



SCRUTINY COMMITTEE

Thursday, 26 January 2023

Subject	Review of Governance Arrangements for the Council's Local Authority Trading Company (LATCO) Group Structure
Report by	Councillor Steve Gallant, Leader
Supporting Officer	Andrew Jarvis Strategic Director andrew.jarvis@eastsuffolk.gov.uk

Is the report Open or Exempt?	OPEN
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Wards Affected:	All Wards
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Purpose and high-level overview

Purpose of Report:

Scrutiny Committee requested a review of governance arrangements for the Council's LATCO group structure.

Recommendation/s:

That the Scrutiny Committee consider this report.

Corporate Impact Assessment

Governance:

This report focuses on governance arrangements and therefore covered within the main body of the report.

ESC policies and strategies that directly apply to the proposal:

East Suffolk Strategic Plan

East Suffolk Medium Term Financial Strategy

Environmental:

Environmental issues were considered in the creation of each of the Council's LATCOs. Part of the strategic case for the establishment of East Suffolk Services for example was the closer control that this would give East Suffolk Council to deliver against a range of current and future policy initiatives.

Equalities and Diversity:

There are no impacts.

Financial:

There are no financial implications arising directly from this report.

Human Resources:

There are no HR implications.

ICT:

There are no ICT implications.

Legal:

Legal advice on the establishment and governance of the Group has been provided initially by Trowers and Hamlin and since the Autumn of 2021 by Bevan Brittan LLP, with support from the Council's in-house commercial lawyers.

Bevan Brittan have expertise in Local Government Law, and specifically Local Authority Trading Companies.

Risk:

The operation of a group of companies inevitably involves acceptance of an element of risk. In particular, risk in relation to the financial performance of those companies. Each

company requires a Business Case to be approved by Cabinet and that document sets out any specific risks relating to that company.

External Consultees: None.

Strategic Plan Priorities

Select the priorities of the Strategic Plan which are supported by this proposal: (Select only one primary and as many secondary as appropriate)		Primary priority	Secondary priorities
T01	Growing our Economy		
P01	Build the right environment for East Suffolk	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P02	Attract and stimulate inward investment	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P03	Maximise and grow the unique selling points of East Suffolk	<input type="checkbox"/>	<input type="checkbox"/>
P04	Business partnerships	<input type="checkbox"/>	<input type="checkbox"/>
P05	Support and deliver infrastructure	<input type="checkbox"/>	<input checked="" type="checkbox"/>
T02	Enabling our Communities		
P06	Community Partnerships	<input type="checkbox"/>	<input type="checkbox"/>
P07	Taking positive action on what matters most	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P08	Maximising health, well-being and safety in our District	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P09	Community Pride	<input type="checkbox"/>	<input checked="" type="checkbox"/>
T03	Maintaining Financial Sustainability		
P10	Organisational design and streamlining services	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P11	Making best use of and investing in our assets	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P12	Being commercially astute	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P13	Optimising our financial investments and grant opportunities	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P14	Review service delivery with partners	<input type="checkbox"/>	<input checked="" type="checkbox"/>
T04	Delivering Digital Transformation		
P15	Digital by default	<input type="checkbox"/>	<input type="checkbox"/>
P16	Lean and efficient streamlined services	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P17	Effective use of data	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P18	Skills and training	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P19	District-wide digital infrastructure	<input type="checkbox"/>	<input type="checkbox"/>
T05	Caring for our Environment		
P20	Lead by example	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P21	Minimise waste, reuse materials, increase recycling	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P22	Renewable energy	<input type="checkbox"/>	<input checked="" type="checkbox"/>
P23	Protection, education and influence	<input type="checkbox"/>	<input checked="" type="checkbox"/>
XXX	Governance		
XXX	How ESC governs itself as an authority	<input checked="" type="checkbox"/>	<input type="checkbox"/>

How does this proposal support the priorities selected?

Commercially Astute/Business Partnerships

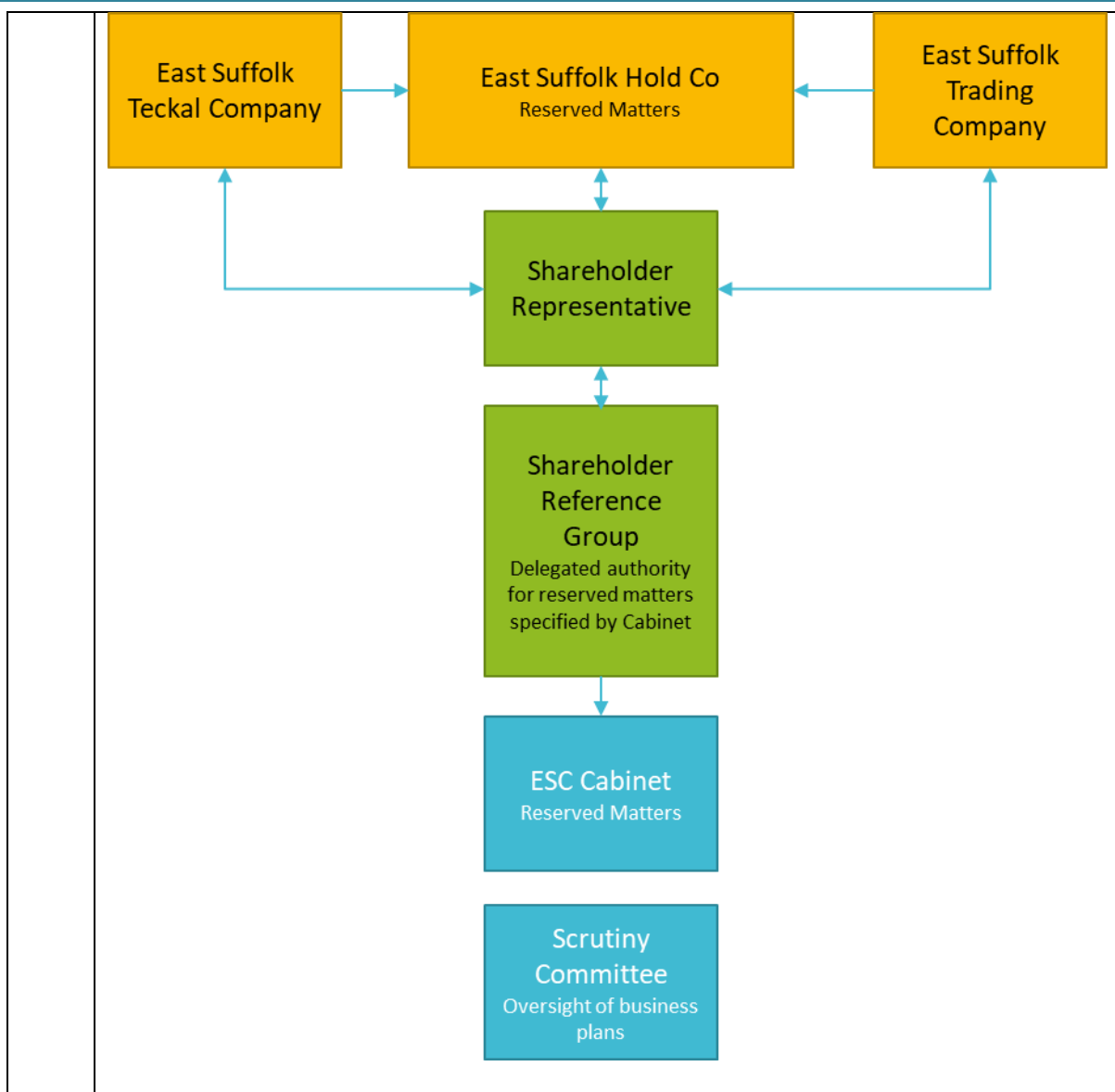
The Joint Venture model entered into by the Council as the means of delivering its Waste Management, Street Scene/Grounds Maintenance and Facilities Management service over the past fifteen years was a successful model for some time, providing the expertise and capacity to deliver a quality service. However, this has reduced with the passage of time and the need now is for a model that will give the Council greater flexibility and control.

Additionally, creating a group of linked property development, maintenance and management companies will enable the Council to deliver a more ambitious development and regeneration agenda and in a way that will enable greater benefits for the Council and local communities. A robust Shareholder Agreement provides the Council with greater control over the strategic direction and priorities of those companies.

Background and Justification for Recommendation

1	Background facts
1.1	<p>The Council has established a number of companies, within a group structure including East Suffolk Holdings Limited (ESHL), East Suffolk Services Limited (ESSL), East Suffolk Property Investments Limited (ESPIL), East Suffolk Property Developments Limited (ESPDL) and East Suffolk Construction Services Limited (ESCSL).</p>
1.2	<p>Each of these companies has been incorporated but in order to become active required a Business Case to be prepared for and approved by Cabinet.</p> <p>Those business cases set out the strategic, economic, commercial and financial case for creating and activating the company in question.</p> <p>In the case of ESSL, currently the Council's largest company, a detailed review and options appraisal was carried out identifying the preferred option of creating a LATCo to take over the services currently delivered by a joint venture arrangement with Norse Commercial Services Ltd. This was approved in principle beforehand by Cabinet ahead of the full business case being prepared.</p> <p>The business cases for the property companies provided detailed frameworks for the way the individual companies will operate and will be followed in due course with project specific business cases as individual property purchase or site developments are brought forward.</p>
1.3	<p>Shareholder Agreement</p> <p>The Council has some rights over the decisions of its companies through the Articles of Association of those companies. However, Cabinet has entered into a Shareholder Agreement (SA) with its group companies in order to strengthen the degree of control that the Council has in this regard.</p> <p>The SA sets out how the Council can monitor and control the business and operations of each company. through the Reserved Matters, through receiving periodic reports, through its Directors on each Board and through information received following ad hoc information requests made of the relevant Company.</p> <p>In particular, the SA:</p> <ul style="list-style-type: none"> • provides a broad description of the business to be conducted by the holding company of the Council's group of companies and each company in the group (referred to as "SPV") (clause 2); • requires the production of a Business Plan for each group company, to be produced for a three-year period and updated annually (clause 3);

	<ul style="list-style-type: none"> • requires the Council's Holding Company to produce a Consolidated Business Case, which will include the full Business Case for each Teckal Company and a summary Business Case for other group companies (clause 3.3); • gives the Council and those acting under its delegated authority (which will include the Shareholder Reference Group, discussed at 1.4 below) unlimited, unrestricted and prompt access to company information and documents (clause 4.3 and 5.8); • gives the Council or its Holding Company (as applicable) approval rights in respect of "Reserved Matters" (clause 5 and Schedule 1). Reserved Matters are proposed actions of a group company that are considered sufficiently important (for example because of their value) that the Council should have the right to decide whether the action is taken. <p>The Council's group companies will sign up to the SA. If they are not signatories at the outset, they will do this by means of a "deed of adherence" which commits them to comply with the terms of the shareholder agreement.</p> <p>A copy of the full SA can be found at Appendix A.</p>
1.4	<p>Shareholder Reference Group</p> <p>The Council has a watching brief as shareholder to ensure its investment and policy objectives are being delivered by the company. A sub-committee of Cabinet, known as the Shareholder Reference Group (SRG) has been set up, and is referred to throughout the SA. The SRG will undertake the functions of the Council as shareholder/ultimate owner of its group of companies and exercise the Council's rights under the Articles of Association of each company and under the SA, except for any rights which the Cabinet or Leader reserves to itself/himself from time to time or which can only be exercised by Full Council. The SRG will, amongst other things, make decisions on "Reserved Matters". The Terms of Reference for the SRG are in the Constitution and can be found at Appendix B.</p>
1.5	<p>The image below, sets out a simplified group structure and reporting lines. ESSL is known as a Teckal company and ESHL, ESPIL, ESPDL and ESCSL are known as Trading companies (LATCos).</p> <p>A Teckal company is a company which can be awarded contracts for works, services or supply from its controlling public sector owner (ie. ESC) without having to go through a competitive tender process.</p> <p>The Teckal company must be "inwardly and not outwardly focused". The Teckal 'rule' requires that at least 80% of the activity of the Teckal company – that is, at least 80% of its turnover – must be for its public sector owner).</p>



2 Current position

2.1 The specific lines of enquiry that Scrutiny Committee are interested in, are set out below with a response.

2.2 **What is considered to be best practice in terms of governance arrangements for these type of Council LATCos?**

The Council has taken a carefully considered approach to designing the governance arrangements for its LATCo Group. Advice has been taken from Trowers Hamlin and Bevan Brittan based on their expertise and previous experience. Advice has also been provided by consultants from the East of England Local Government Association Talent Bank and sought from other LATCos elsewhere.

The Chartered Institute of Public Finance and Accountancy (CIPFA) has recently published a 'good practice guide' for local authorities when establishing private trading companies. The Head of Internal Audit subsequently commissioned CIPFA to analyse the governance arrangements, specifically for ESSL. Overall, CIPFA agreed that the Council's arrangements for the East Suffolk group of companies are in line with the principles of good governance as at July 2022. A copy of their findings is available at Appendix C. Recommendations were made, which have in the main been addressed and referred to in Appendix D.

2.3	<p>How in control of the Companies is the shareholder/owner? What controls are exercised in the Articles and Shareholder Agreement?</p> <p>The Council will principally control the business and operations of each company through the Reserved Matters in the SA which ESHL or Cabinet/SRG will determine</p> <p>The full list of Reserved Matters (27 in total) is set out in Schedule 1 of the SA. In most of these matters identified as Cabinet decisions, the SRG have been given delegated authority to exercise the Council's rights. The key right reserved to Cabinet is approval of the Consolidated Business Plan.</p>
2.4	<p>Who is the main responsible person / persons? Are they Members / Officers of both?</p> <p>Each of the Council's companies has/will have a Board of Directors. The Board is/will be composed of Company Directors (including the Council's Strategic Directors), and one or more external Non-Exec Directors. While on the Company Board the Council's Strategic Directors are required to act in the best interests of the company, but they will clearly bring with them knowledge and insight of the Council's culture and objectives.</p> <p>The Board of Directors is the company's decision-making body, responsible for the company's activities, its prosperity and future. Decision making and leadership will come from the Board of Directors.</p> <p>The Council has also appointed a SRG and SR (the Leader of the Council), to act as its authorised representative in accordance with the constitution. The SR has the right to attend and observe the relevant Board of Director meetings but cannot speak or vote at the Board meeting.</p> <p>As set out in 1.3 and 2.3 above, the SRG which as a committee of Cabinet is made up entirely of Cabinet members and has been set up to exercise certain oversight and control over the company for the Council as shareholder.</p>
2.5	<p>What scrutiny / involvement arrangements will be in place from a Member and Officer perspective?</p> <p>Once a year, Scrutiny Committee will review the business cases that are proposed by the Council's companies.</p> <p>The Audit and Governance Committee shall receive reports from the independent Head of Internal Audit upon governance arrangements between East Suffolk Council and its Local Authority Trading companies. Such reports are expected to be biennial.</p> <p>Officers will work with the Committee clerk to determine the best time of the financial year to carry out the reviews.</p>
2.6	<p>What liabilities will the Council have?</p> <p>The companies within the Council's group structure have been incorporated as limited companies. A shareholder's liability for a limited company will usually be limited to the amount of its investment. Therefore, it is important that the Council is satisfied that the companies have sound business cases and plans in place, monitors the performance of the companies and that the Council carries out necessary and appropriate due diligence enquiries before providing loans/funding to the companies to protect the Council's investments, and the taxpayer.</p>

2.7	<p>How will the Council mitigate any risk to the taxpayer of a failing LATCO?</p> <p>The Council has taken a very considered and cautious approach to setting up its LATCo Group. Each company has its own business case which has been prepared by a range of officers from different disciplines and has been considered and approved by Members. Each company will produce its own business plans that will be considered by the SRG and will be available for scrutiny.</p> <p>The companies have been designed and set up to produce in the fullness of time a net return for its shareholder and so there will be a robust performance management to ensure things stay on track. At any point the Council as 100% owner will be able to invest in the company/ies or alternatively, should it so decide, to sell one or more of them or indeed wind them up.</p> <p>ESSL, the Council's Teckal company will sign up to a contract and heads of terms. This and the other governance measures mentioned above will mean the Council has more influence over the culture of the company and the standard of service delivered, than it would have via any other model, except perhaps full in-house delivery – which presents a whole set of other challenges. In terms of the Waste/street scene contract specifically, the Council has reviewed its contract management arrangements and there is now confidence that it has the tools and resources necessary to manage the contract effectively.</p>
2.8	<p>What training will Officers and Members be required to undertake to ensure that a LATCO operates efficiently and robustly?</p> <p>The Council appointed Directors for ESHL and ESSL have received training, delivered by Bevan Brittan, setting out their duties, and requirements in relation to corporate governance.</p> <p>A similar session for the appointed Members of the SRG was carried out in the summer 2022. Following the Elections in May 2023, a further session will be arranged for any new Members of the SRG in advance of their first meeting.</p>
2.9	<p>Will transparency be maintained in an area of commercial confidentiality? Will councillors be entitled to confidential information about the LATCO, in the same way as they are about general council business?</p> <p>Section 14 of the SA covers confidentiality. A relevant extract from the SA is set out below:</p> <p>“Any Director may at any time discuss the affairs, finances and accounts of the Company with any Council as ultimate shareholder (and any person acting with delegated authority on its behalf). All books, records, accounts and documents relating to the business and the affairs of each Company (collectively Relevant Information) shall be open to the inspection of the Council or any such person acting with that delegated authority, who shall be entitled to make any copies of that Relevant Information as it, he or she deems appropriate to keep the Council properly informed about the business and affairs of each Company or to protect its interests as ultimate owner of each Company. The Council or any person acting with delegated authority on its behalf may share Relevant Information to others within the Council where there is an established need to know. Any confidential information secured as a consequence of such discussions and examinations shall be kept confidential by the Council and such person(s) as receive it in accordance with the terms of clause 14.”</p>

	Following on from the above, it is considered that Councillor access to confidential information will broadly follow current practice, namely that any person acting with delegated authority on the Council's behalf may share Relevant Information to others within the Council where there is an established need to know. And that, any confidential information secured so provided will be kept confidential in accordance with the terms of clause 14 of the SA.
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3 How to address current situation

3.1	It is considered that there are a robust set of governance arrangements in place to ensure that the governance of the Council's LATCo Group accords with best practice.
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4 Reason/s for recommendation

4.1	This report is intended to provide an overview and reassurance for the Scrutiny Committee as to the robust governance arrangements in place for the Council's group companies. Expert external advice has been sought and this advice is reflected in the best practice governance arrangements the council has put in place for the group companies to protect the Council and the taxpayer.
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Appendices

Appendices:

Appendix A	Shareholder Agreement
Appendix B	Terms of Reference for the Shareholder Reference Group
Appendix C	CIPFA Report (Exempt)
Appendix D	CIPFA Recommendations

Background reference papers:

Date	Type	Available From
June 2021	ESSL Business Case	CMIS
September 2022	ESHL Business Case	CMIS
November 2022	ESPIL Business Case	CMIS
January 2023	ESPDL Business Case	CMIS