

# RUNNYMEDE BOROUGH COUNCIL COMMERCIAL GOVERNANCE REVIEW

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## 1. About us

Ethical Commercial Ltd has been working with local government and central government clients for more than six years.

We've provided commercial consultancy, advice and project delivery in areas including:

- Companies' governance
- Commercial strategy
- Trading company reviews
- Procurement and contract management
- Commercial viability assessment
- In-sourcing multi-service contracts

Most recently, we've been supporting Woking Borough Council and Nottingham City Council, working directly with the DHLUC Commissioners to develop and deliver recovery plans following significant commercial and financial failings, as well as other local authorities not currently in formal intervention.

The staff deployed on this review are:

### Ian Edward

Ian is a CIPFA member and holds a LLB(Hons) degree. He is a highly experienced commercial director having worked for blue chip companies for more than 20 years. As a director of Ethical Commercial Ltd, he has acted as an advisor to many public sector bodies since the company was formed some six years ago.

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### Michael Hainge

Michael holds a BA(Hons) degree as well as the Diploma in Environment Sustainability and Governance. He is also a qualified mediator registered with the Civil Mediation Council. He spent 20 years at director level in many local authorities and the private sector before creating Ethical Commercial Ltd with Ian in 2018.

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## 2. The Brief

We were asked to focus on the following questions and areas:

- What was the original intent to having a company structure?
- What is the structure, governance arrangement and reporting mechanism in place now?
- Is the original intent met by the current model?
- Applying leading practice to assure company governance – review the current model.
- Make recommendations to mitigate risk and improve assurance
- Are the companies necessary (a) as an entity (b) to deliver on their intent.

### 3. Our approach

In order to answer the brief, we have gathered information from:

- documents supplied by the Council
- Documents held at Companies House and
- Interviews with key staff

We have compared these findings with best in class guidance and requirements assimilated from:

- Companies Acts
- Institute of Directors
- Local Partnerships
- Financial Reporting Council and
- CIPFA

### 4. Our findings

#### 4.1 Creation of the companies

We would expect to see a number of steps prior to the formation of any companies. These would include:

- Options appraisal to consider *what* actions can be taken for the objectives to be met. In this case, for example, to raise additional net revenues for the Council's general fund through property investments.
- A delivery model assessment (DMA) to consider *how* the preferred option would be pursued, such as in-house, limited company, joint venture (incorporated or otherwise) or outsourcing would best achieve the desired objectives
- Outline business case that shows how costs, risks, returns and commercial, social and environmental benefits can be achieved.

While the committee report seeking approval to create RBC Investments (Surrey) Limited and RBC Services (Addlestone ONE) dated 2<sup>nd</sup> April 2015, is comprehensive and is well supported by external expert advice, we have not had sight of any preceding options appraisals, delivery model assessments or business cases. Neither have we seen any report seeking the creation of RBH Heat Company Limited, which is owned by RBC Services (Addlestone ONE).

Appendix A of the committee report of the 2<sup>nd</sup> of April 2015, Proposed Aims and Objectives of RBCIS, is helpful, it doesn't consider any other options nor address the reason for having a company structure.

In the section of the committee report headed, Background Papers, the only narrative is 'None'. Therefore, we can only assume that no options appraisals, delivery model assessments or business cases supported the original creation of the companies.

#### 4.2 What was the original intent to having a company structure?

In addition to Appendix A, the committee report sets out the following statements of intent:

*The creation of and use of RBC Investments (Surrey) Limited as the Property Investment SPV for the Council to:*

- i) acquire and manage non Housing Revenue Account residential, commercial and other non Housing Revenue Account Council owned property in compliance with the Property Investment Strategy i.e. for income generation and / or regeneration purposes;*
- ii) acquire, refurbish, develop and sell property in compliance with the Property Investment Strategy;*

As well as:

*To create a Special Purpose Vehicle called RBC Services (Addlestone ONE) Limited to deliver the following:*

- i) Providing the Town Centre Management function for Addlestone;*
- ii) Managing the Addlestone ONE Development including the following:*
  - a) Managing the staff required to operate the Development (either Council secondees or directly employed staff);*
  - b) Arranging contracts and Service Level Agreements for the delivery of services in the Development, contract/SLA monitoring and performance management;*
  - c) Providing Commercial and Residential tenant consultation and involvement;*
  - d) Preparing the annual and long term budgeting for service charges;*
  - e) Offering a portfolio of additional services that can be adopted and contracted by individual commercial and residential tenants;*
  - f) Arranging for the management and auditing of the accounts, the collection of service charge, etc payments, debt management and related activities;*
  - g) Developing and implementing the marketing plan for the Development together with agreeing and arranging specialist events for example Easter and Christmas artisan markets;*

company start-up fairs, etc;

h) Liaising with the Community Heating Network provider to ensure the integration of services.

i) Any other related services.

The Council received advice from James Goudie (then) QC which is referred to in the committee report. Of particular interest is Mr Goudie’s advice that commercial property could be acquired and managed by the Council directly for investment purposes, and that, in broad terms, residential property should be acquired through an SPV. We are advised by the Council that the purpose of RBC Investments (Surrey) Limited and RBC Services (Addlestone ONE) were to acquire and manage residential properties to enable provision in the private rented sector with appropriate tenancies.

### 4.3 What is the structure, governance arrangement and reporting mechanism in place now?

Specific shortcomings are identified in section 4.5. In summary, there has been insufficient separation between the companies and the Council. Whilst appropriate separation does not mean that staff and resources cannot be shared, it does require clear definition of roles, clarity over how the Council and companies work together, policies that deal with risks and conflicts of interest, clear recruitment policies for the board and so forth. The documents relating to board reporting that have been made available to us are far from what we would expect to see and do not support the boards’ decision making rationale or processes. Due to the same, the reporting back to the Shareholder [Corporate Management Committee] does not meet expected standards.

### 4.4 Is the original intent met by the current model?

Growth and expansion of activities envisaged by the 2015 report have not been realised neither has the rate and speed of returns been achieved. Without an originating business case it is very difficult to be able to determine whether the original intent has been met.

The objectives set out in the 2015 report have been met in part (but not full) around the most material activities, but not their resultant commercial outcome. For example:

Intentions April 2015 - RBCI	Reflected in 2023 Business plan (Y/N)
acquire and manage non Housing Revenue Account residential, commercial and other non-Housing Revenue Account Council owned property	Yes
acquire, refurbish, develop and sell property in compliance with the Property Investment Strategy	Yes
Intentions April 2015 – RBCS	
Managing the staff required to operate the Development (either Council secondees or directly employed staff	Yes

Arranging contracts and Service Level Agreements for the delivery of services in the Development, contract/SLA monitoring and performance management	Yes
Providing Commercial and Residential tenant consultation and involvement	Yes
Preparing the annual and long term budgeting for service charges	Yes
Offering a portfolio of additional services that can be adopted and contracted by individual commercial and residential tenants	No
Arranging for the management and auditing of the accounts, the collection of service charge, etc payments, debt management and related activities	Yes
Developing and implementing the marketing plan for the Development together with agreeing and arranging specialist events for example Easter and Christmas artisan markets; company start-up fairs, etc	No
Liaising with the Community Heating Network provider to ensure the integration of services	Yes
Any other related services.	Yes

From the legal advice provided we can see the intent was to operate in compliance with legal requirements, through the use of company structure, which we understand was elective for commercial property but required for residential property for the reasons stated above.

## 4.5 Governance Review

	Description	What we're looking for	What we found	Recommendation	Priority
1	Council / companies interface	Clear links between the council's constitution and the equivalent governance of companies or other entities owned or part-owned by the council. In particular, council powers to appoint and remove board members and the process for doing so.	The role of the Council as Shareholder is articulated clearly in the Council's Constitution as being the responsibility of the Corporate Management Committee. There is no guiding document that describes the different relationships between the Council as Shareholder, Client and Lender, and the companies. Nor the differing roles of Council Officers and Members as directors of the companies	The Council creates and adopts a guiding document that sets out the interface between the two entities and the roles of Officers and Members. See <a href="https://moderngov.woking.gov.uk/documents/s33478/EXE23-069%20Appendix%201.pdf">https://moderngov.woking.gov.uk/documents/s33478/EXE23-069%20Appendix%201.pdf</a>	1-3 months
2	Articles, shareholder agreements and reserved matters	Adequate controls and powers in company constitutional documents protect the shareholder's interests and to provide necessary powers of intervention when required (generally beyond those of special resolutions in section 283(4), Companies Act 2006).	Documentation in place. The companies' Articles align closely with the Shareholder Agreements	None	Not applicable

3	Business planning process	There should be evidence of an up-to-date business plan that is reflective of the current circumstances and environment in which the entity operates. A set of minimum requirements for the business plan should be required by the shareholder. Alignment to the shareholder's core strategic aims and sufficient detail to hold the relevant board to account for the business plan's delivery.	From the business plan we reviewed, 20 <sup>th</sup> April 2023, there is insufficient detail on how the organisation's objectives will be resourced and achieved. Many goals were identified but with no explanation as to how they will be delivered, or progress measured. Financial and objectives had no commercial underpinnings or basis on which the Shareholder could, in any real sense, be confident that they would be achieved.	New business plans should be created that set out the organisation's objectives and <i>how</i> these will be resourced and achieved on an annual basis. More comprehensive risk identification, management and mitigation sections should also be included alongside detailed financial performance measures and targets.	3-6 months
4	Risk management	A clear risk management policy for each of the companies and evidence that they comply with the Financial Reporting Council's (FRC) minimum requirements	An overview of risks is, in practice, furnished through council provided services and officers and the close operational relationship that this provides between the Council and the companies. However, in the absence of a clear risk policy this makes officers, members and company directors vulnerable and open to criticism that, were they following a clear policy, would be negated.	A more formal approach to risk is taken by adoption of a risk management strategy and policy and that company risks are reported in detail to the Company Boards, in an auditable way, that shows not only appropriate reporting of risks but also their effective management and mitigation.	3-6 months
5	Conflicts of interest	A clear conflicts of interest policy for each company and evidence that they comply with the FRC's minimum requirements and those in the guidance set out by Lawyers in Local Government	Conflicts of interest are managed on a case by case basis, and we have not seen any evidence where the companies' or Council's interest have been compromised. However, in the absence of a clear conflicts of interest policy specifically re, Officers and Members are left to their own devices to determine when conflicts arise and how	A conflicts of interest policy should be developed and implemented, that addresses the twin roles carried out by Officers and Members. A critical element of this policy should be a full conflicts check <i>prior</i> to any board appointment.	1-3 months



			they should be dealt with. It should be noted that there is a Code Of Conduct for Officers and a Code of Conduct for Members (the LGA model based on the Nolan Principles) but neither of these address the very specific conflicts that can arise within the twin roles that Officers and Members carry out in respect of the companies.		
6	Standard reporting framework	Standard and comprehensive reporting from the companies to the shareholder on a monthly basis to include matters such as: financial and operational performance against business plan, cash flow forecasts, risks, matters for shareholder consent.	Whilst the reporting is effectively carried out by officers who also create the reports, it is important that comprehensive reports are produced and demonstrate the knowledge and understanding the company boards have which in turn drives their decision making and that this is open to scrutiny by the Shareholder.	Adoption of a standard reporting framework.	1-3 months
7	Board activities	There should be evidence of the boards' delivery of strategies and plans, including scrutinising key operational and finance performance information	Insufficient evidence provided to support this requirement	Creation of comprehensive board packs, agendas and minutes that are based on the delivery of a comprehensive and meaningful business plan (see row 3).	6-12 months

8	Board performance reviews	Evidence of annual internal reviews and an external review every third year, in line with FRC guidance	The practice of carrying out a board performance reviews is an essential part of risk management and assurance. Whilst it is discretionary for non-listed UK companies, the reviews have very real benefits and help companies in public ownership demonstrate their commitment to the Nolan Principles amongst other expectations. During our review we noted that, for a period, board agendas and minutes were very superficial and insufficient in terms of record keeping, the Boards' decision making, and reasoning for those decisions. This meant that the conduct of the board was effectively un-auditable.	Establish annual internal reviews and an external review every three years.	6-12 months
9	Board appointments	There should be evidence that appointments to the board are subject to a documented formal, rigorous, and transparent procedure based on merit and published objective criteria which also promote diversity	No evidence of compliance for this requirement.	As part of the guiding documents of the Council and Companies (see 1. above), a formal approach to board member appointments be put in place.	1-3 months
10	Role of Directors	There is evidence that the role of executive directors and NEDs is clearly defined and documented	No evidence of compliance for this requirement.		1-3 months

11	Role of the board Chairs	There is evidence that the chair provides clear board leadership, supporting the directors and taking account of the shareholder's views.	No evidence of compliance for this requirement.		6-12 months
12	Board member competency evaluation and development	Evidence that board members are only appointed when they can demonstrate the skills and competency required to meet the Institute of Directors, Director Competency Framework	Interviewees during our review acknowledged that there was no formal evaluation of the competency of proposed board directors prior to their appointment, nor during their term of office. Training post appointment has been carried out, both for the duties of board directors and as an induction into the companies' business.	As part of the guiding documents of the Council and Companies (see 1. above), a formal approach to board member competency, training and performance evaluation be put in place.	1-3 months
13	Terms of appointment for board members	As a minimum, the FRC guidance should be followed. At present, this means the Chair should serve for no more than three, three year terms, and NEDs for no more than two, three year terms	In practice, Chairs and NEDs have not from evidence we have seen, served for longer than the terms in the FRC guidance. There are provisions in the Shareholders Agreement that limit Council Board Directors to no more than 6 years but allow a non-council NED an indefinite number of 2 year terms.	Shareholders Agreement should be amended to reflect FRC guidance for all directors.	1-3 months

14	Strategic Review	<p>Evidence to show that every three years, or whenever there is a significant change to the purpose or activities of any company a strategic review of six key areas is carried out:</p> <ol style="list-style-type: none"> <li>1. The company's purpose aligns with the Council's priorities and values</li> <li>2. The company demonstrates long term resilience</li> <li>3. Financial and legal commitments with the company can be justified</li> <li>4. Focus on Value for Money</li> <li>5. The company does not generate undue risk to the Council</li> <li>6. The Council has the organisational capacity and capability to maintain adequate oversight</li> </ol>	<p>We found no evidence to show any of the elements of a strategic review have been carried out.</p>	<p>As part of the guiding documents of the Council and Companies (see 1. above), a formal strategic review be carried out every three years. It may be possible to build this into an internal audit programme.</p>	6-12 months
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**4.6** The findings above, whilst demonstrative of a number of shortcomings in the current governance arrangements, should be seen in the context of both proportionality, and the effort and time required to make improvements.

Given the scale of existing company operations, the extent to which changes are required will not be particularly burdensome, though they are important. Once the shortcomings have been addressed, which we believe is comfortably achievable within the next 12 months or less, the Council will be in an excellent position to demonstrate, and indeed to benefit from, a robust governance model.

**4.7 Are the companies necessary (a) as an entity (b) to deliver on their intent.**

Potentially not. However, transferring assets and winding up of the companies would potentially require a scale of change and cost that may not be efficient given the scale of the entity. Expert legal and tax advice would need to be procured and a business case for change created. Again, the absence of an originating business case complicates matters, and our recommendation would be to carry out a strategic review, as outlined in row 14 above, as a starting point.

Ends.