North Yorkshire Council

Audit Committee

11 December 2023

Commercial Governance Review

Report of the Corporate Director, Resources

1.0 PURPOSE OF REPORT

1.1 To provide an update on the report submitted to North Yorkshire County Council's Audit Committee on 12 December 2022 regarding the best practice for commercial governance set out in the Chartered Institute of Public Finance & Accountancy (CIPFA) updated publication "Local Authority Owned Companies – A good practice guide 2022 edition".

2.0 BACKGROUND

2.1 Through Local Government Reorganisation (LGR) North Yorkshire Council (NYC) inherited a number of companies that were owned by the predecessor county, district and borough councils. The following Local Authority Companies are now owned by NYC.

- Central Northallerton Development Company Limited (50% owned by the Council and 50% owned by Wykeland Properties Limited)
- Hambleton District Holdings Limited
- Maple Park (Hambleton) LLP
- Bracewell Homes Limited
- Brimhams Active Limited (Teckal)
- Mercury Housing Company Limited
- NY Highways Limited (Teckal)
- First North Law Limited
- Brierley Homes Limited
- Align Property Partners Limited
- Align Property Services Limited (Teckal)
- Yorwaste Limited (Teckal) (77.3% owned by the Council and 22.7% owned by City of York Council)
- Nynet Limited (Teckal)
- Veritau Limited (Teckal)

An updated structure of all the Council owned companies is at **Appendix A**.

2.2 In June 2022, CIPFA published updated guidance for local authorities to consider in relation to the governance process in place for any local authority owned companies entitled "Local Authority Owned Companies – A good practice guide 2022 edition".

2.3 The CIPFA publication aims to provide local authorities with guidance and best practice around the establishment of trading companies, setting up effective governance and monitoring processes, ensuring compliance, understanding the risks involved and supporting the enduring success of their business aspirations.

2.4 In December 2022 North Yorkshire County Council's Audit Committee were presented with a Commercial Governance Review report (attached at **Appendix B**), which highlighted the best practice guidance set out in the CIPFA publication. The report set out that a review of NYC's commercial governance arrangements would be undertaken post vesting day; with the outcome and actions from that review being reported back to the Audit Committee. This report provides an update on, and should be read in conjunction with, the December 2022 report.

3.0 UPDATE ON CURRENT POSITION

3.1 A Commercial Governance Review Group has been established to review the council owned companies; using the CIPFA guidance as a framework to assess existing arrangements. The Review Group includes representatives from the Council's legal and finance team, who will undertake detailed reviews alongside each company.

3.2 A "checklist" has been produced as a basis for reviewing each company's compliance with the CIPFA guidance and other areas of best practice; a copy of which is attached at **Appendix C**.

3.3 The Commercial Governance Review Group has already met with a number of companies and has scheduled meetings with those remaining companies that are actively trading. The intention of the Group is to write a detailed report to Brierley Board and Shareholder Committee in March 2024, which will set out the findings of the review work along with recommendations to address any areas of identified improvements. An update will be brought to the Audit Committee following the outcome of this work.

4.0 FINANCIAL IMPLICATIONS

4.1 There are no known financial implications in this report. If financial implications are identified through the review process they will be reported in the final report.

5.0 LEGAL IMPLICATIONS

5.1 There are no known legal implications in this report. If legal implications are identified through the review process they will be reported in the final report.

6.0 RECOMMENDATION

i) The Audit Committee is requested to note the contents of the report and agree to receive a further final report early in the next financial year.

APPENDICES:

Appendix A – Company Structure Post LGR
Appendix B - December 2022 Report to Audit Committee
Appendix C – Company Compliance Checklist

BACKGROUND DOCUMENTS:

CIPFA Guidance

Gary Fielding
Corporate Director – *Resources*

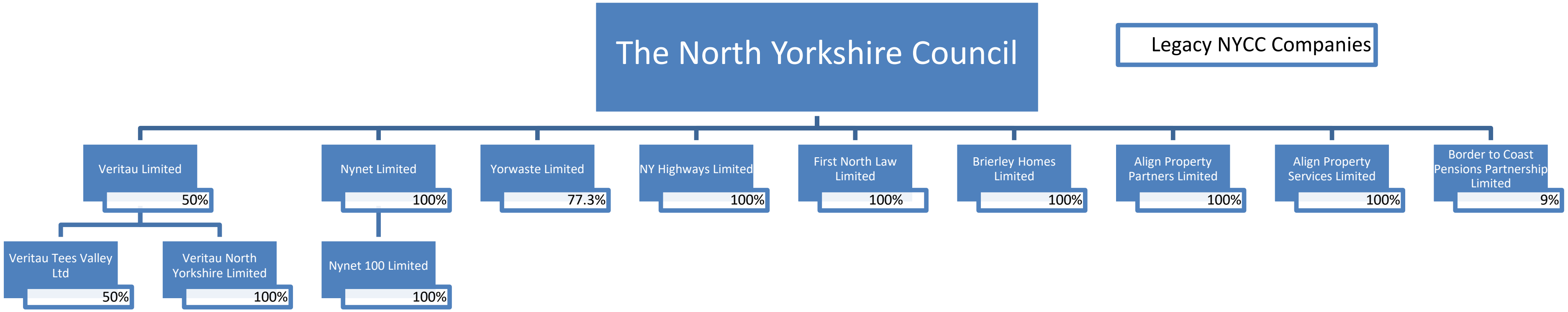
County Hall
Northallerton
11 December 2023

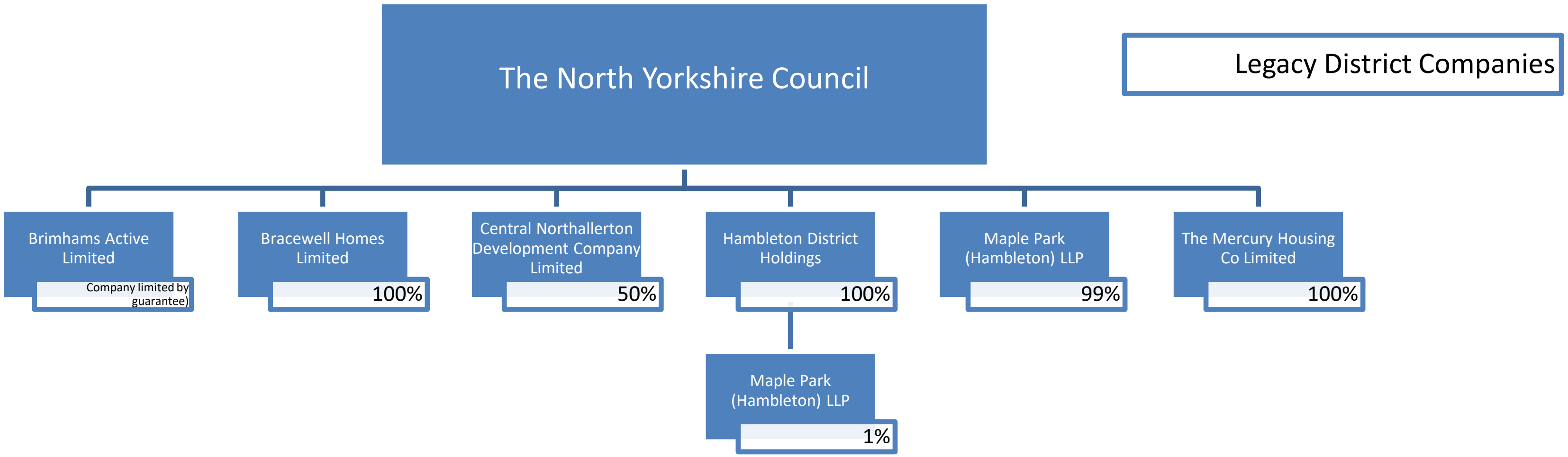
Report Author – *Peter Williams, Head of Finance and Bethany Bilby, Solicitor*
Presenter of Report – *Kerry Metcalfe, Assistant Director Commercial, Property & Procurement*

Note: Members are invited to contact the author in advance of the meeting with any detailed queries or questions.

APPENDIX A

STRUCTURE OF NYC OWNED COMPANIES





APPENDIX B

NORTH YORKSHIRE COUNTY COUNCIL AUDIT COMMITTEE REPORT DEC 22

North Yorkshire County Council

Audit Committee

12 December 2022

Commercial Governance Review

Report of Corporate Director, Strategic Resources

1.0 Purpose of Report

1.1 To highlight the best practice to commercial governance set out in the Chartered Institute of Public Finance & Accountancy (CIPFA) updated publication "Local Authority Owned Companies – A good practice guide 2022 edition". This report summarises best practice from the CIPFA guide. It is intended that a review of the existing arrangements will take place over the next few months in line with Local Government Reorganisation (LGR), with a report brought back to Committee post LGR detailing the outcome and actions from the review.

2.0 Introduction

2.1 The Brierley Group is made up of Council owned Companies. It is considered to be the trading arm of North Yorkshire County Council (NYCC/the Council). The group was established in 2017 to bring together the companies with the aim of improving customer experience and increasing overall shareholder value. Whilst the Brierley Group is not a legal entity in itself, and the group is not a group of companies in the traditional legal sense (with a holding company) it acts to provide oversight for NYCC. NYCC currently has eight commercial operations within the Brierley Group; Veritau, Align Property Partners, Yorwaste, NYnet, Brierley Homes, First North Law, NYES and NY Highways. Of the seven companies, five are wholly owned by NYCC and the other two are jointly owned with City of York Council. In addition, the Council has historically sold a number of services to schools which it now operates under the branding of "North Yorkshire Education Services" (NYES), but this is not set up as a separate company.

2.2 During the exploratory work of the LGR Commercial work stream a number of district owned commercial companies and commercial interests have been noted which will need to be considered in the future as part of the ongoing review of commercial best practice.

2.3 In June 2022, CIPFA published updated guidance for local authorities to consider in relation to the governance process in place for any local authority owned companies - "Local Authority Owned Companies – A good practice guide 2022 edition". In order to facilitate a review of the commercial environment in which the companies operate, this guidance published by CIPFA will be used as a framework to assess existing arrangements.

2.4 The CIPFA publication is titled as a good practice guide, it is aimed at giving Local Authorities guidance and best practice around establishing and forming trading companies, setting up effective governance and monitoring, ensuring compliance, understanding the risks involved and supporting the enduring success of their business aspirations. The publication highlights the areas where others have pursued commercial goals but have failed, examples include Nottingham City Council failed energy company Robin Hood Energy Limited and London Borough of Croydon Council's Brick By Brick housing company.

3.0 Summary of best practice from the CIPFA guidance

3.1 The guide recognises the increased risk to local authorities and the potential problems that engaging in trading companies and joint ventures can cause. It's stated aim is to assist local authorities by setting out and highlighting existing best practice in terms of ensuring a focus on what the authority wants to achieve and then the process to find the right option to achieve that goal. The guide covers the following areas:

- Set-up – the role of the company and the business case or options appraisal
- Governance – including roles and responsibilities
- Operational practices
- Assurance

3.2 Learning points included in the guide for authorities to consider are:

- Focusing on outcomes to be achieved
- Balancing the freedom for the company to deliver with sufficient oversight from the authority
- Ensuring relationships are robust by developing effective channels of communication between the authority and the company
- Choosing the right delivery model – using a robust options appraisal process
- Engaging effectively with stakeholders
- Seeking expert advice – authorities need support and cannot know everything
- Clarifying roles and responsibilities – obligations must be clear
- Ensuring finance, legal and service delivery functions work closely together throughout the life cycle of the company

3.3 Based on the information contained within the document, the following arrangements are key factors to be considered as part of the review, taking into account the CIPFA guidance:

a) Audit of Brierley group companies
b) Risk Management
c) Conflicts of Interest
d) External Board challenge
e) Business plans
f) Shareholder agreement
g) Post vesting day commercial review

4.0 Key considerations arising from the guidance

a) Audit of Brierley Group Companies

4.1 The guidance highlights that both the internal and the external audit function can provide a range of benefits such as;

- Providing assurance to the Board and wider stakeholders
- Ensuring compliance with policies and regulations
- Determining the adequacy and effectiveness of internal controls
- Identify operational weakness and inefficiencies
- Assess the efficient and responsible use of Council resources
- Pre-empt financial losses

4.2 The current arrangements and appropriate involvement of internal and external audit for each Brierley Group company will be considered as part of the review.

b) Risk Management

4.3 The guidance includes that best practice dictates that the ongoing management of risks is vital to the success of commercial organisations. Operating a successful commercial entity is in being cognisant of the current and emerging risks, creating strategies to document the short and long term risks and how the business is placed to address and mitigate them. Management of risks is also a key element of effective governance and in protecting shareholder and stakeholder interests and in exposing the Council to negative press about its investments.

4.4 Risks facing commercial organisations can (but not limited to) include areas such as technological/obsolescence, financial, interest rate, operational, reputational.

4.5 Technological risk can be due to a lack of forward thinking and innovation, what is currently a marketable product, competitive advantage or unique selling point (USP) today can easily be rendered obsolete.

4.6 Financial and economic risk, trading companies will be set up with an expectation and direction to generate a level of return to ultimately make the venture worthwhile for the authority.

4.7 Operational risk is the risk of losses caused by flawed or failed processes, policies, systems or events. Reputational risk can arise directly through the actions of the company or directly through the actions of an employee or related party. Reputational risk can quickly generate negative press and invite significant challenge to its owners, directors and leadership team.

4.8 The guidance suggests adapting the policies relative to the risk tolerance and risk appetite that each company faces. The approach of each company to risk and the processes and procedures in place will be considered as part of the review.

c) Conflicts of interest

4.9 The CIPFA guidance suggests having a policy for declarations and conflicts of interest within each company's articles of association.

4.10 The guidance notes that Members, officers, Directors and Board attendees can often have a diverse role within the authority and sit on multiple Boards as part of their duties as well as having various outside interests. In a dynamic commercial environment, conflicts of interest can arise and change unexpectedly during formal discussions and throughout the year. Conflicts of interest may arise for a number of reasons; these can include business interests but may also extend to personal relationships and conflicts of loyalty.

4.11 As a company Director, their duty is to the company, and this is the case even if the individual happens to also be a senior officer or elected Member of the Council. Directors also have a statutory duty to avoid conflicts of interest. Directors must have regard to the rules on declaring their interests and any restriction on voting, as may be set out in the company's articles of association.

4.12 When acting as a senior officer or Member of the Council, their duty is foremost to act in the best interests of the Council, subject to confidentiality of information required by the company. This wearing of different hats is clearly a cause of potential conflicts of interest.

4.13 The guidance suggests that Local Authority Members and officers are aware of potential conflicts of interest when performing their role for the Local Authority and their role in respect of the company. In general, if there are any doubts about conflicts of interest arising from an appointment, it is preferable not to make the appointment.

4.14 The guidance also states that there should be a formal policy in place to ensure Members and officers are aware of potential conflicts of interest when performing their role for the Local Authority and the company.

4.15 The review will consider Brierley Group arrangements in relation to conflicts of interest.

d) External challenge to the Board

4.16 Previous failures that have affected Local Authority companies have often included a lack of understanding of roles and responsibilities, a lack of relevant skills and experience and conflict of interests. The CIPFA guidance notes that Non-Executive Directors can play a vital role in holding the executive to account for its performance in fulfilling its responsibilities through constructive challenge and scrutiny. As set out above, the Local Authority should always ensure that the scope for conflicts is minimised with a clear divide between those in such roles, and those responsible for holding them to account or overseeing them.

4.17 Non-Executive Directors make up part of the Board of directors of a company. They can bring vital expertise and different perspectives. Non-Executive Directors can include Members, officers and independent directors (who are external to the authority).

4.18 It is good practice to have some 'distance' between key authority decision makers and company decision makers.

4.19 The review will consider arrangements in relation to the involvement of Non-Executive Directors on the Boards of Brierley Group companies.

e) Business Planning

4.20 The success of commercial organisations is reliant in having strong leadership, a commercial culture, establishing a clear strategy and executing on that strategy. The strategy needs to take the form of a commercially focused business plan that details a clear roadmap signalling the companies' direction and aspirations for the future. Building up a successful company can take many years and requires plans that extend beyond a traditional one year cycle to allow the business to work iteratively towards medium to long term goals, under the guidance and direction of the board.

4.21 The CIPFA guidance explains that the subject of several failed Local Authority companies in case studies and public interest reports is through a lack of ongoing due diligence and weak or flawed business plans. A business case needs to be reviewed to ensure it adapts to the current circumstances or exploit opportunities in the market. Ultimately, the Local Authority need to ensure that the company is generating the intended outcomes, while acting in the public interest at all times.

4.22 The guidance highlights the importance of a strategic plan which brings together some of the key documents and it allows the reader to interpret and understand the current and future position against the business case and provides assurance to the Shareholder that a sound, well thought out and robust plan is in place to protect shareholder interests.

4.23 Current and future business planning arrangements will be considered as part of the review.

f) Shareholder Agreement

4.24 The CIPFA guidance recommends having a shareholder agreement in place for each company.

4.25 A shareholder agreement is a document that supplements the Company's articles of association. It is a contractual agreement between the company and the shareholder and is a private document (unlike the articles which are published). It sets out the rights of the Council as shareholder (or co-shareholder as appropriate). The articles form the overarching constitution for a company and are the legal document required to establish a limited company. However, the articles are a public document, therefore certain matters can be put into the shareholder agreement so that they remain private.

4.26 The shareholder agreement can be used to define the entity's risk management strategy, approve the limits for risk taking, and determining the criteria for internal control. This gives the company certain agreed parameters to work within and allows the company to challenge the level of risk averseness.

4.27 The review will consider arrangements in relation to Shareholder Agreements.

g) Post LGR Company review

4.28 A review of the principles contained within the CIPFA guidance will be carried out as part of the work being carried out by the Local Government Reorganisation (LGR) commercial workstream, it has highlighted a number of commercial interests held within the district and borough councils and districts and borough owned companies. As part of this workstream, a requirement for due diligence and a governance review of these companies has been identified. This shall take place post vesting day, and any such review shall take into account the CIPFA guide.

5.0 Next Steps

5.1 A review of the principles contained within the CIPFA guidance, current arrangements and recommendations for any proposed changes to the commercial governance environment arising from this review will be carried out as part of the work of the LGR Commercial workstream.

6.0 Recommendations

6.1 The Audit Committee is requested to note the contents of the report and agree to receive a further report post LGR.

Author of report: Vicki Dixon, Assistant Director Strategic Res

APPENDIX C

GOVERNANCE REVIEW CHECKLIST

GENERAL COMPANY COMPLIANCE

Does the company have detailed and appropriate articles of association? Are they teckal compliant (if appropriate)?
What is the company structure and is this structure appropriate? (eg. Teckal / Commercial) Has the company been set up correctly to reflect the structure?
Is a Shareholder Agreement in place and, if so, does it adequately define the entity's approach to risk management and internal controls? If not, is one necessary?
Is there a Service Agreement in place with the Council? If so, what services does the company provide to the Council and vice-versa. Are the Services Agreements adequate and are they effectively managed? Are there any other contracts in existence with previous Borough/District Councils which may need amalgamating with the Services Contract (eg. waste, property etc).
Are there written SLAs in place for back-office services provided by the Council? What services are currently provided by the Council and how are charges calculated and managed? Are support services provided to the company charged at full cost?
What Insurance does the company have in place? Does it hold insurance itself or are these part of the Council's policies?
What systems or ICT software is used by the company? Have the contracts for these services been reviewed recently?
Does the Company have a bank account?
Are the Company Statutory Books up to date?
Is all Webfiling up to date?
How does the Company report to the Council?
How often are the company accounts reviewed? Is an Annual Budget signed off? Does the Company have a long term financial strategy?
If a Teckal company: does it perform an annual Teckal test on its actuals and forecast to ensure compliance with 80:20% split of work
Does the company have employees?
What Company Policies are currently in place? • Finance • Procurement and/or contract procedure rules • Scheme of delegation
Does the company own or lease property?
What arrangements are in place for the preparation of statutory accounts and the calculation of corporation tax liabilities?

Does the Council have loan agreements with the company? What are the terms of the loan agreements and are the loans on commercial terms?
Do the review of the financial statements highlight any concerns (eg. potential liquidity issues, insufficient financial reserves)?
Are any Pension Fund subsumption agreements in place, which are underwritten by NYC?

ADDITIONAL CIPFA GUIDANCE COMPLIANCE

What internal and external audit controls are in place? Are the current audit arrangements deemed to be appropriate?
Conflicts: • Do any conflicts of interest get declared at Board Meetings as a standing agenda item? • Is there a policy for declarations and conflicts of interest within the company's articles of association? • Are Council appointed directors aware of potential conflicts of interests in their role as Director?
Does the Board membership include Non-Executive Directors or independent directors?
If a teckal company: Does the board contain a majority of Council appointed directors to ensure the "control" test is met?
Business Planning: Does the company have a minimum of 3 years of strategic business plan forecasting using an agreed format (standardised across all companies)? Covering the following matters: • Financial projections – Historic against business case / approved budget, future forecasts • SWOT analysis • Risk register • Capital / Investment plans • Product / service development • New business proposals / pipeline • Technology Roadmap • Workforce planning
What is the company's approach to risk management, and what processes and procedures are in place to manage and monitor risk? Are the risk management approaches deemed to be appropriate given the levels and types of risks facing the organisation?
Have Council appointed Directors been adequately trained / are they sufficiently knowledgeable on their roles and responsibilities as a company Director?