

# Report

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Report to:	<b>Risk and Audit Scrutiny Forum</b>
Date of Meeting:	<b>26 January 2012</b>
Report by:	<b>Executive Director (Finance and Corporate Resources)</b>

Subject:	<b>Audit Scotland Report - Arm's-Length External Organisations (ALEOs); Are You Getting It Right?</b>
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## 1. Purpose of Report

1.1. The purpose of the report is to:-

- ◆ provide an overview of the Audit Scotland report 'Arm's Length External Organisations are you getting it right' and advise of the Council's response to its recommendations.

## 2. Recommendation(s)

2.1. The Forum is asked to approve the following recommendation(s):-

- (1) that the trial of the checklist and toolkit completed by Community Resources in respect of South Lanarkshire Leisure and Culture Limited is noted;
- (2) that it be noted that the detail within the Council's Service Review Guidance relating to options appraisal would be updated and included within the new Project management Checklist document;
- (3) that it be noted that the Good Governance Group would consider the points for action for officers and councillors and future use of the toolkit and checklist

## 3. Background

- 3.1. In June 2011 the report entitled 'Arm's Length Organisations; are you getting it right?' was published by Audit Scotland on behalf of the Accounts Commission. This is one of a series of reports being prepared by the Commission with the aim of identifying common themes to stimulate change and improve performance.
- 3.2. The information included within the Audit Scotland Report is designed to promote and encourage good practice in the way Arm's Length External Organisations (ALEOs) are set up and operated.
- 3.3. The report highlights what councils should do when considering the use of an ALEO. It then goes on to consider what should be done on an ongoing basis, once established, to ensure it remains the best option and that governance arrangements remain fit for purpose.
- 3.4. The report includes the definition for an ALEO as 'Companies, trusts and other bodies that are separate from the local authority but are subject to local authority control or influence'.
- 3.5. In order to assist councils, the report includes a summary of key points for action to be considered by councillors and officers involved with ALEOs, as well as checklist

for use in checking progress and a toolkit which will help identify any improvements on the governance of ALEOs.

- 3.6. The Commission recommends that councils consider the report and use it to assess current practices and to identify where there may be scope to improve. It is noted that the Commission will review progress as part of the ongoing audit work.

#### **4. Key points from the report**

- 4.1. The report notes that ALEOs may offer an alternative to more traditional 'in-house' or contract based service delivery and usually take the form of companies or trusts. They are 'arm's length' because the council retains a degree of control or influence, usually through a funding agreement, and 'external' because they have a separate identity to the council.
- 4.2. An ALEO may offer different and/or better ways of providing services. However, whilst the ALEO takes on the responsibility for service delivery, the council remains responsible for ensuring the ALEO makes proper use of funds and can demonstrate best value 'although monitoring should be risk based and proportionate'. Therefore, councils must ensure sound governance arrangements are in place from the outset and applied effectively.
- 4.3. It is noted that governance arrangements should take account of the principles included within the Code of Guidance on 'Following the Public Pound'. These state that councils must:
- have a clear purpose in funding an ALEO;
  - set out a suitable financial regime;
  - monitor the ALEO's financial and service performance;
  - carefully consider representation on the ALEO board;
  - establish limits to involvement in the ALEO; and
  - maintain audit access to support accountability

Sound governance includes establishing clear roles and responsibilities both for officers and councillors involved

- 4.4. The report also notes that any decision to use an ALEO should be based on options appraisal and a sound business case. This enables councils to assess the options that best meet their objectives. Options appraisal will consider the risk involved, the financial implications, governance arrangements and impact assessments.
- 4.5. The Commission notes that its audit work to date has not highlighted widespread problems, but that there were some concerns in specific cases. Therefore, the report published in June 2011 is designed to promote and encourage good practice in the ways ALEOs are set up and operated.
- 4.6. In order to effectively consider the detail of the report, four areas of work were identified as follows:
- update information on options appraisal currently included within the Council's Service Guidance document, to take account of ALEO recommendations;
  - Council's Good Governance Group to review the key points for action relative to councillor and officers involved in ALEOs;
  - Good Governance Group also to consider the wider use of the toolkit and checklist within the Council as good practice for similarly arranged organisations. This would support continuous improvement in the governance of ALEOs;

- Checklist and toolkit (Audit Scotland Report Appendices 1 and 2) to be completed in respect of Council's ALEO arrangement with South Lanarkshire Leisure and Culture Limited to pilot in the first instance

## **5. Governance**

- 5.1. The report notes that strong governance requires clear roles and responsibilities, both in terms of officers and councillors responsible for monitoring the ALEO and also for those who are on its Board. The report recognises the contribution officers and councillors make in overseeing and monitoring ALEOs.
- 5.2. The report includes an outline of key points for action for councillors and officers involved with ALEOs. Details of these are attached at Appendix 1. It is proposed that the Good Governance Group will review these, together with the toolkit in order to determine any areas for development and recommendations.

## **6. Checklist and toolkit**

- 6.1. The checklist and toolkit were completed by Community Resources in respect of South Lanarkshire Leisure and Culture Limited (SLLC).
- 6.2. The checklist includes four headings to support good management of ALEOs, ie:
  - Rationale for ALEO
  - Governance of ALEO
  - Are we aware of how well ALEO is performing
  - Are we aware of the risks faced by the council and the ALEO

The Community Resources' response to the checklist confirmed that arrangements are in place to support good management of the ALEO, and a small number of actions were identified to be scheduled over the next few months.

- 6.3. The toolkit was also completed in respect of SLLC. The toolkit aims to establish how well the Council ensures that effective governance and accountability is maintained when the Council delivers services through an ALEO, including companies and trusts. The purpose of the toolkit is to assess the Council's response to four key questions in terms of attaining 'Basic', 'Basic and Better' or 'Advanced' practice. The Community Resources assessment confirmed two areas of 'Advanced' practice and two 'Basic and Better'. Further consideration is being given to those which are not 'Advanced'.

## **7. Further use of checklist and toolkit**

- 7.1. Whilst the checklist and toolkit were considered by SLLC, good practice would be to carry out the assessment in respect of any future ALEOs, and to apply targeted use to other similar areas within the Council.

## **8. Further action: Consideration of options appraisal**

- 8.1. The Council's Service Review Guidance currently includes advice on options appraisal. The explanatory text related to this option is a good high level explanation of what should be considered. However, it is recommended that the guidance be updated to include the more detailed list from within the Audit Scotland report (see Appendix 2) and used as part of the development of any future ALEO business cases. An exercise is currently underway within Audit and Improvement Services to develop a comprehensive Project Management Checklist document which will bring together the most significant aspects of project management from a number of documents, including Service Review Guidance.

## **9. Employee Implications**

- 9.1. There are no employee implications.

## **10. Financial Implications**

- 10.1. There are no financial implications.

## **11. Other Implications**

- 11.1. The approach to risk management in terms of ALEOs will be considered as part of the exercise to be carried out by the Good Governance Group.

## **12. Equality Impact Assessment and Consultation Arrangements**

- 12.1. This report does not introduce a new policy, function or strategy or recommend a change to an existing policy, function or strategy and therefore, no impact assessment is required.

**Paul Manning**

**Executive Director (Finance and Corporate Resources)**

5 January 2012

### **Link(s) to Council Objectives/Improvement Themes/Values**

- Governance and accountability
- Performance management and improvement
- Efficient and effective use of resources

### **Previous References**

- None

### **List of Background Papers**

- Audit Scotland report (June 2011) – Arm's-length external organisations (ALEOs): are you getting it right?

### **Contact for Further Information**

If you would like to inspect the background papers or want further information, please contact: - Heather McNeil, Head of Audit and Improvement

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The tables below outline key points for action for councillors and officers involved with ALEOs

## Getting it right from the start

Councils must:

- observe the Accounts Commission/COSLA Code, and other guidance to understand their responsibilities and good practice when involved with ALEOs
- base any decision to set up an ALEO on sound options appraisal and feasibility assessments including risks
- ensure that where they use an ALEO it fits their priorities or policy objectives
- consider governance at the outset to ensure the council and the ALEO can effectively:
  - scrutinise performance and be held accountable
  - monitor costs, performance, and risk
  - engage service users and citizens
- clearly understand and set out the roles of boards, committees and the council in the articles of association or other constitutional documents
- set clear criteria for appointing representatives to the boards of arm's-length organisations, their required skills and experience, and any payments to board members
- agree clauses to terminate or review the delivery arrangement at the outset, taking into account the impact on services and their users, employees, and assets.

## Keeping it right

Councils must ensure that council representatives involved in ALEOs:

- are aware of how well council objectives are being met by the ALEO
- carry out their scrutiny or management roles effectively, and take action on any shortcomings or under-performance
- are risk aware and satisfied that risks to the council and the ALEO are identified and acted upon
- act quickly on potential conflicts of interest, including declaring interests and seeking advice
- take action to withhold funding or to review or terminate the agreement, particularly where services or public money are at risk
- take action where the intended objectives of the ALEO are not being met, or diverge from council priorities
- periodically review their delivery arrangements to ensure that the best use is made of resources and that clear governance is in place
- review or wind-up ALEOs that are no longer active or effective, or contribute to the council's aims
- ensure that they have the skills and training to undertake their role.

### Examples of governance and operational issues to consider in options appraisal

Legal and governance	Business and operational
Is there a clear statutory basis for undertaking the activity?	Does the activity fit in with the council's objectives?
How will governance work – including the means of council control and representation?	What are the service implications, eg quality, access, marketability, pricing?
How will the ALEO be accountable to the community and the service user?	How will services users be involved and customer satisfaction measured?
How will the council demonstrate that the ALEO offers best value and assure that it accounts for all public money provided to the ALEO?	What are the financial implications, eg taxation, treatment of profits, ability to attract investment and residual liabilities for the council?
What are the implications of EU and other procurement law, for example on the award of the contract or service delivery agreement?	What is the payback time, allowing for initial set-up costs?
How will obligations including equal opportunities, best value and sustainable development, data protection and freedom of information be observed?	Are there benefits in sharing services with other councils or partners?
How will the delivery method be reviewed, and what is the basis for withholding funds or terminating the arrangement?	What will be the impact on demand, including the council's ability to subsidise any increase?
How will council employees and assets be treated including transfer arrangements and pensions?	How will flexibility or changes to delivery be allowed for?
What are the statutory financial reporting and auditing requirements?	What are the operational risks, including future changes in legislation or the marketplace?
	What management information will be shared by the ALEO to demonstrate financial control and best value?

Source: Audit Scotland