

Appendix 1 – Governance Improvement Programme Progress Update

Recommendation 1: *Using the current Strategic Review and other appropriate advice to assist with decision-making, the Council should urgently determine the future of Robin Hood Energy, with options properly evaluated and risks properly assessed. This assessment should also take into account the context of the Council's current financial position.*

In March 2020, prior to the publication of the PIR, Nottingham City Council launched a strategic review of Robin Hood Energy with a view to determining the long term future of the company. At the same time, the company, at the direction of the Council as shareholder, appointed external advisors with significant industry experience to take over the management of the company and support the strategic review process.

The Strategic Review has considered a range of options for the future direction of Robin Hood Energy culminating in the decision to dispose of the customer book through an agreement with Centrica, the parent company of British Gas. This decision is consistent with the aim of resolving the Council's financial exposure while minimising the final cost of doing so.

From the 4th of September, Robin Hood Energy began the transfer of its customers to British Gas a process that will conclude in early 2021.

Recommendation 2: *The Council should review its overall approach to using Councillors on the boards of its subsidiary companies and other similar organisations. This should be informed by a full understanding of the role of and legal requirements for company Board members.*

Between September and November 2020, the Council has undertaken a review of best practice with regard to Council owned companies alongside a review of the current and historic practice of the City Council. This review identified many examples of Councillors acting as directors for Local Authority controlled subsidiaries and found no reason to recommend the exclusion of Councillors from acting as directors. There is however, an over reliance on elected members to serve as unpaid directors and the use of Executive Councillors, particularly members of the Companies' Governance Executive Sub-Committee, gives rise to difficult conflicts of interest that are more challenging to resolve.

The Lawyers in Local Government Example Best Practice Code states that "whilst it will therefore be the norm that officers, not members, will be appointed as directors, this should not prevent the Council from appointing Members as directors where that is considered to be in the best interests of the company and the Council."

Similarly the 2016 Grant Thornton review of group governance at Birmingham City Council included in its recommendations that "entity boards will

remain a combination of elected members and NEDs.”

In both cases however, the guidance highlights the inability of Councillors to waive any conflict of interest they may have in their role as Councillor, thereby preventing them from participating in any decision making process in relation to the company.

For these reasons, it is not proposed that a blanket restriction on Councillor appointments to Council company directorships be adopted. Instead, it should be considered that restrictions on membership for Executive and Non-Executive Committees with a role in the governance of Council owned companies be drafted into their terms of reference. This is addressed under recommendations six and nine of the auditor’s report and Nottingham City Council’s own recommendation three.

The review has also considered the powers of the Council as shareholder or member to control the composition of company boards through the appointment and removal of directors. The ability to appoint directors is ordinarily laid out in the articles of association for each company. For companies limited by shares, this power is commonly held by shareholders who may exercise it through ordinary resolution. The board of directors themselves may also hold the same power, either with shareholder consent required – for example at the next AGM following appointment – or without consent.

For companies limited by guarantee without share capital, the appointment of directors is often tied directly to membership where each member is able to nominate a certain number of directors. In the case of charitable trust these directors will usually also serve as trustees.

For the Council to maintain effective control of the composition of the company board, the right to appoint must be exclusively reserved by the shareholder or member. A review of the articles of association for all subsidiary companies has been undertaken. This initial review has found five of the eight subsidiary companies whose articles do not exclusively reserve the right of appointment to NCC. It is suggested that the Council should prioritise amending the provisions of these Articles to ensure control of appointments and removals are retained by the Council.

Recommendation 3: *Where it continues to use Councillors in such roles, it should ensure that the non-executives (including Councillors) on the relevant board have, in aggregate, the required knowledge and experience to challenge management. This is of particular importance where the company is operating in a specialised sector which is outside the normal experience of Councillors.*

The level of individual knowledge and expertise required of directors will in large part depend on the purpose of their appointment to the board. In the case of Councillors appointed to company boards, they bring significant experience and understanding of their local communities, the Council’s vision for the City and expectations and experiences of citizens. Where a company’s primary areas of operation are concerned with these dynamics, Councillors are able to make extremely valuable contributions to the goals of the organisation. While a Councillor may also bring additional experiences, knowledge and skills from roles outside local democracy, it is questionable whether this can be relied on in the long term as the sole means of bringing industry expertise to the board.

A review of the employment history and technical background of directors other than NCC Councillors and Officers has also been conducted. Nottingham City Homes and Nottingham City Transport both have non-executive directories including independent non-executive directors with considerable combined experience in property management and housing. Nottingham City Homes also benefits from the inclusion of tenant board members, who are able to provide a valuable alternative perspective to board decisions.

Similarly, the board of Nottingham Ice Centre Limited includes five non-executive directors (other than those who are NCC Officers or Councillors), all of whom have other directorship experience and a range of professional qualifications. It is reasonable to accept that in these companies' sufficient industry skills and experience exists among the non-executive board members to hold the management of the companies to account.

The recently acquired company Thomas Bow has a board consisting of three executive directors, each with considerable experience in the relevant industrial sector, and one Councillor who is also an Executive Councillor. While the required knowledge and skills clearly exist at the board level, the industry expertise is consolidated exclusively among executive directors without a realistic prospect of independent challenge from an industry expert. Consideration ought to be given to the appointment of an independent non-executive director, or to whether NCC Officers with experience in highways construction contracts or similar might provide valuable challenge to the board.

The remaining four subsidiaries have no directors other than NCC Officers or Councillors and on the face of it, are likely to lack the level of sector specific expertise required. It is important to note that one of those companies is Robin Hood Energy, which is the subject of the strategic review outlined under recommendation one and has commissioned significant support from industry experts.

The remaining two companies are Enviroenergy and Nottingham Revenue and Benefits. Enviroenergy is itself the subject of strategic review linked to the Council's district heating infrastructure and waste processing arrangements. The strategic significance and complexity of the overarching project is well understood by the Council and has also been identified by the NSR as a strategic priority for the Council.

As part of the Council's response to the broader question of Council owned companies raised under Nottingham City Council's own recommendation one and reiterated by the NSR, Nottingham Revenue and Benefits has been identified as a priority for a Strategic Review in 2021.

Control of the appointment and removal of directors as outlined under recommendation 2 is also of importance here.

Recommendation 4: *Where Councillors are used in such roles, the Council should ensure that the Councillors are provided with sufficient and appropriate training, which is updated periodically.*

Regardless of the varying roles different directors may have, it is essential that all NCC Councillors and Officers are equipped with the basic core competencies and understanding of the legal duties and liabilities associated with their position.

Advice on the core competencies and training required to effectively discharge the duties of directors has been sought from appropriately qualified

external bodies which, alongside guidance found in the review of best practice, has been used to produce a list of training requirements.

A review of training records for Councillors and Officers serving on company boards has been undertaken to identify any previous training that would meet these requirement either in full or in part. Whilst there are instances of training and professional development that would certainly contribute to being an effective board member, there is limited evidence of training to enable them to fully and effectively execute the duties of directors.

This is not say that training hasn't taken place, and there are anecdotal accounts of such training being delivered, but the record keeping of attendance and course content does not provide a robust basis to form a judgement on the sufficiency of such training. The gap is partly explained by Councillor training records having only transferred to the Corporate system in 2018, however, in the absence of a clear record it is recommended that all Councillors serving in the role of company directors regardless of whether it is a wholly owned subsidiary.

A training and development framework for Councillors serving in the capacity of directors has been produced. This is a tiered approach building on the foundational skills developed by Councillors through existing induction and refresher training with additional training covering:

- The role of a company director
- Legal obligations for directors
- Company structures
- Board effectiveness
- Risk Management
- Corporate culture and corporate social responsibility

A training specification has been produced and proposals sought from three well established and well regarded bodies with relevant experience. It is anticipated that this training will be commissioned and rolled out from the end of January 2021, subject to contract.

As an immediate measure, Nottingham City Council has developed and delivered its own internal training course for Councillors acting as directors.

Recommendation 5: The Council should ensure that all elements of its governance structure, including the shareholder role, are properly defined and that those definitions are effectively communicated to the necessary individuals.

The elements of the Council's governance structure are set out in the Council's constitution. In particular, the Terms of Reference for Committees which sets out the distinctions between Executive, Non-Executive and Scrutiny functions and the roles of different Committees with regard to decision making.

Reviews have been undertaken of the Terms of Reference for Audit Committee, Overview & Scrutiny Committee and Companies Governance Executive Sub-Committee. A redraft of the Audit Committee Terms of Reference has been produced and at the time of writing further advice and

challenge was being sought from CIPFA with a view to bringing a version for formal adoption to Council in early 2021.

A review of the existing Overview and Scrutiny Committee terms of reference has been undertaken against identified best practice. This review redrafted the Terms of Reference in order to provide clarity on the role of the committee, particularly in relation to Council owned companies, CGESC and Audit Committee. A draft of the proposed Terms of Reference for Overview & Scrutiny Committee has been presented to and accepted by the Committee and is appended to this report for formal adoption as detailed in the recommendations of this report.

The review of best practice has identified a need for a clear mechanism for exercising the rights and controls of shareholder or member. This has particular relevance to the appointments process (for Councillor and Officer directorships), that should be strengthened. It is considered good practice for the role and rights of shareholder and member to be consolidated in an Executive Committee of the Council and for this reason consideration should be given to amending the Terms of Reference of the Companies Governance Executive Sub-Committee accordingly.

A redraft of the Terms of Reference has not been produced at this stage in order that any changes also take into consideration the findings of the recently published NSR, however, it is proposed that the following addition be made to the purpose of the Committee:

"To discharge the executive functions of Shareholder, Member or Guarantor of companies within the Nottingham City Council Group and companies in which Nottingham City Council holds shares or membership rights."

In addition it is proposed that the following additions be made to the listed responsibilities of the committee in its terms of reference:

Consider matters reserved to the Council for shareholder approval, such as:

- Varying Articles of Association
- Varying ownership and structure including the formation of subsidiaries to any company
- Variations to shares (number of, rights, etc.)
- Entering contracts that; have a material effect on NCC Council business (including other companies within the group), are outside of the business plan or do not relate to the business, or are significant in relation to the size of the business, the business plan, etc.
- Material legal proceedings outside of ordinary business
- Adopting and amending business plans each year and strategic plans (3 years)
- Appointment, removal and the remuneration of directors (members of the company board)
- Selection of the chair of the board
- Appointment of auditors
- Issue of dividends

In parallel, the role of the Shareholder Representative (as distinct from shareholder) has been considered at Companies Governance Executive Sub-Committee on the 20th of October 2020, and a subsequent draft role description and competency requirements produced.

The Commissioning & Procurement Executive Sub-Committee, although not mentioned in the Auditor's report, has a role in protecting the client interests of the Council and VfM, where the Council awards contracts to subsidiary companies. Proposals will also be developed and brought forward for the

Commissioning & Procurement Executive Sub-Committee.

Recommendation 6: When allocating roles on Council-owned organisations to individual Councillors, the Council should ensure that the scope for conflicts of interest is minimised, with a clear divide between those in such roles and those responsible for holding them to account or overseeing them.

In response to recommendation six of the external auditor's report, Nottingham City Council has reviewed its process for appointments to company boards. The review process has also highlighted the potential to minimise the scope for conflicts of interest through restrictions on membership in the Terms of Reference of key Committees.

The use of membership restrictions in this way has been presented to Audit Committee for discussion on the 18th of December 2020. The Committee has concurred with the view that restrictions on membership should exclude Executive Members who hold directorships from membership of Companies Governance Executive Sub-Committee.

In addition Audit Committee have given a view that where practical, Executive Members ought not hold directorships in Council companies whose primary activity falls within the scope of their portfolio. In relation to this point, the Committee has requested further clarification of the role of Portfolio Holders in relation to companies of this kind and the proper alignment of company's policy objectives to those of the Council.

Appointment / nomination to Outside Bodies is a Local Choice Function and NCC has determined that it is an Executive Function. Appointments / nominations are therefore approved by Executive Board, an Area Committee or, for in-year changes, the Director for Legal and Governance. Executive Board is responsible for the majority of approvals with Area Committees being responsible for nominations / appointments to Outside Bodies that operate exclusively within their area.

While these provisions provide a framework for the general case of appointments to Outside Bodies, they do not address the specifics of exercising the shareholder rights to appoint to a company board. In the case of an appointment made by the existing board of directors (where they have the right to do so), the above provision would have little or no effect.

It is proposed that the nominations and appointments process for Directors of all NCC companies be rationalised. This should include a record of the decision to indemnify Officers or Councillors appointed as directors.

By virtue of the Local Authorities (Indemnities for Members and Officers) Order 2004, officers or members may be indemnified by the authority for actions undertaken for or at the direction of the authority (within certain limitations), including in any role they take as the director of a Council company. While there is specific insurance provision for a range of eventualities there is no explicit communication or confirmation of the indemnification offered by the Council to the individual.

It is also recommended that a robust system for recording the decisions of the shareholder/member, including appointments and nominations of

directors, be established. In addition it is recommended that the details of all decisions for appointments and current board memberships be published on the Council website.

Recommendation 7: *The Council should ensure that risks relating to its companies are considered for inclusion in its overall risk management processes, with appropriate escalation and reporting, rather than being seen in isolation.*

On the 24th of November the City Council approved a refreshed Corporate Risk Management Framework, including risk registers for each Council Company and an integrating strategic risks from the company group as a whole into the high level corporate risk register.

In light of the NSR findings and subsequent Recovery and Improvement Plan, effective risk management will continue to be a central consideration for the Council and the Corporate Risk Register will remain under continual review.

Recommendation 8: *As the new arrangements for monitoring companies are rolled out alongside the Companies Governance Executive Sub-Committee (CGESC), the Council should ensure that financial information is provided in accordance with its requirements and is fully understood by the Sub-Committee and others involved in holding the companies to account, and that robust action, with the oversight of the s151 officer, is taken if suitable information is not provided.*

The Companies Governance Executive Sub-Committee has established clear reporting mechanisms for each company in the group. This includes the changes to the Corporate Risk Management Framework referred to under recommendation 7 alongside key indicators of financial performance.

The Committee is advised by the Section 151 Officer, Monitoring Office and Chief Executive to support them in holding companies to account and ensuring full compliance with these reporting requirements.

In addition to these arrangements, consideration has been given to introducing additional controls including the establishment of an Officer Shareholder Executive to sit alongside the Companies Governance Executive Sub-Committee as well as the introduction of Company Loans protocol to scrutinise the borrowing requirements of individual companies. The NSR has identified similar requirements and it is proposed that these considerations be further developed through the implementation of the Recovery and Improvement Plan.

Recommendation 9: Within the new arrangements involving the Companies Governance Executive Sub-committee, the Council needs to ensure that responsibilities for scrutiny and risk management are given sufficient prominence, including giving the Audit Committee explicit responsibility for scrutiny of governance and risk management across the group.

As outlined under recommendation five, the City Council has reviewed the terms of reference for Overview and Scrutiny Committee, Companies Governance Executive Sub-Committee and Audit Committee as well as bringing forward proposals to further review the Terms of Reference for the Commissioning & Procurement Executive Sub-Committee.

The review of the existing Overview and Scrutiny Committee redrafted the Terms of Reference in order to provide clarity on the role of the committee, particularly in relation to Council owned companies, CGESC and Audit Committee. Input was sought from the LGA on the draft and, as a result of their feedback, further amendment was made, including the addition of reference to risk management.

The draft has been taken to Overview & Scrutiny Committee on 9th December 2020 and is brought forward for approval at this meeting of full Council.

At the time of writing redraft of the Audit Committee Terms of Reference has been produced and at the time of writing further advice and challenge was being sought from CIPFA with a view to bringing a version for formal adoption to Council in early 2021.

Recommendation 10: In addition to those referred to in recommendations above, the Council should apply the lessons from Robin Hood Energy in a further review of its company governance arrangements, in particular to ensure that risks are appropriately flagged and managed, as well as successfully implementing the more robust monitoring agreed by the Companies Governance Executive Sub-Committee

The production of this report for consideration by full Council is intended to respond to recommendation 10 of the PIR. In light of the recently published NSR, the broader findings and lessons learnt will naturally feed into the Recovery and Improvement Plan. Consideration should be given to the extent of overlap between the Action Plan in response to the PIR and the Recovery and Improvement Plan in response to the NSR.

Recommendation 11: As part of this review, the Council should consider the appropriateness of the definition of the shareholder role adopted in the 2019 report and give it an emphasis on protection of the Council's financial interests alongside other elements.

As outlined under recommendation five, the role of the Shareholder Representative (as distinct from shareholder) has been considered at Companies Governance Executive Sub-Committee on the 20th of October 2020, and a subsequent draft role description and competency requirements has been produced for consideration.

Shareholder Representatives are in place for seven of the eight subsidiaries. During the period of the review the current Interim Director of Strategic Finance has been appointed Shareholder Representative for Nottingham Revenue and Benefits to replace his predecessor. While these arrangements are currently sufficient, further consideration will also be given to the capacity of shareholder representatives in the longer term and their role in relation to the shareholder panel identified in the best practice review.

Recommendation 12: *The Council should use the experience of owning RHE to consider whether there are any lessons for its wider governance, particularly in relation to the ‘checks and balances’ which need to be in place, including the need for a stronger monitoring and scrutiny function and moving to a culture in which challenge of political priorities and how they are being implemented is seen as a positive.*

Nottingham City Council has already started the process of reviewing and improving its system of governance and internal control. The City Council's response to the PIR details the actions the City Council is taking and will take up to June 2021.

The subsequent report of the NSR team builds on findings and recommendations of the external auditor, and as a result there is significant overlap in the actions and activities required by both. In order to streamline management and reporting arrangements and maximise the efficient use of limited resources consideration should be given to which activities are best managed and delivered through Governance Improvement Programme and which would be better rolled into the overall Improvement Programme.

The Nottingham City Council Constitution has been the subject of review since October, following the adoption by full Council of the Action plan in response to the PIR.

This work focuses primarily on the Committee structure and functions and on the their Terms of Reference. This work will now continue alongside a comprehensive rewriting of the whole constitution with the aim of simplifying it and enabling the Council to make effective decisions and implement the broader change programme at the rate required.

This work will create greater separation and independence between the Executive and Non-Executive roles within the constitution and strengthen the roles of the Overview & Scrutiny Committee and Audit Committee.

The NSR has highlighted the need to bring greater clarity to different roles of Councillors and officers, and their responsibilities to the organisation as a whole. To this end it is proposed that a new Member Officer Protocol be adopted to help set a common set of shared expectations for officers and Councillors.

Recommendation 13: *The Council should ensure that it reflects the financial pressures arising from RHE alongside those from covid-19, demand-led services and other areas to produce balanced and achievable financial plans for the current year and for the medium-term, without disproportionate, unsustainable reliance on one-off measures.*

The Council has passed a revision to the in-year budget bringing forward £12.5m of savings proposals and further proposals facilitated by accepting 113 VR applications, with a full year impact £2.3m.

Work on the 2021/22 budget is now well advance and a proposed budget will be submitted to the Council's Executive Board in January 2021, to commence the formal consultation process. Once adopted, the budget will be monitored through the introduction of new budget oversight procedures to ensure savings are both tracked and delivered. These will ensure that both members and officers are clearly sighted on the budget and the key risks surrounding it and have a joint responsibility for managing these.

The 2021/22 budget will also contain the rolling three year MTFS and clearly set out the parameters against which this will be managed and delivered. In addition Nottingham City Council will develop a Debt Management Strategy which will manage the Council's overall debt downwards over MTFS time horizons.

Additional Officer Recommendations:

The Action Plan prepared by the Council in response to the PIR included three additional recommendations made by Officers and agreed by Council. The additional recommendations (shown below for reference) were planned to take place between January and June 2021.

In light of the recently published NSR the actions proposed in relation to these recommendations need to be reviewed to avoid duplication or abortive work. In particular the NSR includes the recommendations that NCC should:

- “conduct an in-depth assessment of its group of companies during the first year of the Plan and integrate their conclusions within their medium-term financial planning process”; and
- “produce a clear policy statement within 6 months which established the roles and responsibilities of nominated non-executive directors and shareholder representatives and incorporate it as an element of the Constitution”.

These recommendations when taken with the broader aims of the proposed Recovery and Improvement Plan are likely to subsume and supersede the Officer recommendations listed below:

NCC 1 - Review of Council's approach to the ownership of companies: The Council has a range of companies totally in its ownership and some owned jointly with others. These companies have developed over time and further are planned to be created during this period of office as outlined in the Council Plan. In the light of the findings of this report the overall approach of the Council to its relationship with its companies could benefit from a review.

NCC 2 - Review of effective governance practice in NCC companies: The Council has a number of companies which have had effective governance over a number of years and which have involved elected members on the boards. As part of this improvement work it is important to understand what has made those council companies and Boards effective and how any learning can be applied to other council companies and the other recommendations in this Action Plan.

NCC 3 - Review of membership of the Audit Committee: As a solution to the pressures from the reduction in public funding of services, the Council either owns or has a major interest in a considerable number of companies. It has also pursued a policy of in-house commercialisation of some services. As such the company and commercial trading risks it carries are more than would normally be expected for a local authority.