity.

This guidance can be used as a tool to help councils ensure that they strike an appropriate balance between allowing a company the freedom to manage its activities and ensuring that it is accountable for its actions.

A summary of evidence and an accompanying action sheet is provided in Section 8.



3 COUNCIL GOVERNANCE ARRANGEMENTS

3.1 Introduction

This section provides a best practice checklist of issues to be considered when reviewing of wholly or partly owned entities, focusing on councils' governance arrangements for overseeing the entities and holding them to account.

3.2 Governance aims

Good corporate governance requires councils to carry out their functions in a way that demonstrates accountability, transparency, effectiveness, value, integrity, and inclusivity.

The Governance arrangements for council owned entities should seek to ensure that:

- ▶ the entity should have sufficient freedoms to achieve its objectives
- ▶ the council should have sufficient control to ensure that its investment is protected, appropriate returns on investment can be obtained and that the activities of the entity are aligned with the values and strategic objectives of the council
- ▶ the entity continues to be relevant and required (in its existing form) and if not, appropriate steps are taken (for example, amending constitutional documents or changing form or terminating the vehicle)

Any so-called "Teckal"¹ companies should remain compliant with relevant exemption requirements under EU procurement law.

¹ The case of *Teckal Srl v Comune di Viano and Azienda Gas-Acqua Consorziale (AGAC) di Reggio Emilia (Case C-107/98) [1999] ECR I-8121* established how a contracting authority could procure direct from an external company in which it has control similar to that it exerts over its own departments. Subject to meeting certain criteria (Reg12 of the Public Contracts Regulations 2015), procurement would be outside rules regulating public contracts.



The audit report on Nottingham City Council's arrangements relating to its company, Robin Hood Energy, stresses the need to ensure that **"sufficient checks and balances are in place and in particular that risks are appropriately recognised and managed, that there is an effective scrutiny function and that challenge of political priorities by both members and officers is seen as a positive"** and provides an important message that all councils establishing commercial entities should be cognisant of the risk of what is referred to as **"institutional blindness"** whereby effective governance arrangements are overshadowed by a council's determination that the company should be a success.

Generally, although not in all cases, it would be expected that an entity which is a trading company will have more autonomy than a Teckal company. Also, the amount of autonomy will depend on the size and scale of the business, the board make up, the size of any debt owed to the council or wider dependency on public sector loans or grants.



EVIDENCE

- C1 There should be evidence that the council and senior management recognise the importance of establishing appropriate and proportionate governance arrangements for the oversight of entities
- C2 There should be evidence of a culture of challenge and clarity relating to the purpose, efficiency, effectiveness, specific objectives, and freedoms of the entity

3.3 The council's shareholder role

The council must have a designated "shareholder" to represent its ownership of the entity. The process for appointing a shareholder needs to be set out in the council's constitution which should also detail how the shareholder reports on the exercise of delegated powers.



The shareholder may also have responsibility for liaison between the council and the entity and for access to information, although this role may also be vested in a distinct “contract officer” role.

The council may require that certain decisions of the shareholder (within the council’s typical levels of materiality and thresholds in its schemes of delegation) require ratification by the Section 151 Officer and/or Monitoring Officer.

Councils may decide to delegate the shareholder function to a shareholder committee or board of the council or to the executive rather than to a designated individual.

The role of the shareholder should be to provide:

- ▶ oversight of any decisions that can only be made by the shareholder, rather than left to the entity (known as “reserved matters”). These may cover areas such as approval of annual business plan, key appointments, setting up subsidiaries, borrowing money, giving guarantees or winding up
- ▶ a mechanism to review the implementation and development of the council’s commercial approach through the entities it influences and owns
- ▶ the necessary oversight from a shareholder’s perspective that the parameters, policies and boundaries that the council has established are being adhered to
- ▶ an articulation of what success looks like in terms of achieving social outcomes and/or a return on investment
- ▶ effective and systematic engagement between the Chair/CEO and shareholder role to assure effective performance against strategy and governance
- ▶ a mechanism to communicate the shareholder’s views to the entity
- ▶ a means to evaluate the effectiveness of the company board and the delivery of the company performance against strategic objectives and the business plan
- ▶ a regular review of whether the entity provides the most effective vehicle to deliver the outcomes it requires and whether there are viable alternative models which might offer a more effective means of delivering its priorities
- ▶ a holistic review of risk to the council offered by all active entities

Shareholders or their designated representatives may attend company board meetings as observers, but they should not be there as board members.

An up-to-date shareholder's agreement should describe the powers of the board of the entity and how and when the shareholder might influence those powers. This can help demonstrate the required level of council control over any Teckal companies. For trading and investment companies, it can lay out how the entity is independent from the council to ensure it is not treated as a public sector entity.

If the council is the sole shareholder, a formal shareholder's agreement may not necessarily be required. However, it is good practice to document such an agreement to ensure that there is no doubt about the powers of a company board to take decisions without the approval of the shareholder. It is also important to prevent unwarranted interference by council officers or members in the entity's affairs.

EVIDENCE



- C3 There should be a clearly designated council shareholder role or function which is both understood and recognised by the council and the entity (and documented in terms of reference)
- C4 There should be clarity regarding the role of shareholder, with reserved matters clearly documented and updated as required, reflecting any changes made as the entity has developed, in a shareholder's agreement, or as set out in the company's governing articles of association
- C5 There should be evidence that the individual undertaking the shareholder role is provided with suitable training and support commensurate with the role
- C6 There should be evidence of formal periodic shareholder/ Chair/CEO meetings with effective supporting papers to inform subsequent company board meetings

3.4 Council oversight, scrutiny, and governance framework

The council should have a clear, systematic framework which underpins arrangements for overseeing, interfacing, and engaging with entities to ensure its interests are safeguarded.

The framework should be underpinned by clear governance principles, such as keeping the role of shareholder separate from that of the board and applying arrangements in a similar legal model, by using standard articles of association or shareholder's agreements so that the overall approach is standardised.

The council should regularly undertake an objective assessment of how successfully each entity supports its policies and strategies.

The council should regularly review risks relating to its entities and establish whether they are effectively managed and scrutinised. Different types of entities will be exposed to different risks. For example, development/asset-based companies will be constrained by any changes to council borrowing powers, whereas service-based companies will potentially be impacted by Teckal constraints around growth.

The council's approach to governance should be determined by whether it wholly or partly owns several distinct entities or whether it funnels its interests through a holding company. A group structure may provide a single point of focus for managing the council's commercial activity and an effective use of resources.

For councils with a cabinet system, the council should establish a company management committee which should be a sub-committee of cabinet to look at the totality of a council's holdings and the decisions of that body should be subject to scrutiny.

The council may also want its overview and scrutiny committee (or equivalent) to provide overview, pre-decision scrutiny and call-in of decisions regarding the council's shareholding interest in its entities.

The council may wish to programme formal oversight and scrutiny reviews which focus on whether the financial and social objectives of the entity are being delivered.

One of the roles of the council's audit committee should be to pay specific attention to how the integration of the various external auditors across all its entities is achieved.

The council should ensure, for the sake of openness and transparency, that reviews of entities by committee or executive can be viewed by the public where feasible.



EVIDENCE

- C7 There should be documented evidence of transparent member and officer scrutiny, oversight, and approval of business plans
- C8 There should be evidence of a clear set of KPIs that fall out of the business planning process
- C9 There should be evidence that senior company staff are performance managed against KPIs
- C10 There should be evidence of ongoing assessment of value-for-money and quality offered by the entity through an adequately resourced monitoring function
- C11 There should be ongoing assessment of risks relating to the entity, supported by processes to ensure that risks are managed as part of the council's overall risk management approach, with appropriate escalation and reporting
- C12 There should be evidence of a consistent approach across the council when it comes to engaging with its entities
- C13 The council should have clear and unfettered access to audited accounts for its entities

3.5 Business case for the entity

The council should have a clear understanding of what it wanted to achieve by establishing an entity and be able to articulate clearly what success looks like in terms of achieving social outcomes and/or a return on investment.

Form should follow function; the model adopted should derive from its intended purpose, not the other way round.

The decision-making process should have been informed by the development of a detailed business case, ideally using the HM Treasury five-case model, based on the Government's green book².

The business case should have been produced prior to the establishment of the entity and have set out the rationale, enabling stakeholders to review and challenge the establishment of the entity.

² **The Green Book** is issued by HM Treasury on how to appraise policies, programmes and projects. It also provides guidance on the design and use of monitoring and evaluation before, during and after implementation.

The business case should cover:

- ▶ a clear strategic case which identifies direct and indirect benefits
- ▶ a rigorous appraisal of the options available for delivering the service or desired outcomes
- ▶ the objectives of the entity
- ▶ the expected financial results of the company, together with any other relevant outcomes that the business is expected to achieve
- ▶ the investment and resources required to deliver the objectives of the entity
- ▶ any risks involved
- ▶ other important legal, commercial and financial considerations for setting up a company including company law issues; the cost of bidding for contracts; tax liability (corporation tax and VAT); procurement law and state aid/subsidy rules and employment law (TUPE and pensions)

Market conditions and changes will affect commercial activity and therefore assumptions underpinning the activities of an entity may need to be revised over time.

Once set up, councils should continually re-assess the business case and challenge the ongoing existence and relevance of their entities and review the extent to which their objectives remain relevant over their lifetimes.

EVIDENCE



C14 It should be possible to review the business case which assessed the risk involved in establishing the entity and recommended its establishment, taking account of other potential delivery models

C15 Objectives of the entity should be clearly defined and documented, and regularly reviewed to ensure that its operation continues to support council policy and strategy, including periodically reviewing the business case to ensure it is still valid

3.6 Agreements with the entity

The council should have commercial agreements which set out any assistance provided to the entity and the terms for that assistance, such as a loan or a parent guarantee.

The terms of any support provided to the entity in the form of goods, services or staff should be captured in appropriate legal agreements.

Where there is a service contract between a council and an entity, contract management arrangements should be established and may include a joint liaison committee to review issues (relating to performance, disputes, or changes in the relationship, for example).

Additional agreements should be established as required, including data protection and information sharing protocols.

EVIDENCE



- C16 Agreements should be documented between the council and the entity for any support or services provided by either party to the other party
- C17 All agreements should be clear, up-to-date, and regularly monitored and reviewed, with any changes to agreements documented so that a clear audit trail exists

3.7 Avoiding and managing conflicts of interest

Local authority members and officers should be aware of potential conflicts of interest when carrying out their roles for their authorities, or when acting as directors of trading companies.

Council officers and members also have fiduciary duties to the council. Situations can inevitably arise where the same person will be a decision maker or advisor both for the council and one of its entities. Examples of this include matters of reporting, contractual discussions, investment requests or resourcing agreements.



When acting as director of the entity, a council officer or member is obliged to act in the best interests of the entity. As the [Institute of Directors' Corporate Governance Guidance and Principles](#) states **"an important principle of company law is that directors have a duty to promote the success of the company as a whole. They are specifically prohibited from directing the activities of the company in favour of themselves or particular shareholders and/or stakeholders"**.

If there is a risk of a conflict of interest, the officer or member should not act for both the council and the entity unless they agree that they are both seeking the same common objective.

Conflicts of interest can arise in a wide variety of ways. The council should use its internal and external audit functions to regularly review the governance arrangements relating all of its entities to ensure that potential conflicts do not arise.

Examples of areas where conflicts can arise include:

- ▶ individuals acting as representative for both the entity and the council. For example, given that it is likely that certain decisions of the shareholder will require ratification by the Section 151 officer, it is not considered good practice for a Section 151 officer to hold a position with a council owned entity
- ▶ holding a council role which involves potential oversight and scrutiny of the entity, while also holding a position with the entity. For example, an entity board member who also holds a position on the council's audit committee would clearly be conflicted
- ▶ holding a position as a company board member while having private financial or non-financial interests which may conflict or may be perceived to conflict with the role. For example a company board member, or member of the family, having an interest in a supplier or competitor to the company
- ▶ board members receiving benefit (such as gifts and hospitality) from third parties (such as potential suppliers to the company)
- ▶ the exploitation by a board member of any asset, information or opportunity related to the entity

Officers and members who hold roles with the entity must declare any interest they have in a proposed transaction in advance of the transaction being entered into. The declaration of an interest in an existing transaction must be declared as soon as reasonably practicable.

The council should have a formal policy to deal with conflicts.

All potential conflicts of interest should be referred to the council's Monitoring Officer for a decision about whether a conflict exists.

In the event of a conflict of interest, the Monitoring Officer should operate an "ethical wall" policy, whereby an information barrier is erected to prevent communication that could lead to the disclosure of information which is confidential to one organisation or the other.

Officers and members should report back to the council on their involvement in outside entities to which they have been nominated by the council.

This should involve making themselves available for council scrutiny committees and other council governance forums which oversee the entity (although they should not be obliged to disclose commercially confidential information about the entity).

EVIDENCE



- C18 There should be evidence that a culture exists whereby actual or potential conflicts of interests are identified, declared, and acted upon, including evidence of appropriate training across the organisation
- C19 The council should have clear and up-to-date policies and processes to consistently manage actual conflicts or potential conflicts of interest, including a clear process for investigations and procedures for appropriate disciplinary actions in the event of breaches
- C20 The roles, responsibilities and reporting lines of officers and members who are involved in council oversight of the entities, the provision of services between the entities or the running of the entities should be clearly defined and documented

3.8 Council appointments to the board

The council should carefully consider nominations to the board, taking account of:

- ▶ the benefits of appointing independent directors to the entity
- ▶ the need to avoid council members and officers also being appointed to senior positions in the company, if such an eventuality is likely to lead to a conflict of interest

Potential appointees to the board should complete declaration of interest forms.

Appointments to the board should relate to the relevant post or office of the council, not to a specific individual. It follows that, if a council appointed director ceases to be an employee or office holder of the council, then they should automatically no longer be able to hold board membership.

The process for the appointment and renewal of directors should be set out in the articles of association, which should state those appointments which are wholly reserved to the council. For those appointments which are not reserved to the council, the company may establish a remuneration committee to make appointments and remuneration decisions and recommendations to the council.

Appointments should be based on a review of the skills, qualifications, diversity, and other attributes required for the role.

Where a board member is eligible for renewal and reappointment, this should be subject to considering their performance to date and skills, and the needs of the board.

EVIDENCE



- C21 There should be evidence that appointments to the board are subject to a documented formal, rigorous, and transparent procedure based on merit and published objective criteria which also promote diversity



4 ENTITY GOVERNANCE ARRANGEMENTS

4.1 Introduction

This section provides a best practice checklist of issues to be considered when reviewing a wholly or partly owned entity, focusing on governance arrangements for the entity itself.

4.2 Articles of association

The entity should have articles of association, documenting its constitution and addressing purpose, conduct of meetings and appointment of directors³.

For the purposes of applying the relevant exemption under procurement law, the articles for a Teckal company should be consistent with the need to demonstrate that:

- ▶ the council exercises over the company a control, similar to that which it exercises over its own departments
- ▶ more than 80% of the activities of the company are carried out in the performance of tasks entrusted to it by the controlling council or by other legal persons controlled by that council
- ▶ there is no direct private capital participation in the company⁴

EVIDENCE



E1 The entity's articles of association should be clear, up-to-date, and reflective of how the entity is run

³ See under "Starting a company" at www.gov.uk/government/organisations/companies-house for model articles

⁴ Regulation 12(1), Public Contracts Regulations 2015 www.legislation.gov.uk/uksi/2015/102/contents/made

4.3 Business planning

The entity should have an annual business plan which sets out its objectives and how the objectives are to be resourced and achieved. Key areas of focus should include:

- ▶ a description of the core offering and articulation of potential future services and/or innovations
- ▶ strategy and implementation; a description of the value proposition, underpinned by effective marketing, communications, and branding strategies
- ▶ financial break-even analysis, projected surplus or deficit, cash flow, balance sheet and reliance on trading income
- ▶ operations and management; an analysis of the entity's capacity and capabilities to fulfil its purpose, in terms of commercial skills, workforce planning, board development, support services, managing the supply chain and clients
- ▶ market analysis and a description of market trends and competitors

Requirements to meet the legal criteria in relation to any Teckal companies should also be reflected in the business plan.

EVIDENCE



- E2 There should be evidence of an up-to-date business plan that is reflective of the current circumstances and environment in which the entity operates

4.4 Role and behaviours of the board

The board should operate openly and transparently. According to the Cadbury Report⁵ **“the basic procedural requirements are that the board should meet regularly, with due notice of the issues to be discussed supported by the necessary paperwork, and should record its conclusions”**.

Meetings on at least a quarterly basis would be considered good practice.

⁵ The Financial Aspects of Corporate Governance – “The Cadbury Report”



The Cadbury Report states that **“the responsibilities of the board include setting the company’s strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship”**.

The Higgs Review⁶ suggests that the role of the board includes:

- ▶ promoting the success of the company by directing and supervising the company’s affairs
- ▶ providing entrepreneurial leadership within prudent and effective controls where risk is assessed and managed
- ▶ setting strategic aims and ensuring sufficient resources (financial and human) are available to meet objectives
- ▶ reviewing management performance
- ▶ setting corporate values and standards
- ▶ ensuring obligations to shareholders and others are met

The board should have processes to ensure that the entity continues to be financially viable, supported by the role of internal audit and its external auditor.

Larger entities or holding companies should have:

- ▶ an audit committee to provide independent scrutiny, challenge, and assurance
- ▶ a remuneration committee, which will manage appointments and remuneration decisions (where an appointment is not reserved to the council)

The board should ensure processes are in place to confirm how financial issues are to be dealt with including business planning, budget control, financial systems and financial monitoring and reporting.

The Cadbury Report recommends that boards should **“recognise the importance of the finance function by making it the designated responsibility of a director, who should be a signatory to the accounts on behalf of the board and should have access to the audit committee”**.

⁶ Review of the Role and Effectiveness of Non-Executive Directors – “The Higgs Review”

The board should undertake in-depth consideration of company matters that are deemed significant including new projects, existing projects, approvals and endorsement of advice.

The board should ensure that workforce policies and practices are consistent with the company's values and support its long-term sustainable success. The workforce should be able to raise any matters of concern.

There should be a record of the essential functions and other matters which are reserved for board decision and cannot be delegated.



EVIDENCE

- E3 There should be evidence that the board meets regularly to consider, review and record discussions and conclusions
- E4 There should be evidence of delivery of strategies and plans, including scrutinising key operational and finance performance information
- E5 There should be evidence of the desired culture and behaviours
- E6 The company structures should be regularly scrutinised in order to ensure they remain fit for purpose
- E7 There should be evidence that the board has clear policies and procedures for its members to ensure that actual or potential conflicts of interests are identified, declared, and acted upon

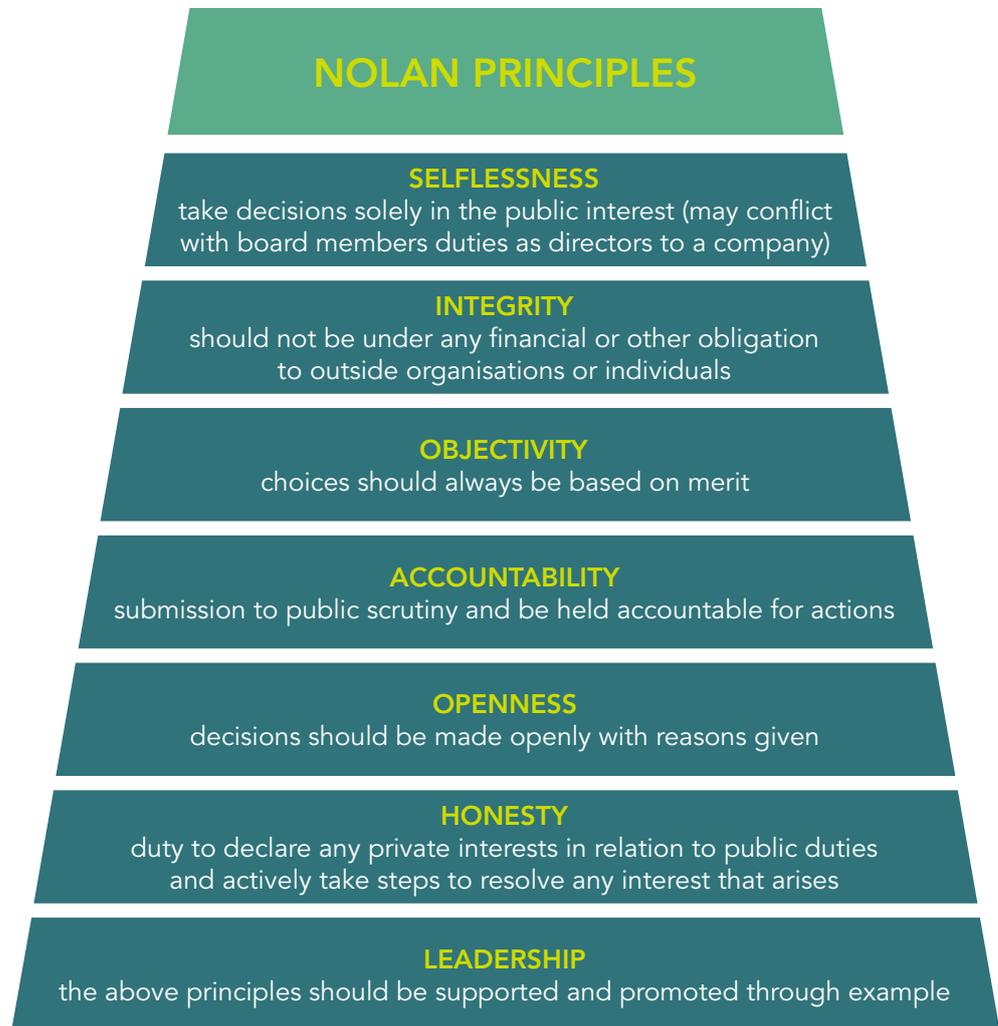
4.5 Role and behaviours of company directors

The Companies Act 2006⁷ (sections 171-177) states that directors must:

- ▶ act within their powers
- ▶ promote the success of the company
- ▶ exercise independent judgement
- ▶ exercise reasonable care skill and diligence
- ▶ avoid conflicts of interest
- ▶ not accept benefits from third parties
- ▶ declare an interest in proposed transactions or arrangements with the company

⁷ The Companies Act 2006
[www.legislation.gov.uk/
ukpga/2006/46/contents](http://www.legislation.gov.uk/ukpga/2006/46/contents)

Directors of wholly or partly owned council entities must also act in accordance with the seven Nolan Principles⁸:



EVIDENCE



- E8 There should be evidence that directors have sufficient skills and experience to run the entity
- E9 There should be evidence that directors' behaviours are aligned with the requirements of the Companies Act 2006 and the Nolan Principles as well as Cabinet Office's Code of Conduct for Board Members of Public Bodies⁹
- E10 The scope of directors' authorities should be documented and clear to all parties

⁸ The Seven Principles of Public Life – “Nolan Principles”

⁹ Code of Conduct for Board Members of Public Bodies published by the Cabinet Office in 2011 as updated/replaced in June 2019

4.6 Company board composition

Achieving the right board composition should facilitate good governance and minimise the scope for conflicts of interest.

The optimal size of a board should be between five and 10 directors, although this will be dependent on the circumstances of each entity.

Boards of wholly or partly owned council entities are often a mix of council officers, members, and independent directors. Board skills and expertise can be improved through the effective use of independent directors with both public sector and market specific experience. The UK Corporate Governance Code¹⁰ advises that at least half the board (excluding the chair) should be independent non-executives.

Appointments to the board should be subject to a formal, rigorous, and transparent selection procedure based on merit and published objective criteria.

Board composition and individual director performance should be reviewed periodically to evaluate board composition, the effectiveness of individual contribution, and how effectively board members work together to achieve the objectives of the entity.

EVIDENCE



- E11 There should be evidence that the board has a diverse membership with the collective skills and attributes needed to lead the entity effectively
- E12 There should be evidence that board membership is reviewed regularly for composition and fitness for purpose

4.7 The board and risk management

The board should have ultimate responsibility for risk management within the entity and ensure that appropriate risk management arrangements are in place.

The board should regularly review risks and how they are being managed, and potentially delegate the detailed scrutiny and evaluation of risk to a committee.

¹⁰ The UK Corporate Governance Code, Financial Reporting Council, July 2018
www.frc.org.uk/getattachment/88bd8c45-50ea-4841-95b0-d2f4f48069a2/2018-UK-Corporate-Governance-Code-FINAL.pdf

The board should be aware of its appetite for risk and determine the risk profile for the entity. The board's approach to risk should be proportionate and appropriate to its model. For example, an entity which has borrowed money from the council and needs the council's support for working capital and revenue will have a different risk profile to a trading company which relies exclusively on external revenue.

EVIDENCE



E13 There should be evidence that the board understands the organisation's risk profile and the effectiveness of key controls and regularly reviews risks and risk appetite

¹¹ The Insolvency Act 1986
www.legislation.gov.uk/ukpga/1986/45/contents

¹² The Bribery Act 2010
www.legislation.gov.uk/ukpga/2010/23/contents

¹³ The Modern Slavery Act 2015
www.legislation.gov.uk/ukpga/2015/30/contents/enacted

¹⁴ Data Protection Act 2018
www.legislation.gov.uk/ukpga/2018/12/contents/enacted

¹⁵ Health and Safety at Work etc. Act 1974
www.legislation.gov.uk/ukpga/1974/12/contents/enacted

4.8 Board members' skills and development

Training should cover legal roles and responsibilities, company directors' roles and companies generally. The training should include responsibilities under the Companies Act 2006, Insolvency Act 1986¹¹, Bribery Act 2010¹², Modern Slavery Act 2015¹³, Data Protection Act 2018¹⁴ and Health and Safety at Work etc. Act 1974¹⁵.

The entity should seek a board which includes a range of skills and backgrounds including commercial, financial, business development, technical, legal and HR experience. Those skills may either be provided by council nominees or by engaging non-executive directors.



The Cadbury Report states that **“given the varying backgrounds, qualifications and experience of directors, it is highly desirable that they should all undertake some form of internal or external training; this is particularly important for directors, whether executive or non-executive, with no previous board experience. Newly-appointed board members are also entitled to expect a proper process of induction into the company's affairs. It is then up to individual directors to keep abreast of their legislative and broader responsibilities”**.

There should be an annual evaluation of board, committee, chair, and director performance. UK Corporate Governance Code suggests that the chair should consider having this evaluation externally facilitated.



EVIDENCE

- E14 There should be documented evidence that the board regularly undertakes a skills audit to ensure that it has an appropriate balance of skills and experience
- E15 There should be evidence of ongoing professional training provided to ensure that all board members are up-to-date in their understanding and supported in their roles

4.9 Role of executive directors and non-executive directors

It is important to distinguish the between the roles of executive director, non-executive director and independent non-executive director. Legally, they all share the same individual and collective duties and responsibilities. However, they should all bring a distinct focus to their roles.

The role of executive directors will vary greatly from entity to entity. Essentially, they are focused on running the entity's business activities and implementing the board's plans and policies. They may be expected to be board members, although this is not essential.

Non-executive directors have a wider role, providing independent and constructive challenge.

Council appointees to boards will generally be expected to fulfil the role of a non-executive director. However, council officers who are appointed to undertake a dedicated role within an entity may be appointed in an executive capacity, such as to undertake the role of a finance director.



The Cadbury Report states that “**non-executive directors have two particularly important contributions to make to the governance process as a consequence of their independence from executive responsibility... The first is in reviewing the performance of the board and of the executive. The second is in taking the lead where potential conflicts of interest arise**”.

Independent non-executive directors are external appointees who do not hold a role as officers or members within the council. Entities should consider the use of independent non-executive directors to improve the quality of board representation. These appointments should be external to the council and provide detailed experience and insight into the company’s particular area of activity as well as providing independent and constructive challenge.

According to Higgs¹⁶, the role of a non-executive is to:

- ▶ challenge, and contribute to the development of the company’s strategy
- ▶ scrutinise performance of management in meeting agreed goals and monitor reporting of performance
- ▶ satisfy themselves on the accuracy of financial information and that financial controls and risk management are robust and defensible
- ▶ determine executive directors’ remuneration and prime role in appointing/removing senior management

Higgs describes a number of desirable personal attributes and behaviours of non-executive directors:

**HIGGS’
DESIRABLE
PERSONAL
ATTRIBUTES AND
BEHAVIOURS OF
NON-EXECUTIVE
DIRECTORS**

Sound judgement
and an enquiring
mind

Knowledge
of the business,
its operating
environment,
and issues
it faces

Integrity,
probity, and
high ethical
standards

Objectivity as
the basis for
questioning
and challenging
accepted
thinking of
executives

Strong
interpersonal
skills

¹⁶ Review of the role and effectiveness of non-executive directors, Department of Trade and Industry, January 2003 [web.archive.org/web/20080910081648/http://www.berr.gov.uk/files/file23012.pdf](http://www.berr.gov.uk/files/file23012.pdf)



EVIDENCE

- E16 There is evidence that the role of executive directors is clearly defined and documented
- E17 Non-executive directors are in place to bring an independent judgement to bear on issues of subject matter expertise, strategy, performance, resources including key appointments, and standards of conduct
- E18 There is documented evidence that the board values the role of non-executive directors, and their views are influential in the board's decisions

4.10 The role of the board chair

The Cadbury Report describes how the chair's role in securing good corporate governance is crucial. Chairs are primarily responsible for the workings of the board, for its balance of membership subject to board and shareholders' approval, for ensuring that all relevant issues are on the agenda, and for ensuring that all directors, executive and non-executive alike, are enabled and encouraged to play their full part in its activities.

Chairs should be able to stand sufficiently back from the day-to-day running of the business to ensure that their boards are in full control of the company's affairs and alert their obligations to their shareholders.

In addition, the chair should have the following leadership responsibilities:

- ▶ formulating the board's strategy
- ▶ promoting the efficient and effective use of staff and other resources
- ▶ delivering high standards in terms of integrity and propriety



The Cadbury Report states that the chair's role **"should in principle be separate from that of the chief executive. If the two roles are combined in one person, it represents a considerable concentration of power... therefore, there should be a clearly accepted division of responsibilities at the head of a company, which will ensure a balance of power and authority, such that no one individual has unfettered powers of decision"**.



EVIDENCE

E19 There is evidence that the chair provides clear board leadership, supporting the directors and chief executive and taking account of the shareholders views

4.11 Financial management

The business plan and business planning process are critical parts of the governance culture and environment. They are the basis for monitoring financial performance and should also feed into the medium-term financial planning of the council in situations where it expects to receive dividends, loan repayments, capital receipts or provide financial support in terms of working capital or longer-term finance.

Board reports should feature clear articulation of the current financial position of the company in terms of its trading position (income and expenditure), liquidity (cash flow) and solvency (balance sheet).

The company should have an independent financial status from the council. This should include separate bank accounts and designated signatories.

The financial transactions of the company should be recorded on the company's own, separate ledger system and the council should be able to demonstrate how the results of the company are consolidated into its own group accounts.

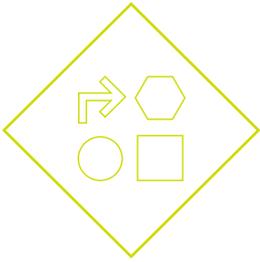
The company should have a set of documented financial policies and procedures which describe areas such as borrowing and overdraft limits and levels which are reserved for council approval. These reserved matters should also be documented in the company's articles of association.

It should operate a system of internal controls that are consistent with these policies and procedures. The company's internal controls should be the subject of periodic testing by internal auditors, whether they be the council's own internal audit function or separately appointed by the company.



EVIDENCE

- E20 There should be a fully documented and approved business plan that is consistent with and no more than 12 months older than the previous business plan. The changes within the updated business plan should accord with the trajectories that are apparent from monthly financial and non-financial performance reports
- E21 The financial transactions and values attributable to the company within the council's medium term financial plan should agree with the projections in the business plan
- E22 Board reports should include clear presentation of the monthly income and expenditure position of the company as well as a cash flow statement and balance sheet
- E23 There should be evidence of an annual audit letter from the council's external auditors, confirming the degree of confidence they hold in respect of consolidation or treatment of financial instruments entered by the company
- E24 Documented financial policies and procedures should be available
- E25 There should be evidence of an effective annual internal audit programme



5 ALTERNATIVE DELIVERY MODELS

5.1 Introduction

The **Localism Act 2011** gave local authorities new and broader general powers of competence to trade and since that time there has been a surge in the creation of new companies. These range from wholly owned and partly owned companies, joint ventures with either the public or private sector, and social enterprises.

The main benefits of an alternative delivery approach are perceived to be:



Establishing an alternative delivery approach such as a wholly or partly owned entity is a significant strategic decision that should be given consideration with an appropriate level of analysis and attention.

This section of guidance aligns with HM Government's Sourcing Playbook **Delivery Model Assessments** process. It covers the approach councils should adopt and suggests questions they should address when thinking about setting up a new Local Authority Trading Company (LATCo).

5.2 Framing the challenge

The initial challenge is to determine whether the council's service and the outcomes it delivers can be best delivered by alternative means.

If there is insufficient oversight and assurance placed on this fundamental analysis, particularly where a commercial initiative is progressed at speed, this will create significant operational, commercial, and reputational risks.

From the outset, it is important to clarify the objectives, timescales, and drivers of change.

A dedicated core team of suitably skilled individuals should be appointed that will input into the process. This may include finance, commercial, programme and operations and technical experts.

The approach to governance needs to be established, as well as a clear understanding of the decision-making process.

Identifying the final approvers of the recommendations to establish (or not) LATCos is critically important.

A good understanding of all the key stakeholders who will be involved in and/or affected by the outcomes needs to be developed, ensuring that all relevant parties can be engaged in the assessment process.

There should also be suitable administrative and project management support available to keep things on track.

5.3 Defining the service, delivery model options and data inputs

It is important to identify the service components to be delivered and the outcomes sought and the options for how they might be delivered. It is essential to develop a clear definition of these before starting the delivery model assessment to enable an effective comparison of alternative delivery models.

Once a long list of options has been developed, potential delivery models should be short-listed based on critical success factors, practical limitations, and discussions with senior stakeholders.

The final list of potential delivery models should be signed off at member and senior officer level before evaluation.

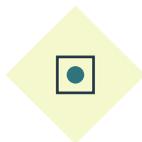
5.4 Potential options for consideration

In this section, we outline the main options for delivery models that local authorities may choose to consider:



A description of potential options is provided below, including an overview of the benefits and risks of adopting each model. It should be noted that this list is not exhaustive, and the specific options considered by each council will differ depending on its priorities and local circumstances.

The most important thing is that councils should not jump to a specific model without a comprehensive consideration of the potentially viable options for delivering the outcomes required. For example, in addition to the option of establishing a company or participating in a joint venture, councils may consider other options including in-house delivery, outsourcing, and sharing services with another public body.



In-house delivery

Description	This option involves services/functions being delivered in-house
Benefits	<ul style="list-style-type: none"> The council retains full control of service delivery and of any efficiencies achieved Existing skills and knowledge of service are retained Familiarity of relationships, experience, and expertise
Risks and issues for consideration	<ul style="list-style-type: none"> Ability to invest in, resource and upskill the service/function may be constrained No benefits of scale or sharing of resources/expertise All risk and responsibility retained by the council



Council owned company (for example, company limited by shares or company limited by guarantee)¹⁷

Description	This option involves the council establishing a company The company limited by shares model is designed for profit distribution to the participating organisations A company limited by guarantee is not designed for profit distribution
Benefits	Limited liability for shareholders Ringfences risks and liabilities, but council still retains reputational risk Freedom from direct management or standing orders of the council. A company has the capability to employ its own staff. Employees can be given greater incentive to succeed through new employment opportunities and financial reward, thereby promoting cultural change and developing a commercial mind-set Under this model, commercially delivered incidental services can be provided to the private sector (under Section 95 of the Local Government Act 2003) Commercial focus on business plan and goals Flexibility for the company to buy/sell/hold assets
Risks and issues for consideration	Can be administratively time consuming both in terms of set up and ongoing running This model requires compliance with the requirements of the Companies Acts and the administration of setting up and operating a separate entity There are additional regulatory requirements to comply with e.g., company audit and annual returns. Income may be liable to corporation tax VAT structures will be changed Potential loss of control to directors whose primary duty is to the company, not the council Risk exposure will vary depending on whether services are provided solely to the council or more widely to external organisations On paper, the “limited by shares/guarantees” structure limits councils’ liabilities. However, there is a question as to the extent to which a council would realistically allow a company to fail without meeting their liabilities. Consideration would be needed with regard to what interventions the council would make should the company make significant losses Potential for reputational damage to the shareholders in the event of non-performance

¹⁷ There are a range of legal structures that can be considered under this broad commercial entity option which may include Community Interest Companies (intended for social enterprises that wish to use assets and profits for public benefits, with mandatory asset lock and controls on dividends to reassure potential participants, donors, or investors) and Industrial & Provident Societies for Community Benefit (organisations with social objects to run a trade or business for the benefit of the community).



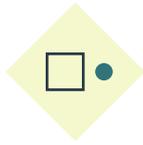
Joint service delivery or public sector consortium (shared services)

Description	Two or more councils or other public bodies join to effect service delivery and deliver better outcomes
Benefits	Potential economies of scale Scope for seamless service delivery Sharing of skills and improved resilience
Risks and issues for consideration	Potential impact of future changes in political control Problem of co-ordinating objectives and requirements of each local or public body Problem of assimilating procedures and IT systems of each public body Available capital will not necessarily be increased Long period of complex negotiation may be needed



Joint venture with the private sector

Description	Council enters into a joint venture with a private sector partner to facilitate the provision or delivery of services, investment and/or development This can include the creation of a separate legal entity
Benefits	May introduce capital resources which would not otherwise be available to the council Improved access to skills, resources, and systems of the partner (commercial acumen, technology) Potential wider opportunities for employees Risks in service delivery identified and allocated – enables some risk transfer Council influence can be preserved through controls on company decision-making
Risks and issues for consideration	Potentially significant time and costs involved in establishing the vehicle Additional regulatory requirements (company audit, annual returns) and potential tax implications Challenges in matching diverse organisational cultures in one entity Need for council vigilance in relation to commercial risks and cost structures



Outsourcing

Description	The council contracts with a private sector provider to provide certain services This generally involves a total transfer of the service provision to the service provider
Benefits	The competitive nature of the procurement should ensure the most economic price Scope for investment in the service from the partner A mature market exists
Risks and issues for consideration	Potential concerns over loss of direct control of service and risk of becoming “locked in” with a single provider TUPE ¹⁸ issues may prevent savings and lock in terms and conditions that would otherwise change over time Potential loss of key people from the council Additional costs of client-side arrangements Intense public scrutiny and reputational damage if the service provider performs poorly

5.5 Establishing strategic and operational evaluation criteria

There are many potential issues to consider in the selection of a delivery model.

Evaluation criteria will be specific to the service or function under consideration, but the following areas give some examples of the potential issues that might help to determine the most appropriate strategic approach for delivery.

Individual criteria should be given weightings reflecting the importance of that criterion to the council and the nature of the specific service.

The criteria should be signed off at member and senior officer level board before the evaluation of the delivery options begins.

¹⁸ Transfer of Undertakings (Protection of Employment) regulations (TUPE) www.gov.uk/transfers-takeovers

Description	Issues to consider
Strategy and policy	How well does the delivery model align with corporate strategies and policies?
Transition and mobilisation	How easy will it be to transfer existing services into the new model?
People and assets	What capabilities and skillsets are needed and what is the existing capacity (internal or in the external market)?
Service delivery	How will the delivery model help to deliver ongoing quality, innovation and continuous improvement?
Risk and impact profile	Have the risks that may impact the delivery of services or on the council's finances been identified?

5.6 Assessing the cost and benefits of the options under consideration

A financial model should be used to help evaluate different delivery model options. For example, a council may wish to compare the expected cost and benefits of establishing and running a wholly or partly owned entity with the cost and benefits of other delivery models under consideration.

An appraisal of the company model against the in-house delivery model will typically focus on a comparison of the expected whole life cost of procuring a service from an outside supplier, including the cost of additional market factors such as risk and profit, against the whole life cost to deliver a service using internal resources and expertise.

5.7 Conducting the evaluation and aligning the analysis

A cross-functional team should evaluate each criterion against the agreed weightings.

Learning should be derived from objective evidence, past projects, and colleagues across the public and private sector (this may include engaging with the market) to test and sense-check findings.

There are several critical success factors in completing a successful assessment:

- ▶ appropriate governance and sponsorship with appropriately qualified individuals
- ▶ senior leadership should be clear about why the evaluation is taking place, provide sponsorship, clear governance, and allocate suitably experienced and skilled individuals
- ▶ good availability of input data
- ▶ data should be available to input into the model design and evaluation
- ▶ informed strategic and operational criteria
- ▶ independent facilitation should take place to bring together stakeholders, clarify objectives and drive credible outcomes
- ▶ realistic timelines
- ▶ enough time should be allocated to run a comprehensive process

5.8 Key questions at the evaluation stage

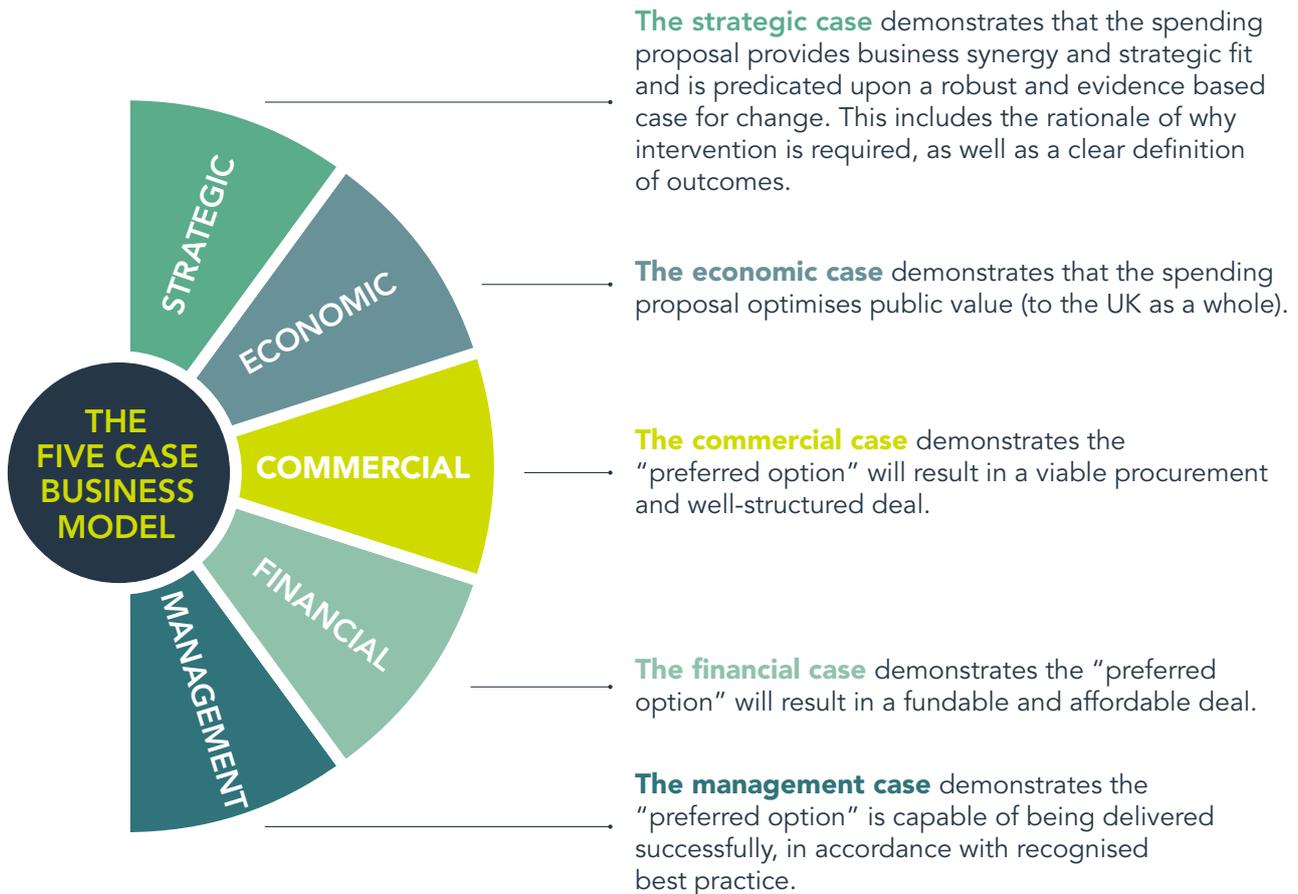
Specific questions should be asked when evaluating the viability and benefits of establishing a new commercial entity.

Criteria	Issues to consider
Strategy and policy	<p>How will the delivery model ensure delivery of strategic objectives, such as social value?</p> <p>What will be the internal council impact on officers and elected members (including training and recruitment implications), service and departmental structures, staffing requirements, and financial budgets?</p>
Legal and financial	<p>What is the optimum legal authority for activities which the new activity will pursue?</p> <p>What is the most appropriate and beneficial legal form and structure for a new entity (taking account of the objectives of the council)?</p> <p>What external legal and financial obligations which will be placed upon the entity and to what extent will these impact upon the objectives of the council and the relationship between the council and the new entity?</p>

Criteria	Issues to consider
Governance and risk	<p>Who will control the entity and what does that mean for governance, leadership, and the legal status of the entity?</p> <p>What is the optimum form of and limits to the relationship between the entity and council officers and elected members?</p> <p>How will performance be managed and monitored?</p> <p>What are the commercial and operational risks that relate to the establishment of the new entity?</p> <p>Who is best placed to manage these risks and how might they be mitigated?</p>
People and assets	<p>Is there a clear understanding of TUPE considerations or asset transfer/ownership considerations?</p> <p>Has the council ensured it has sought legal and commercial advice on any issues and considered potential pension liabilities?</p>
Commercial	<p>Has sufficient data on market demand both locally and wider afield been gathered and investigated?</p> <p>Has sufficient financial, operational, past performance and governance data on potential competitors been gathered and interrogated?</p> <p>Has the impact of the new entity been considered on existing local infrastructure and particularly on public, private and third sector organisations that are currently operating in the market sector that the entity will enter?</p> <p>Does the impact that has been considered include financial and relationship issues?</p> <p>Does the entity intend to trade and if so, will this be with other local authorities? Or to a wider market?</p>
Stakeholders	<p>Is there evidence of support by relevant members and senior officers in relation to the establishment of the new entity?</p>
Skills and capability	<p>Have suitably qualified subject matter experts been engaged to provide appropriate input into the evaluation?</p> <p>Has suitable and appropriate specialist financial and taxation advice been sought from independent consultants?</p>

5.9 Developing a business case

Before setting up a company a council must prepare a business case. This should follow the HM Treasury Green Book approach to public sector investment, adopting the five-case model, as set out in the Guide to Developing the Project Business Case, Better business cases: for better outcomes¹⁹.



5.10 Key activities at business case stage

Specific activities should be undertaken when developing the business case for the establishment of a new commercial entity. They include activities to develop and communicate the business case.

¹⁹ Guide to Developing the Project Business Case, Better business cases: for better outcomes assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/749086/Project_Business_Case_2018.pdf

Criteria	Issues to consider
Strategy and policy	<p>What are the compelling reasons for establishing the entity and what should be achieved?</p> <p>Which options have been considered and what are the reasons for selecting a commercial entity as the way forward?</p> <p>Which form and type of entity has been chosen as the preferred option and what are the reasons for that choice?</p> <p>What are the desired outcomes and objectives and how do these fit with and contribute to the overall strategy of the council? This should include consideration of any dependencies with other projects, programmes or initiatives</p> <p>Why it is the right time to establish the new entity?</p>
Legal and financial	<p>What are the legal considerations relating to the establishment of the entity?</p> <p>What levels of control and freedom are required for the organisation?</p> <p>What set-up costs will be incurred by both the entity and the council?</p> <p>Has the high-level viability of the new entity been assessed?</p> <p>Are there any affordability issues given other commitments?</p> <p>Where appropriate, how will the new entity enable the maximisation of possible commercial and grant funded income streams? And, also the minimisation of VAT and other taxation impacts?</p> <p>What financial, legal, taxation and operational advice has been obtained from external consultants and other sources?</p>
Governance and risk	<p>What are the key risks and how they will be managed?</p>
People and assets	<p>Has advice been sought on staffing issues, including TUPE arrangements, union negotiations and pension transfers?</p>
Commercial	<p>Has the competitive landscape been assessed, as well as the positioning of the new entity within that landscape?</p> <p>What will be the impact on the local and wider operating environment and market?</p>
Stakeholders	<p>What is the appetite for change, including stakeholder engagement and the level of support provided?</p>
Skills and capability	<p>What are the capabilities of existing staff to oversee and manage the new entity and what will be the future training and recruitment requirements?</p>

5.11 Recommendations and approvals

From the outset councils should be clear about the assurance and approval process at each stage.

A board or cabinet decision should be made at each stage to progress, or to stop the process, if a viable option cannot be moved forward.

5.12 Key activities prior to approval

Specific activities should be undertaken prior to the council approving the establishment of a new commercial entity.

Criteria	Activities to be undertaken
Legal and financial	<p>Ensure all legal, financial, taxation, operational and governance duties, responsibilities and obligations of the chosen legal form of entity are understood and communicated to all officers and members and all potential executives and non-executives of the new entity</p> <p>Ensure that the proposed arrangements comply with procurement and state aid legislation</p> <p>Ensure that all external legal, financial, taxation and operational advice has been understood and acted upon</p> <p>Confirm the financial, legal, and reputational impacts if the entity fails</p>
Governance and risk	<p>Identify possible exit or alternative strategies if the new entity is unsuccessful or there is a change in strategy within the council</p> <p>Identify and clarify the council officer and/or member involvement on the entity board</p>
Commercial	<p>Ensure understanding of updated realistic demand projections based upon third party sector expertise</p> <p>Ensure that monitoring information requirements and arrangements are clearly identified in both the council and the new entity</p>

5.13 Implementation

Once the final delivery model recommendation has been signed-off through appropriate governance forums there should be a clear plan in place for implementation.

5.14 Key transition activities

Specific transition activities should be undertaken prior to the formal establishment of the new entity.

Criteria	Activities to be undertaken
Strategy and policy	Ensure that arrangements are in place for both leading the new entity and leading the transition to put it in place
Legal and financial	<p>Confirm that the choice of entity delivery vehicle chosen maximises the possibility of commercial and grant funding income streams and minimises the impact of VAT and other taxation and is based on clear analysis of external legal, financial, taxation and operational advice</p> <p>Test the adequacy of the entity's opening financial projections including that the opening cash flow arrangements are adequate</p> <p>Confirm any contract arrangements, including arrangements for annual review, initial contract length and projected longer term budget impacts on both the council and the entity</p> <p>Ensure that adequate financial controls are in place</p> <p>Ensure that the formation and start-up of the entity has been notified to all relevant statutory and regulatory bodies</p> <p>Confirm that any ongoing services or assets that might be provided by the council are underpinned by agreements between the parties and can legally be provided, including consideration of the leases and/or licences relating to all assets and buildings to be used by the entity</p> <p>Ensure that the entity's systems and processes, including financial and payroll processes, are fit for purpose</p> <p>Ensure that the council have adequate insurance cover for the new entity's liabilities and assets</p> <p>Ensure that the entity's Articles of Association and other governing documents are fit for purpose and allow the organisation to fulfil its obligations and meet its objectives</p>

Criteria	Activities to be undertaken
Governance and risk	<p>Confirm that the business case still makes sense in terms of funding, affordability and expected benefits</p> <p>Ensure that the plan through to completion of transition is appropriately detailed and realistic, including risk management arrangements</p> <p>Identify and document service and financial risks</p> <p>Develop the performance measures and tools to be used</p> <p>Confirm the limits of council officer and member involvement in the day to day operational and strategic management of the entity</p> <p>Ensure that potential conflicts of interest have been addressed for council members or officers who will also holding positions with the new entity</p> <p>Confirm that the necessary and appropriate assurance bodies such as auditors, have been appointed or are in the process being appointed</p>
People and assets	<p>Ensure that all TUPE and pension transfer arrangements have been finalised</p> <p>Develop the processes for appointing entity non-executives, executives and any external appointments and commencing any recruitment processes</p>
Commercial	<p>Review the business model and commercial model and whether these appear to be viable given the overall environment within which the new organisation will be operating</p> <p>Develop a detailed, credible business plan which is subject to challenge and review</p>
Stakeholders	<p>Confirm that stakeholder support remains strong</p> <p>Develop and implement a public relations strategy</p>
Skills and capability	<p>Confirm that the right capacity and capability is in place to both transition to and then run the new organisation</p> <p>Develop requirements for training and support of officers and members and for prospective entity non-executives, executives and staff on new arrangements and relationships</p> <p>Identify areas of expertise and personnel to appoint to entity board</p>

5.15 Review

Once the entity is operational, it should be subject to effective oversight and regular review. Sections 3 and 4 cover the governance arrangements which need to be in place, within both the council and entity, to enable that oversight and review.



6 STANDARD DOCUMENTS REQUIRED FOR A REVIEW

When carrying out a review, documentation should be made available as evidence, to provide assurance that the governance structures and processes for managing risk are sufficiently robust and the entities are meeting councils' expectations.

As a minimum, these documents should include:

12 months of minutes (to cover the full business planning cycle) for all entity boards, any shareholder group(s), and engagements between shareholder groups and entity board members

Key executive and scrutiny reports

The entity's business plan and other key documents which document performance to date

Key governance documentation such as:

- articles of association
- shareholder's agreement
- members' agreement
- any financial agreements (covering any support or services provided by either party to the other)

Governance and structure charts and any descriptions of key roles and responsibilities for:

- the entity
- council oversight of the entity

The original business case which resulted in the creation of the entity and any updates

Terms of reference for:

- the shareholder role
- the board
- the entity's audited accounts

The risk logs for:

- the entity
- the council

The policies and processes to manage conflicts of interest for the council and the entity

Board member training plans



7 KEY REFERENCE DOCUMENTS

Code of Conduct for Board Members of Public Bodies published by the Cabinet Office in 2011 as updated/replaced in June 2019

This code sets out the personal and professional standards expected from non-executive board members of UK public bodies and forms part of their terms of appointment. The 2019 code includes new provisions making clear that bullying, harassment, or other discriminatory behaviour will not be tolerated. It also introduces a new requirement for the board member to notify the sponsor department of any bankruptcy, current police investigation, unspent criminal conviction, or disqualification as a company director. The new code also reminds office holders of their role in promoting diversity and inclusivity within their organisation, including at board level.

The Seven Principles of Public Life – “Nolan Principles”

The Seven Principles of Public Life outlines the ethical standards those working in the public sector are expected to adhere to. They were first set out by Lord Nolan in 1995 in the first report of the Committee on Standards in Public Life and are included in a range of Codes of Conduct across public life.

The Financial Aspects of Corporate Governance – “The Cadbury Report”

This report was published in December 1992. The committee, chaired by Sir Adrian Cadbury, had a remit to review those aspects of corporate governance relating to financial reporting and accountability and to make recommendations to raise standards in corporate governance.



The 2018 UK Corporate Governance Code

This code builds on the Cadbury Report, revising and expanding the guidance to take account of the increasing demands on the UK's corporate governance framework.

Review of the Role and Effectiveness of Non-Executive Directors – “The Higgs Review”

This report was authored by Derek Higgs and was published in January 2003. It was commissioned by the Secretary of State for Trade and Industry.

Corporate Governance Guidance and Principles for Unlisted Companies in the UK

This document was published in November 2010 by the Institute of Directors and European Confederation of Directors' Associations.

UK Government Investments Framework Document April 2018, Updated July 2020

A framework document drawn up by HM Treasury in consultation with UK Government Investments Limited, a private limited Government-owned company.

Nottingham City Council – Report in the Public Interest concerning the Council's governance arrangements for Robin Hood Energy Ltd – Grant Thornton

This report was issued in the Public Interest under section 24 and Schedule 7 of the **Local Audit and Accountability Act 2014**. It addresses failings in the Council's governance for Robin Hood Energy (RHE), which was established in 2015 as a wholly owned not-for-profit subsidiary of the Council.



Public Interest Report – Governance issues in relation to remuneration of Council officers for work as Directors of City of York Trading Ltd February 2016 – Mazars

This report related to payments made in March 2015 by City of York Trading Ltd (a trading company specialising in the provision of temporary staff and wholly owned by the Council) to two of the company's executive directors who were also officers of the Council. It provides lessons to be learnt and to ensure the future good governance of a Council's relationships with its trading companies.

The Green Book guidance – HM Treasury, 2018

This document provides guidance for public bodies on how to appraise policies, programmes and projects. It also provides guidance on the design and use of monitoring and evaluation before, during and after implementation. It contains the 'Five Case Model' – the required framework for considering the use of public resources to be used proportionately assess costs and risks.

The Sourcing Playbook – Cabinet Office, May 2021

This document provides guidance on choosing the best model for delivering public services.



8 SUMMARY OF EVIDENCE

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
Governance aims					
C1	There should be evidence that the council and senior management recognise the importance of establishing appropriate and proportionate governance arrangements for the oversight of entities	<ul style="list-style-type: none"> ▶ The council has sufficient control to ensure that its investment is protected, appropriate returns on investment can be obtained and that the activities of the entity are aligned with the values and strategic objectives of the council ▶ “Teckal” companies demonstrate compliance with relevant exemption requirements under EU procurement law 			
C2	There should be evidence of a culture of challenge and clarity relating to the purpose, efficiency, effectiveness, specific objectives, and freedoms of the entity	<ul style="list-style-type: none"> ▶ There is a culture of challenge ▶ There is a clarity of purpose ▶ The entity has clear objectives ▶ The entity has sufficient freedoms to achieve its objectives 			

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
The council's shareholder role					
C3	There should be a clearly designated council shareholder role or function which is both understood and recognised by the council and the entity (and documented in terms of reference)	<ul style="list-style-type: none"> ▶ The council has a designated "shareholder" role to represent its ownership of the entity ▶ The shareholder provides oversight of any decisions taken by the entity ▶ The shareholder provides a regular review of whether the entity provides the most effective vehicle to deliver the outcomes it requires and whether there are suitable alternatives ▶ The process for appointing a shareholder is set out in terms of reference 			
C4	There should be clarity regarding the role of shareholder, with reserved matters clearly documented and updated as required, reflecting any changes made as the entity has developed, in a shareholder's agreement (or as set out in the company's governing articles of association)	<ul style="list-style-type: none"> ▶ The council has sufficient control to ensure that its investment is protected, appropriate returns on investment can be obtained and that the activities of the entity are aligned with the values and strategic objectives of the council ▶ "Teckal" companies demonstrate compliance with relevant exemption requirements under EU procurement law 			

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
C5	There should be evidence that the individual undertaking the shareholder role is provided with suitable training and support commensurate with the role	<ul style="list-style-type: none"> ▶ There is a culture of challenge ▶ There is a clarity of purpose ▶ The entity has clear objectives ▶ The entity has sufficient freedoms to achieve its objectives 			
C6	There should be evidence of formal periodic shareholder/Chair/CEO meetings with effective supporting papers to inform subsequent company board meetings	<ul style="list-style-type: none"> ▶ The shareholder has a mechanism to communicate its views to the entity ▶ Periodic and effective shareholder/Chair/CEO meetings are documented 			

Council oversight, scrutiny, and governance framework

C7	There should be documented evidence of transparent member and officer scrutiny, oversight, and approval of business plans	<ul style="list-style-type: none"> ▶ There is a clearly defined governance framework underpinned by clear governance principles ▶ The role of the shareholder is separate from the board ▶ The business plan is current and updated at least annually ▶ The business plan is challenged and monitored by the board 			
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Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
C8 There should be evidence of a clear set of KPIs that fall out of the business planning process	<ul style="list-style-type: none"> ▶ The council regularly undertakes an objective assessment of how successfully each entity supports its policies and strategies ▶ KPIs are relevant to “SMARTER” goals ▶ KPIs are reported and monitored within the context of the governance framework 				
C9 There should be evidence that senior company staff are performance managed against KPIs	<ul style="list-style-type: none"> ▶ Board, committee, chair, and director performance is evaluated annually, including against agreed KPIs 				
C10 There should be evidence of ongoing assessment of value-for-money and quality offered by the entity through an adequately resourced monitoring function	<ul style="list-style-type: none"> ▶ Regular reviews take account of value-for-money and performance quality 				
C11 There should be ongoing assessment of risks relating to the entity, supported by processes to ensure that risks are managed as part of the council’s overall risk management approach, with appropriate escalation and reporting	<ul style="list-style-type: none"> ▶ The council regularly reviews risks relating to its entities and establishes whether they are effectively managed and scrutinised ▶ The council’s overview and scrutiny committee (or equivalent) provides overview, pre-decision scrutiny and call-in decisions in relation to the entity 				

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
C12 There should be evidence of a consistent approach across the council when it comes to engaging with its entities	<ul style="list-style-type: none"> ▶ All council entities are managed in a consistent way with appropriate support, guidance and controls 				
C13 The council should have clear and unfettered access to audited accounts for its entities	<ul style="list-style-type: none"> ▶ The council's audit committee pays specific attention to accounts and audit reports ▶ The council's internal auditors are able to gain clear and transparent access to financial information and oversight of internal controls 				
Business case for the entity					
C14 A business case which assessed the risk involved in establishing the entity and recommended its establishment, taking account of other potential delivery models, should be available to review	<ul style="list-style-type: none"> ▶ There is a clear and comprehensive business case that recommended the creation of the entity ▶ The business case took account of alternative delivery methods, with the case for the entity's creation having clear benefits over other methods 				
C15 Objectives of the entity should be clearly defined and documented, and regularly reviewed to ensure that its operation continues to support council policy and strategy, including periodically reviewing the business case to ensure it is still valid	<ul style="list-style-type: none"> ▶ The objectives of the entity are clearly articulated, defined and documented ▶ The objectives are regularly reviewed ▶ The objectives continue to reflect council policy and strategy ▶ The business case and objectives are regularly reviewed to ensure they are still valid 				

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
Agreements with the entity					
C16	Agreements should be documented between the council and the entity for any support or services provided by either party to the other party	<ul style="list-style-type: none"> ▶ The council and entity have clear and documented agreements for any services or support provided by either party to the other party ▶ There is a clear process for escalation if the support or services agreements are not performed to either party's satisfaction 			
C17	All agreements should be clear, up-to-date, and regularly monitored and reviewed, with any changes to agreements documented so that a clear audit trail exists	<ul style="list-style-type: none"> ▶ Agreements for support or services between the parties are up-to-date and regularly monitored and reviewed ▶ Changes to agreements are documented with a clear audit trail 			
Avoiding and managing conflicts of interest					
C18	There should be evidence that a culture exists whereby actual or potential conflicts of interests are identified, declared, and acted upon, including evidence of appropriate training across the organisation	<ul style="list-style-type: none"> ▶ All parties have been trained and demonstrate a commitment to avoiding and monitoring actual or potential conflicts 			

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
C19 The council should have clear and up-to-date policies and processes to consistently manage actual conflicts or potential conflicts of interest, including a clear process for investigations and procedures for appropriate disciplinary actions in the event of breaches	<ul style="list-style-type: none"> ▶ There is a clear conflict of interest policy which is managed actively ▶ There is a clear process for investigating and dealing with breaches of the conflicts of interest policy ▶ Internal and external auditors review the management of conflicts of interest and escalate any concerns to the Monitoring Officer 				
C20 The roles, responsibilities and reporting lines of officers and members who are involved in council oversight of the entities, the provision of services between the entities or the running of the entities should be clearly defined and documented	<ul style="list-style-type: none"> ▶ Officers and members make themselves available to scrutiny and other council governance forums 				

Council appointments to the board

C21 There should be evidence that appointments to the board are subject to a documented formal, rigorous, and transparent procedure based on merit and published objective criteria which also promote diversity	<ul style="list-style-type: none"> ▶ Board members have completed declaration of interest forms ▶ Appointments to the board are relevant to the post or office of the council ▶ Council appointed directors cease to be members if they leave their qualifying roles ▶ The process for the appointment and renewal of directors is set out in the articles of association 				
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Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
	<ul style="list-style-type: none"> ▶ If there is a remuneration committee, relevant matters are referred appropriately ▶ Appointments are based on a review of the skills, qualifications, diversity, and other attributes required for the role ▶ Where a board member is eligible for renewal and reappointment, this is subject to considering their performance to date and skills, and the needs of the board 				
Articles of association					
E1	<p>The entity's articles of association should be clear, up-to-date, and reflective of how the entity is run</p>	<ul style="list-style-type: none"> ▶ The entity has articles of association, documenting its constitution ▶ The articles address the entity's purpose, conduct of meetings, and role and appointment of directors ▶ If the entity is a Teckal company, the articles demonstrate that the council exercises control 			
Business planning					
E2	<p>There should be evidence of an up-to-date business plan that is reflective of the current circumstances and environment in which the entity operates</p>	<ul style="list-style-type: none"> ▶ There is an up-to-date business plan, setting out the organisation's objectives and how these will be resourced and achieved ▶ Requirements to meet the legal criteria in relation to any Teckal companies are reflected in the business plan 			

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
Role and behaviours of the board					
E3	There should be evidence that the board meets regularly to consider, review and record discussions and conclusions	<ul style="list-style-type: none"> ▶ The board meets regularly, and all decisions are recorded and documented ▶ Decisions are taken at the appropriate place, including deferral and recommendations of decisions on matters that are reserved for the shareholder 			
E4	There should be evidence of delivery of strategies and plans, including scrutinising key operational and finance performance information	<ul style="list-style-type: none"> ▶ The board has delegated detailed scrutiny to committees or directors with appropriate skills, including financial management ▶ The board challenges performance and key financial and operational reporting 			
E5	There should be evidence of the desired culture and behaviours	<ul style="list-style-type: none"> ▶ The board promotes the success of the company ▶ The board provides entrepreneurial leadership ▶ Prudent and effective controls are demonstrated where risk is assessed and managed ▶ The board sets strategic aims and ensures sufficient resources (financial and human) are available to meet objectives ▶ The board reviews management performance, including that of the CEO/MD and leadership team ▶ The board sets corporate values and standards ▶ The board ensures obligations to shareholders and others are met 			

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
E6	The company structures should be regularly scrutinised in order to ensure they remain fit for purpose	<ul style="list-style-type: none"> ▶ The company structures are regularly reviewed ▶ Financial and performance benchmarking exercises are carried 			
E7	There should be evidence that the board has clear policies and procedures for its members to ensure that actual or potential conflicts of interests are identified, declared, and acted upon	<ul style="list-style-type: none"> ▶ The board regularly monitors conflicts of interest, including with suppliers and users 			

Role and behaviours of company directors

E8	There should be evidence that directors have sufficient skills and experience to run the entity	<ul style="list-style-type: none"> ▶ Directors' skills align well to the organisation's purpose and objectives ▶ Directors are trained so that they are competent in undertaking their roles and responsibilities 			
E9	There should be evidence that directors' behaviours are aligned with the requirements of the Companies Act 2006 and the Nolan Principles as well as Cabinet Office's Code of Conduct for Board Members of Public Bodies	<ul style="list-style-type: none"> ▶ Directors: <ul style="list-style-type: none"> ■ act within their powers ■ promote the success of the company ■ exercise independent judgement ■ exercise reasonable care skill and diligence ■ avoid conflicts of interest ■ do not accept benefits from third parties ■ declare an interest in proposed transactions or arrangements with the company 			

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
	<ul style="list-style-type: none"> ▶ Directors act in accordance with the seven Nolan Principles: <ul style="list-style-type: none"> ■ selflessness ■ integrity ■ objectivity ■ accountability ■ openness ■ honesty ■ leadership 				
E10	The scope of directors' authorities should be documented and clear to all parties	<ul style="list-style-type: none"> ▶ Directors' authorities are demonstrated in a scheme of delegation ▶ The scheme of delegation includes reference to matters that are reserved for board decision and cannot be delegated 			
Company board composition					
E11	There should be evidence that the board has a diverse membership with the collective skills and attributes needed to lead the entity effectively	<ul style="list-style-type: none"> ▶ There are between five and ten directors on the board ▶ At least half of the directors are independent non-executives ▶ Appointments to the board are subject to a formal, rigorous, and transparent selection procedure based on merit and published objective criteria 			

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
E12	There should be evidence that board membership is reviewed regularly for composition and fitness for purpose	<ul style="list-style-type: none"> ▶ Board composition and individual director performance is reviewed periodically to evaluate board composition, the effectiveness of individual contribution, and how effectively board members work together to achieve the objectives of the entity 			

The board and risk management

E13	There should be evidence that the board understands the organisation's risk profile and the effectiveness of key controls and regularly reviews risks and risk appetite	<ul style="list-style-type: none"> ▶ The board demonstrates ultimate responsibility for risk management within the entity and ensures that appropriate risk management arrangements that are in place ▶ The board regularly reviews risks and how they are being managed ▶ The board is aware of its appetite for risk and determines the risk profile for the entity ▶ The board's approach to risk is proportionate and appropriate to its model 			
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Board members' skills and development

E14	There should be documented evidence that the board regularly undertakes a skills audit to ensure that it has an appropriate balance of skills and experience	<ul style="list-style-type: none"> ▶ The board regularly undertakes skills audits ▶ The entity has a board which includes a range of skills and backgrounds including commercial, financial, business development, technical, legal and HR experience 			
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Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
E15	There should be evidence of ongoing professional training provided to ensure that all board members are up-to-date in their understanding and supported in their roles	<ul style="list-style-type: none"> ▶ Regular training and updates cover legal roles and responsibilities, company directors' roles and companies generally ▶ Directors' training includes responsibilities under the Companies Act 2006, Insolvency Act 1986, Bribery Act 2010, Modern Slavery Act 2015, Data Protection Act 2018 and Health and Safety at Work etc. Act 1974 			

The role of executive directors and non-executive directors

E16	There is evidence that the role of executive directors is clearly defined and documented	<ul style="list-style-type: none"> ▶ Executive directors' roles are clearly defined and documented ▶ Directors' roles are focused on running the entity's business activities and implementing the board's plans and policies 			
E17	Non-executive directors are in place to bring an independent judgement to bear on issues of subject matter expertise, strategy, performance, resources including key appointments, and standards of conduct	<ul style="list-style-type: none"> ▶ Non-executive directors: <ul style="list-style-type: none"> ■ challenge, and contribute to the development of the company's strategy ■ scrutinise performance of management in meeting agreed goals and monitor reporting of performance ■ satisfy themselves on the accuracy of financial information and that financial controls and risk management are robust and defensible ■ determine executive directors' remuneration and prime role in appointing/removing senior management 			

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
E18 There is documented evidence that the board values the role of non-executive directors, and their views are influential in the board's decisions	<ul style="list-style-type: none"> ▶ The board values its non-executive directors, so that they are able to demonstrate: <ul style="list-style-type: none"> ■ sound judgement and an enquiring mind ■ knowledge of the business, its operating environment, and issues it faces ■ integrity, probity, and high ethical standards ■ objectivity as the basis for questioning and challenging accepted thinking of executives ■ strong interpersonal skills 				

The role of the board chair

E19 There is evidence that the chair provides clear board leadership, supporting the directors and chief executive and taking account of the shareholders views	<ul style="list-style-type: none"> ▶ The chair is primarily responsible for: <ul style="list-style-type: none"> ■ the workings of the board ■ its balance of membership subject to board and shareholders' approval ■ ensuring that all relevant issues are on the agenda ■ ensuring that all directors, executive and non-executive alike, are enabled and encouraged to play their full part in its activities ▶ The chair is able to stand sufficiently back from the day-to-day running of the business to ensure their board is in full control of the company's affairs ▶ The chair is responsible for: <ul style="list-style-type: none"> ■ formulating the board's strategy ■ promoting the efficient and effective use of staff and other resources ■ delivering high standards in terms of integrity and propriety 				
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Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
Financial management					
E20	There should be a fully documented and approved business plan that is consistent with and no more than 12 months older than the previous business plan. The changes within the updated business plan should accord with the trajectories that are apparent from monthly financial and non-financial performance reports	<ul style="list-style-type: none"> ▶ The business plan and business planning process are critical parts of the governance culture and environment 			
E21	The financial transactions and values attributable to the company within the council's medium term financial plan should agree with the projections in the business plan	<ul style="list-style-type: none"> ▶ The business plan provides the basis for monitoring financial performance and feeds into the medium-term financial planning of the council in situations where it expects to receive dividends, loan repayments, capital receipts or provide financial support in terms of working capital or longer-term finance 			
E22	Board reports should include clear presentation of the monthly income and expenditure position of the company as well as a cash flow statement and balance sheet	<ul style="list-style-type: none"> ▶ Board reports feature clear articulation of the current financial position of the company in terms of its trading position (income and expenditure), liquidity (cash flow) and solvency (balance sheet) 			

Evidence	What should you be able to find?	What evidence have you found?	RAG rating	Actions recommended	Responsible person/body
E23 There should be evidence of an annual audit letter from the council's external auditors, confirming the degree of confidence they hold in respect of consolidation or treatment of financial instruments entered by the company	<ul style="list-style-type: none"> ▶ The council's external auditor has provided an annual audit letter annually ▶ The annual audit letter confirms the degree of confidence they hold in respect of consolidation or treatment of financial instruments entered by the company 				
E24 Documented financial policies and procedures should be available	<ul style="list-style-type: none"> ▶ The company has an independent financial status from the council, including separate bank accounts and designated signatories ▶ The financial transactions of the company are recorded on the company's own, separate ledger system and the council is able to demonstrate how the results of the company are consolidated into its own group accounts ▶ The company has a set of documented financial policies and procedures which describe areas such as borrowing and overdraft limits and levels which are reserved for council approval 				
E25 There should be evidence of an effective annual internal audit programme	<ul style="list-style-type: none"> ▶ The company operates a system of internal controls that are consistent with financial policies and procedures ▶ The company's internal controls are subject to periodic testing by internal auditors 				



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