

North Yorkshire Council

Shareholder Committee

19 March 2024

Commercial Governance Review

Report of the Corporate Director, Resources.

1.0 PURPOSE OF REPORT

- 1.1 To provide an analysis of how Council owned companies are governed using best practice for commercial governance as a guide as 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 provides an update to the Commercial Governance Review report presented to the Audit Committee on 11 December 2023.

2.0 SUMMARY

- 2.1 A review of governance of companies has been undertaken taking into consideration CIPFA good practice guidance. This report sets out the findings of the review and considers - where applicable - standardized approaches to governance between companies following local government reform. The recommendations identified from the review are laid out in the report. The guidance from CIPFA is welcome but it should be seen in the context of ensuring sound decision making and it is therefore suggested that it should not be taken as definitive in all cases. For example there is a risk that potential conflicts of interest lead to a distancing of company and shareholder objectives.
- 2.2 Pleasingly, the outcome of the review shows that the Council's governance and reporting structures surrounding commercial entities are largely compliant with the CIPFA guidance and are deemed to be robust and appropriate for each company.

3.0 BACKGROUND

- 3.1 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)

These companies are referred to as the “Brierley Group”. 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 significant oversight for NYC through regular meetings of the Brierley Board. An updated structure of all the Council owned companies is at **Appendix A**.

3.2 The governance structure for the Brierley Group is tiered into multiple levels:

- (a) Executive
- (b) Shareholder Committee & Shareholder Representative
- (c) Brierley Board
- (d) Individual Company Boards

3.2.1 Each tier within this hierarchy has a different responsibility and performs a different role regarding the governance of the Brierley Group companies.

3.2.2 Brierley Board is an advisory board made up of the members of the Shareholder Committee and senior Council officers (including in particular, the Chief Executive, Corporate Director, Resources and Assistant Chief Executive Legal and Democratic Services). Brierley Board reviews quarterly financial and company updates. The companies are each invited to an annual “deep dive” where detailed discussions take place with the managing director from each respective company. The Brierley Board acts to assist the Shareholder Committee and also receives reports from each company on behalf of the Council as shareholder/member.

3.2.3 The Council’s Shareholder Committee is a committee of the Executive established to provide oversight of the Council’s company interests in accordance with any principles agreed by Council and provisions contained within any shareholder and company member agreement. The Shareholder Committee and Shareholder Representative exercise the powers and responsibilities of the Council as a shareholder or member of each company in accordance with the Shareholder Committee Delegation of Decision Making. The Shareholder Representative, currently the Council’s Chief Executive, is authorised to take certain decisions on behalf of the Council. The Shareholder Representative is also the person who can sign documents on behalf of the Council as a corporate body. Certain decisions are reserved to the Executive.

3.3 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 entitled “Local Authority Owned Companies – A good practice guide 2022 edition”.

3.4 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.

3.5 In December 2022 North Yorkshire County Council’s Audit Committee were presented with a Commercial Governance Review report, and an update report covering the Review was presented to Audit Committee in December 2023. Those reports highlighted the best practice guidance set out in the CIPFA publication and 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 and December 2023 reports.

3.6 In recent years there has been many instances where Local Authority trading companies have failed or fallen into decline. Successive years of reduced funding from central government have exposed underlying flaws in Local Authority business models, exposing the relevant Council to financial stress, reputational damage and questions around its leadership. Grant Thornton published lessons learned from the 2020 and 2021 Public Interest Reports. Some recurring themes are:

- Inappropriate or weak governance
- Political agenda with no scrutiny and challenge
- Lack of adequate skills and commercial acumen
- Roles and responsibilities unclear
- Failure to understand, identify and mitigate the risks (current and emerging)
- Lack of ongoing due diligence, failure to understand market complexities
- Weak or flawed long term Business Plans

3.7 The Brierley Group has paid considerable attention to setting up a strong system of governance and creating a commercial culture that is open to scrutiny and challenge that promotes the success of the companies. The Council is prudent and proactive in taking appropriate care of its resources and carefully managing its exposure to risk. The review found that the companies have good control and due diligence to mitigate the points listed in 3.6. The companies demonstrate strong and effective controls in order to create sustainable and enduring shareholder value to the Council.

4.0 CIPFA COMMERCIAL GOVERNANCE REVIEW FINDINGS

4.1 A Commercial Governance Review Group was established to review the council owned companies; using the CIPFA guidance as a framework to assess existing arrangements. The Review Group included representatives from the Council's legal and finance team, who undertook detailed reviews alongside each company that is actively trading.

4.2 A "checklist" was 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 B**.

4.3 The Review Group met with a total of 10 companies. It did not meet with the following companies due to their proposed imminent closure and/or dormant status:

- Central Northallerton Development Company Limited – This company is a Joint Venture that was established by Hambleton District Council to progress the Treadmills Development in Northallerton. The development is now complete and the only trading activity within the company relates to the operation of the Crosby Road car park on the development site. The Council and its Joint Venture partner are reviewing options that will allow trading activity to cease and allow the JV to be dissolved / closed within the next twelve months.

Hambleton District Holdings Limited and associated Maple Park (Hambleton) LLP – Work is underway to review options to bring the Maple Park (crematorium) operation in-house for the 2024/25 financial year, which will negate the need for these entities and, if agreed, will result in them being closed or remaining dormant.

- Mercury Housing Company Limited – this company is currently dormant.

5.0 RECOMMENDATIONS FOR IMPROVEMENTS

The intention of this report is to “report by exception” and detail the areas that were identified through the governance review. Pleasingly the review showed that the Brierley Group entities are largely compliant with the CIPFA Guidance and the overall governance structure and reporting procedure to the Council is deemed to be robust and appropriate. The areas identified for improvement within the review are set out in the sections below.

5.1 Conflicts of Interest

5.1.1 The company boards contain a mix of executive and non-executive directors. All of the companies have Council officers appointed as non-executive directors, and some also have councillors appointed as non-executive directors. The CIPFA guidance suggests having a policy for declarations and conflicts of interest within each company’s articles of association. This is something which the companies currently do and conflicts are generally declared as a standing agenda item at board meetings. Directors also 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.

5.1.2 The guidance sets out that the Council should minimise the potential for conflicts of interest within its companies and ensure potential conflicts are identified and managed appropriately. Careful consideration should be given as to the representation of the Council on the Company boards of directors. This is of particular importance for Council officers as the potential for conflicts of interest may be greater where council appointed directors fulfil a client / commissioning role on behalf of the Council and/or where directors are also the Council’s statutory officers. Where this is the case, it is recommended (and often implemented) that Council officers delegate their responsibilities when acting as the client.

5.1.3 Having senior Council officers as directors of companies can improve the shareholder value of the companies through the contribution of relevant knowledge, skills and expertise as well as the officer’s duty to promote the success of the company. It can help to ensure that the priorities of the Company and the Council are aligned and are ultimately ensuring best value for the public purse. As a director, the officer should consider their wider role in relation to the aims and objectives of the company to ensure that the council is getting best value as the shareholder. This could be through service provision of the company, utilising the Council’s services or through income generation.

5.1.4 Due to recent updates to the board members following LGR, there are some companies and directors who have received recent training. However, not all company directors have received recent training to support their roles and duties. Best practice guidance recommends that regular training is provided to ensure directors and company management teams have appropriate knowledge and experience. This includes training to clarify roles and responsibilities, and sector specific training to promote a deeper understanding of the specific challenges and issues facing the relevant company.

5.1.6 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. The Council has a policy within its constitution in relation to appointments to companies. However, this could be reviewed and additional guidance prepared.

- **Recommendation:** to require all companies to include conflicts of interest as a standing agenda item at board meetings.
- **Recommendation:** to develop an in-depth policy for dealing with conflicts of interest for all directors and in particular Council appointed directors. This will supplement the current policy in the constitution.

- **Recommendation:** for all directors to provide annual declaration of interests and for all companies to keep an up-to-date register of interests.
- **Recommendation:** for all companies and directors to undergo refresher training relating to their roles and responsibilities and Directors Duties and how this may interact with their obligations and roles within the Council.

5.2 Elected Members on Boards

5.2.1 Where councillors are appointed to a board the CIPFA guidance sets out that conscious thought should be given as to ensuring that they hold the required skills, knowledge and experience to fulfil the roles. The guidance also cites that the inclusion of elected members on boards could have a negative impact on council decision-making where councillors subsequently need to withdraw from committees due to conflicts of interest and there can be risks to continuity if councillors lose their positions if not re-elected. It should be noted that the guidance does not positively prohibit Councillors sitting on Council Boards and the Council is free to have regard to but deviate from the guidance if it considers it appropriate.

5.2.2 The current companies that have elected members on the board are: Yorwaste Limited, Veritau Limited, Nynet Limited and Central Northallerton Development Company Limited. Elected Member oversight of companies is provided within the Brierley Group's governance structure via the Shareholder Committee and Brierley Board. On that basis, and subject to the exception set out in paragraph 5.2.3 below, it is recommended that the appointment of Elected member representatives to company boards be reviewed, and where appropriate elected members stand down from company boards. Relevant elected members could still be offered the opportunity to attend board meetings as observers where this is deemed to be appropriate.

5.2.3 Veritau and Yorwaste are both jointly owned between North Yorkshire Council and City of York Council. Therefore, elected member directorships are deemed appropriate where City of York elected members also sit on the board. Where possible the board memberships of these companies will be reviewed together with City of York Council.

- **Recommendation:** that the board membership for companies is reviewed and consideration given to whether Elected members should stand down as directors (except Veritau and Yorwaste) on the basis that the Shareholder Committee provides the elected member oversight of commercial entities and that potentially 'observer' status could be offered to Councillors on the relevant Boards.

5.3 Business Plans

5.3.1 A business plan is the internal document which helps to lay out the future strategy of the company. This is not the same as any annual reporting which is for public consumption.

5.3.2 Every company requires a business plan to enable the company to plan effectively. Business plans are presented to Brierley Board annually for review and challenge. The majority of companies do have an annual business plan but the review identified that the content is variable. Whilst it is recognised that there will be variations in business plans from company to company (so a standardised format is not proposed) there are a number of areas of key content which it is felt should be included in every business plan.

- **Recommendation:** to ensure that each business plan contains the following information unless there are very specific reasons not to:-
 - Minimum of 3 future years financial forecasting including details of any key assumptions.

- Opportunities
- Risks
- Pipeline of work
- Major developments
- Key performance indicators
- Teckal test results (where applicable)

5.4 Back Office Service Level Agreements (SLAs)

5.4.1 The majority of our companies rely on and buy from the Council the support service functions they need, e.g. finance, HR, legal, payroll, admin, accommodation, etc. These arrangements have developed over time on an ad-hoc basis and vary from company to company. In some cases no formal agreements (in the form of an SLA document) can be found between the company and the Council. Having formal SLAs in place would better reflect the commercial nature of the arrangements, help to clarify the expectation of the two parties and provide a definitive path to resolving disputes should any issues arise.

5.4.2 In addition, it may be beneficial to put in place an SLA framework of overarching terms and conditions encompassing all support services for all companies. From the Council's perspective it would avoid any unnecessary variations in the support the companies receive, and for the companies it could be more efficient to monitor and manage.

- **Recommendation:** a phased approach to implementing the recommended changes – in 2024, to review and refresh the back office SLAs for financial year 2024/25, documenting the agreed charges in advance and the details of service to be provided; next year to put in place the SLA framework with standardised terms and conditions.

5.5 Audit

5.5.1 An audit exemption can be applied for companies where two of more of the following apply:-

- Turnover of less than £10.2m
- Assets worth less than £5.1m
- 50 or fewer employees.

However, a company may require an audit for reasons of reassurance or due to the industry that they operate in. Currently only Yorwaste and NY Highways require an audit by law. Of the other companies, the majority conduct full audits with a small number having limited or no audits.

5.5.2 There are three options for each of the companies that do not meet the criteria to have a mandatory audit:-

- No audit (or internal independent audit conducted)
- Medium audit
- Full audit (an audit on the same level as NYC)

At present all of the companies either have a full external audit or no audit. The current external audit provider has offered the opportunity of a 'medium' audit. Discussions are taking place to understand the implications of this and the differences between that and a full audit, so that impacts on assurance and resources can be assessed. Once this is fully understood, a proposal will be considered as to what level of audit is appropriate for each company.

- **Recommendation:** that work is undertaken to review each entity and agree the level of audit required in line with their requirements and complexity, which ensures there is a balanced approach whilst providing the necessary assurance for company directors, as well as the Council as shareholder.

5.6 Teckal Testing

5.6.1 Some companies are known as “teckal” companies. These are companies that comply with the provisions of Regulation 12 of the Public Contracts Regulations 2015. The Council is able to award work to its teckal companies without the need for a procurement procedure. As part of the teckal exemption, teckal compliant companies are required to undertake at least 80% of its work for the controlling authorities. i.e. 80% of that company’s turnover for the rolling three-year period must be for the Council (or joint councils where appropriate). Therefore, up to 20% of turnover can be delivered from external commercial activity. This is taken as a rolling three-year test and is sometimes referred to as the 80:20 test.

5.6.2 There have been some inconsistencies in the approach and timing of teckal testing within the Brierley Group’s teckal entities. All teckal companies should calculate annually that they remain within the 80:20 rule on a rolling three-year basis. This should then be reported in the business plan.

5.6.3 Teckal companies should ensure they have appropriate Procurement and Contract Procedure rules in place and seek appropriate Procurement and Legal support.

- **Recommendation:** All teckal companies to complete annual teckal calculations and report these calculations within their business plan.

5.7 Risk Registers

5.7.1 There has been an inconsistent approach to risk registers between the companies. Most companies have a risk register but in some instances they were out of date or not subject to reviews throughout the year. It is suggested that risk registers are updated at least annually, with the risk register being included in the business plan. The format of the risk register is not prescriptive as different approaches may be relevant to each company. Risk registers should be monitored periodically through the year as part of company board reporting to ensure no major issues.

- **Recommendation:** Complete annual risk register reviews and include the risk register within the business plan. Company Boards to monitor and review risk registers periodically during the year.

5.7 Other matters

It should be noted that certain gaps were identified in the review of Bracewell Homes’ governance arrangements, therefore additional work is required to be put in place to ensure that arrangements are consistent with other NYC companies and the CIPFA best practice guidance. Examples of gaps identified in the review include a lack of audit arrangements, lack of formally drafted support service arrangements, and lack of a risk register and formal risk management arrangements.

5.8 Although gaps have been identified it should be noted that this is predominantly reflective of the fact that the activities undertaken by Bracewell Homes are particularly low risk in nature from a commercial perspective. The review confirmed that there are no significant financial risks associated with the company, or any areas that would be deemed to cause potential reputational risk for the Council; and the company is financially sound and makes strong

financial returns. A review of Bracewell homes is currently taking place to determine whether its operations and assets could be insourced to the Council. The officers responsible for the company are keen to address the issues identified in the governance review and the majority of issues identified have either already been addressed or are currently being actioned and will be addressed imminently.

- **Recommendation:** for the governance arrangements for Bracewell Homes to be updated to ensure consistency with other Brierley Group entities and the CIPFA best practice guidance.

6.0 FINANCIAL IMPLICATIONS

6.1 There are no financial implications arising from this report. The review did not highlight any issues which would indicate that the financial standing of any of the entities is of concern.

7.0 LEGAL IMPLICATIONS

7.1 The legal implications of the recommendations in this report are set out against the relevant recommendation.

8.0 EQUALITIES IMPLICATIONS

8.1 Not applicable

9.0 CLIMATE CHANGE IMPLICATIONS

9.1 Not applicable

10.0 REASONS FOR RECOMMENDATIONS

10.1 The recommendations in the report are made to ensure the appropriate level of governance is maintained in all commercial companies considering CIPFA guidance and also to ensure there is a consistent approach to governance post local government reorganisation.

11.0 SUMMARY OF REPORT RECOMMENDATIONS

- To require all companies to include conflicts of interest as a standing agenda item at board meetings.
- To develop an in-depth policy for dealing with conflicts of interest for all directors and in particular Council appointed directors. This will supplement the current policy in the constitution.
- For all directors to provide annual declaration of interests and for all companies to keep an up-to-date register of interests.
- For all companies and directors to undergo refresher training relating to their roles and responsibilities and Directors Duties and how this may interact with their obligations and roles within the Council.
- That the board membership for companies is reviewed and consideration given to whether Elected members should stand down as directors (except Veritau and Yorwaste) on the basis that the Shareholder Committee provides the elected member oversight of commercial entities.
- To ensure that each company business plan contains the following information unless there are very specific reasons not to:-
 - Minimum of 3 future years financial forecasting including details of any key assumptions.
 - Opportunities

- Risks
- Pipeline of work
- Major developments
- Key performance indicators
- Teckal test results (where applicable)
- A phased approach to implementing the recommended changes to Back Office Service Level Agreements.
 - In 2024, to review and refresh the back office SLAs for financial year 2024/25, documenting the agreed charges in advance and the details of service to be provided;
 - 2025/26 to put in place the SLA framework with standardised terms and conditions.
- That work is undertaken to review each entity and agree the level of audit required in line with their requirements and complexity which ensures there is a balanced approach whilst providing the necessary reassurance.
- All teckal companies to complete annual teckal calculations and report within the business plan.
- All companies to complete annual risk register reviews and include the risk register within the business plan; with the register being monitored periodically during the year.
- For the governance arrangements for Bracewell Homes to be updated to ensure consistency with other Brierley Group entities and the CIPFA best practice guidance.

12.0 RECOMMENDATIONS

12.1 Shareholder Committee are requested to:

- i) approve the recommendations as set out in each section of the report and as summarised in paragraph 11;
- ii) delegate the approval of the new conflicts of interest policy to the Assistant Chief Executive – Legal and Democratic Services; and
- iii) delegate all other necessary steps to secure the implementation of all other recommendations set out in this report to the Corporate Director, Resources.

APPENDICES:

Appendix A – Company Structure Post LGR
Appendix B – Company Compliance Checklist

BACKGROUND DOCUMENTS:

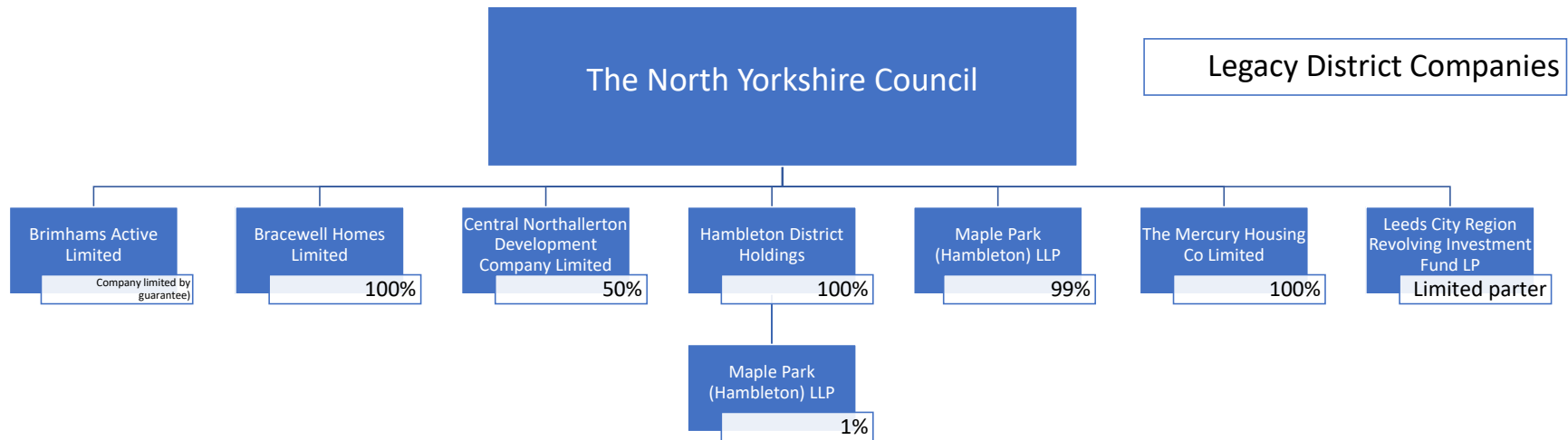
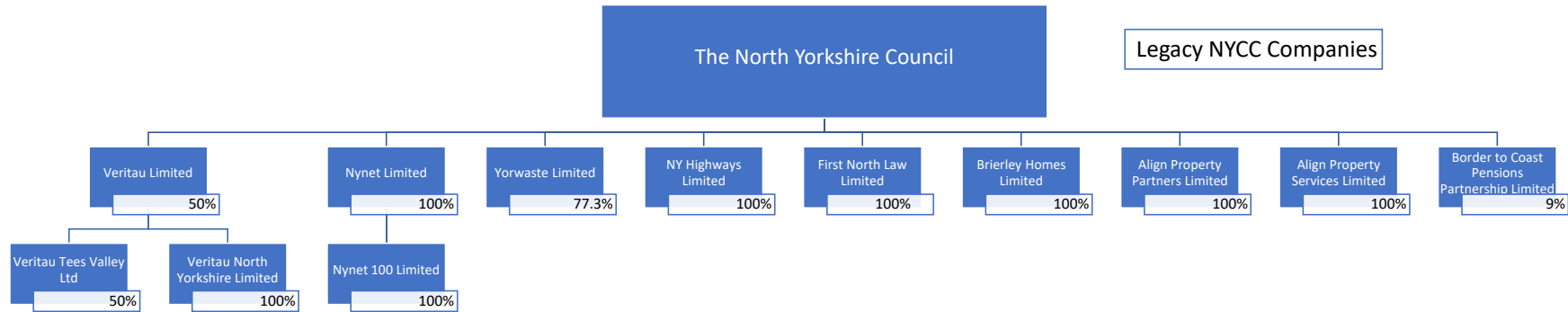
CIPFA Guidance

Gary Fielding
Corporate Director – Resources
County Hall
Northallerton
(7 March 2024)

Report Author – *Peter Williams, Head of Finance, Qingzi Bu, Senior Accountant 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
COMPANY STRUCTURE POST LGR**



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 and 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? <ul style="list-style-type: none"> • 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 there 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?
<p>Conflicts:</p> <ul style="list-style-type: none"> • 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?
<p>Business Planning:</p> <p>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:</p> <ul style="list-style-type: none"> • 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?