

Report of the Chief Executive

Public Interest Report – City of York Trading Ltd

Summary

1. This report is submitted in response to the Public Interest Report (PIR) issued by Mazars LLP, the council's external auditor, on 26th February (attached at Annex 1). The council is legally required to consider the report and recommendations within one month of issue.
2. In summary, the Auditor's conclusions were :
 - that there were failings in governance by the Council;
 - action is now needed to regularise the position in relation to remuneration in March 2015 made by City of York Trading Limited (CYT) to two of its executive directors who are also officers of the Council; and
 - important governance lessons should be learned and applied to ensure future good governance of the Council's relationships with its trading companies.
3. The Public Interest Report makes 10 specific recommendations and these are set out within this report. Council is asked to note the actions that have either been taken or are planned in order to address the Auditor's recommendations.

Background to CYT

4. There were two reports to CYC's Cabinet seeking to authorise the establishment of City of York Trading Limited. The first was presented on 15 February 2011 and this authorised the creation of the company with the objective of providing business support activity to public sector and other organisations. The company was to be formed as a trading company with a number of Council Officers appointed as directors on the board, including the:
 - Director of Customer and Business Support Services (CBSS) who was to act as Chief Executive;

- Assistant Director Financial Services, to act as Head of Finance for the company;
 - Assistant Director of CBSS for Customers and Employees, who would have responsibility for staffing matters; and
 - The Assistant Director Governance and Legal to act as Company Secretary.
5. On 4 October 2011 the Cabinet formally authorised the creation of CYT, the approval of the business case and the general principles of governance and operation as set out in the report and the five Annexes.
 6. In addition to the previously reported directors, as set out above, the Cabinet Member for Corporate Services was nominated to serve as a director (non-Executive) on the Board and to act as Chairman. The same Cabinet Member was authorised to approve the final Articles of Association and the Leader of the Council was authorised to agree and sign off the Shareholder Agreement.
 7. The Cabinet also approved the establishment of a Shareholder Committee, to be made up of the Leader of the Council and two other members of CYC chosen by the Leader. The purpose of the Shareholder Committee, as resolved by the Cabinet on 4 October 2011, was:
 8. *"to properly exercise the Council's powers and responsibilities as the sole shareholder of the LATC". The report went on to state "**Reason:** In order to properly exercise the Council's powers and responsibilities as the sole shareholder of the LATC".*
 9. That Committee was therefore intended to have all of the powers and responsibilities of CYC as the sole shareholder of the company i.e. authority to decide on all matters reserved in the Shareholder Agreement as "Corporate Covenants" for CYC decision.
 10. The final recommendation in relation to the October 2011 report authorised the Director of CBSS to bring forward proposals on which activities should be considered for trading through CYT, subject to approval of business cases approved by CYC's Management Team, the Board of Directors and the Shareholder Committee.
 11. Appended to the report was an Executive Summary of the Shareholder Agreement, along with the Articles of Association. That summary report notes that the Shareholder Committee was not intended to take an operational role, but was to be the means by which CYC would appoint and remove directors, review the annual business plan, discuss and

review the financial performance of the company and its performance as a whole. The Shareholders' Agreement at clause 8.2 noted that the Shareholder Committee was authorised to "exercise the functions flowing from its ownership of shares".

12. The Shareholder Agreement reserved a number of matters to CYC for CYC's consent. These matters require the "prior written consent of the Council" before taking action. Such matters include a range of usual matters including whether to enter into or establish any joint venture with another third party, incurring material levels of expenditure or financial indebtedness, or making amendments to the business plan etc. One of those "Corporate Covenants" as they were termed was to:
 - *"vary the emoluments of any of its Directors or Shareholders or of any Shareholder or of any Associate of a Director or Shareholder"*.
13. CYT was required to provide quarterly information to CYC on the financial and other performance of the business. The annexes to the report also included guidance on directors' conflicts of interest and the Companies Act duties and guidance on how to avoid/manage them. The advice covered both transactional conflicts and situational conflicts and a process for considering authorisation in the event that such conflicts arose.
14. Annex 5 explained that staff would be seconded to the company, at least initially.
15. CYT has continued to be a profitable company for CYC and plans to broaden its service offer in the near future.

Auditor's Findings

16. On 30th September 2015, Mazars issued an unqualified audit opinion on the council's accounts and an unqualified value for money conclusion. However the audit of accounts was extended whilst further consideration was given to the governance arrangements covering the payments made by City of York Trading Ltd to two of the company's executive directors who were also officers of the council. Section 2 of the Public Interest Report sets out the overall conclusions from the audit. In the following section of the report, the Auditor's subsequent recommendations are set out with the council's response.

PIR Recommendations

17. It should be noted that Executive and the Chair of the CYT Board have already taken steps to address the auditor's recommendations. It has been agreed that the Board structure of the company will be revised so that there are two elected Members providing cross party representation, two external non-executive directors, one officer non-executive director and a Managing Director (who will be externally recruited). On 4th April, the shareholder group will consider more detailed proposals for the Managing Director role. The result of this is that 'no payment will be made by CYT in future to Board members other than to the full-time Managing Director and any agreed amount paid to external Directors. Additionally, the Shareholder Committee is now meeting in public.

The Auditors specific recommendations are as follows -

Council approval of the payments

18. R1 The Council should take steps to rectify the omission of Council approval for the payments made to the two directors of City of York Trading Ltd in March 2015 for work for the company in 2013/14.

CYC Response – In light of the auditor's findings, this matter will be considered by Executive on April 28th. (The decision is one for Executive rather than Full Council).

Governance arrangements

19. R2 Where the Council envisages a role for a committee within a Council-owned trading company to fulfil a Council function, as appears to have been the case with the Shareholder Committee of City of York Trading Ltd, the Council should ensure that the Constitution is amended to reflect this role and that the composition of the Committee is consistent with the Council's decision making and governance arrangements.
20. R3 The Council should review its approach to the establishment and governance of Council-owned companies to ensure that it fully reflects good practice and the lessons from this report.
21. R4 In the light of the conclusions of the review recommended in R3, the Council should prepare specific guidance to members and officers on their involvement in Council-owned companies.

CYC Proposed Response to Recommendations R2/R3/R4 – A full review of the constitution will be undertaken for all CYC companies by the Monitoring Officer and the recommendations in relation to Executive and Policy matters will be reported to Executive and any proposed changes to the constitution will be reported to Audit & Governance Committee within 3 months of the Full Council meeting held on March 24th.

- 22.R5 The guidance recommended in R4 should address the conflict of interest risks likely to arise where members and officers hold both Council and Council-owned company roles (unpaid and paid) and set out clear advice on how these should be managed. The guidance should also specifically address how the conflict of interest risks should be managed where the Council officers involved hold one of the three Statutory Officer roles of Head of Paid Service, Chief Finance Officer and Monitoring Officer.

CYC Proposed Response – This recommendation will be addressed when drafting new guidance. The Monitoring Officer, supported by the Head of Human Resources will be responsible for this recommendation. In general, statutory officers, will not be appointed as directors of council companies because their office requires them to advise the Council and this may conflict with the position of a company in which the Council is involved. However there are occasions where it would be appropriate, and in these circumstances, officers will set out for Executive how conflicts of interest will be managed as part of the decision making process.

- 23.R6 The Council should review its arrangements for ensuring that internal legal advice is followed, and that any instances where such advice is not followed are identified.

CYC Proposed Response – We note the Auditor's recommendations. On a daily basis the council is in dialogue with its lawyers over a range of matters including property & assets, procurement and safeguarding. Much of this advice is given to aide decision making by setting out the risks the organisation may face. However, where legal advice is prescriptive, it will be followed unless there are good reasons for the decision-maker choosing not to follow the advice; the impact and consequences of not following the advice are understood; all relevant considerations are taken into account; the decision would be a reasonable one for the authority to make (i.e. not irrational or perverse;) and the reasons for departing from the legal advice are recorded in writing.

The Monitoring Officer must be notified of instances where legal advice is not followed and will keep a record.

Disclosures in financial statements

- 24.R7 Where there are unusual or sensitive transactions such as the remuneration paid to Council officers for their work for a Council-owned trading company, particularly where they take place for the first time, the Council should bring the matter to the auditor's attention during the audit.

CYC Response – agreed and this will be the responsibility of the Section 151 Officer.

- 25 .R8 Where senior Council officers receive remuneration for their work for a Council-owned trading company, the Council should recognise this as a related-party transaction and disclose it in the notes to the financial statements.

CYC Response – Agreed and this will be the responsibility of the Section 151 Officer.

Register of interests

26. R9 The Council should update the officer register of interests form and guidance notes to require disclosure of the value of any remuneration received for an individual officer's role in a Council-owned trading company.
- 27.R10 The Council should review its system for ensuring that all annual returns are received for the officer register of interests.

CYC Proposed Response to recommendations R9/R10 – This is currently under review and a series of changes are planned for the end of March 2016. In due course the council will publish Chief Officer declarations of interest on the council website. It is the Section 151 Officer, supported by the Monitoring Officer who has responsibility for this recommendation.

28. The Chief Executive will have overall responsibility for ensuring that all of the Mazars recommendations are addressed.

Implications

- **Financial** – There are no direct financial implications in this report
- **Human Resources (HR)** - The recommendations within the PIR will require changes in the way that the council manages companies that it creates.

- **Equalities** - None
- **Legal** - Section 8 of the Audit Commission Act 1998 requires the Council to consider the Public Interest report and recommendations at a meeting of the full Council within one month of issue. The Council's response to the report and recommendations must then be published. Members are reminded that should they wish to discuss anything in detail relating to the two Council Officers who are the subject of the payments or the other staff referred to in the report then Council Procedure Rule 36.2 states "If any question arises at any meeting of the Council relating to the appointment, dismissal, promotion, conduct, remuneration or conditions of service of any member of the Council's staff no discussion shall take place until the meeting has considered whether or not to exclude the public and press in accordance with the Access to Information Procedure Rules." Members should therefore consider the points they wish to make about the report carefully and limit any statements that they may wish to make in public session about the two officers. At some point the Lord Mayor may require the exclusion of the press and the public and go into private session, should members wish to raise any issues about the officers concerned.
- **Crime and Disorder** - None
- **Information Technology (IT)** - None
- **Property** - None
- **Other** - None

Recommendations

- 1) Members are asked to read the Public Interest Report that the Auditor has published.

Reason: It is a legal requirement for Members to consider the Public Interest Report.

- 2) Members are asked to note and endorse the proposed responses that CYC has made to the recommendations (set out from Para 19) and those that will be considered by the Executive.

Reason: There is a legal requirement for the Council to respond to the Auditors recommendations.

Contact Details

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**Report
Approved**



Date 17 March 2016

Specialist Implications Officer(s) *List information for all*

Wards Affected: *List wards or tick box to indicate all*

All

For further information please contact the author of the report

Annexes

Annex 1 – Mazars report

Abbreviations

CYT – City of York Trading Ltd
LATC – Local Authority Trading Company
PIR – Public Interest Report