

Agenda Item	<b>19</b>
Report No	<b>RES/47/14</b>

**Internal Audit Report – Governance of Arm’s Length External Organisations**

**Report by Depute Chief Executive**

**Summary**

The findings of the audit review to identify the governance arrangements in place in relation to ‘Arm’s Length External Organisations’ (ALEOs) and to report on how well they comply with the Audit Scotland report, ‘Arm’s Length External Organisations’ (ALEOs): are you getting it right?’ were reported to the meeting of Finance, Housing and Resources Committee on 26 February 2014.

This report advises on the consultation undertaken with communities benefitting from Beinn Tharsuinn Windfarm Community Limited and the progress that has been made on meeting the recommendations that were made.

**1. Background**

1.1 The audit findings set out in the attached Appendix were reported to Audit and Scrutiny Committee and to the February 2014 Finance, Housing and Resources (FHR) Committee. The Action Plan agreed at the November 2013 meeting of the Audit and Scrutiny Committee was adjusted at February 2014 FHR meeting. This report updates Members on the consultation undertaken with the communities benefitting from Beinn Tharsuinn Windfarm Community Limited and upon the progress that has been made on achieving the recommendations.

1.2 As noted previously, the audit confirmed that the Council’s larger arm’s length external organisations (High Life Highland, Eden Court Highlands and Caledonia Community Leisure Limited) had well-developed governance arrangements in place and largely complied with the good practice guidance referred to in the Audit Scotland report. There was scope, however, to improve the Council’s oversight of those organisations, particularly those established a number of years previously, in order to ensure compliance.

**2. Beinn Tharsuinn Windfarm Community Limited**

**2.1 Background**

2.1.1 The Audit Report Action Plan finding in respect of Beinn Tharsuinn Windfarm Community Limited is:

“Beinn Tharsuinn Windfarm Community Ltd was set up by the then Area Manager to manage income received from the operators of the windfarm. All financial transactions are managed by Council staff using Council systems. The rationale behind this arrangement and the set-up of the company could not be established.”

2.1.2 The recommendation is:

“Consideration should be given to the reasons for the Council’s continuing input to this company with a view to investigating the possibility of transferring it to the Community and thus effecting a saving of Council resources.”

2.1.3 The Agreed Action is:

“Company Secretary to consult the developer and the Company Board of Directors regarding the transfer of the Company to community control.”

2.1.4 Beinn Tharsuinn Windfarm Community Limited is a Council-owned company that administers the community benefit fund from Beinn Tharsuinn Windfarm on behalf of ten beneficiary communities. Income depends on generation and is approximately £90,000 per year. The Company has a Board of Directors consisting of representatives of each of the ten communities. The Company is administered by a Company Secretary, who is the Ward Manager for East Sutherland and Edderton. The Company uses the Council’s Oracle financial system to process payments. Community Councils receive applications for funding and decide whether or not to award grants.

2.2 Future Structure of the Company

2.2.1 The Company Secretary has investigated the possibility of transferring the ownership of Beinn Tharsuinn Windfarm Community Limited to the ten affected communities. The Company Secretary met with the Board of Directors on three occasions: 8 April, 27 May and 1 July 2014, to brief the Board and to give them the opportunity to discuss the issue in their respective communities.

2.2.2 Highland Council’s preference was to retain Beinn Tharsuinn Windfarm Community Limited as a structure and transfer the ownership of the Company to the ten communities. The Developer (Scottish Power Renewables) indicated a willingness to deal directly with Community Councils, or a third party, or a mix of approaches.

2.2.3 The first and second preferences of the communities are set out in the table below. In summary, the first preference of two communities is to withdraw from Beinn Tharsuinn Windfarm Community Limited and receive their funding through an existing Trust (Kyle of Sutherland Development Trust). The first preference of the remaining eight communities is to maintain the status quo, i.e. Highland Council administers the Company. Six of these eight communities stated that if the Council did not continue to administer Beinn Tharsuinn Windfarm Community Limited, they would prefer their respective Community Councils to receive funds directly from the Developer. Of the remaining two, one community stated their second choice was to use the Kyle of Sutherland Development Trust and the other was undecided between receiving funds directly or through a Trust.

2.2.4

Community	First Preference	Second preference	
Ardross	Status quo	CB paid direct to CC	
KALE	Status quo	CB paid direct to CC	
Kiltearn	Status quo	CB paid direct to CC	
Creich	Fund admin by KofSDT*	No second preference	
Ardgay	Fund admin by KofSDT*	No second preference	
Tain	Status quo	Fund admin by KofSDT*	
Dornoch	Status quo	CB paid direct to CC	
Alness	Status quo	CB paid direct to CC	
Invergordon	Status quo	CB paid direct to CC	
Edderton	Status quo	Undecided: CB paid direct to CC or 3 <sup>rd</sup> party administrator	

\*KofSDT = Kyle of Sutherland Development Trust

## 2.3 Audit Requirements

2.3.1 The Auditors' recommendation that consideration is given to transferring ownership of the Company is based on both the cost to the Council and on concerns/risks associated with the continued operation of the Company by Highland Council.

## 2.4 Purpose of the Company

2.4.1 The principal issue raised by the Audit report was the rationale for the Council's operation of the Company. The Auditors noted that the Company was established and is managed using Council resources (see below), without clearly contributing to the Council's stated aims and objectives. Furthermore, the Auditors note that there is no recorded Committee decision approving the establishment of the company by Highland Council. The Auditors also note that, elsewhere in Highland, community benefit is managed by communities through trusts and that Beinn Tharsuinn is the only instance of a community benefit fund being managed by Highland Council

2.4.2 The auditors have also identified two specific risks associated with the continuation of the company as it currently operates.

## 2.5 Borrowing Powers

2.5.1 The Company's Memorandum and Articles of Association give unlimited borrowing powers to the Company Directors, without recourse to Highland Council. Furthermore, Highland Council, as the owner of the Company, would be liable for such borrowing. It is recommended that a review of the Company's Memorandum and Articles of Association is undertaken to limit or remove the risk to the Council

## 2.6 Large Balances

2.6.1 Two communities are accruing funds to establish a separate Trust Fund to establish a sustainable source of income. Whilst this is an objective that should be encouraged, there is no process in place for ensuring that the funds are paid into properly established and managed Trust Funds. This would mean that the Council would lose control over the use of funding paid to the Council by the Developer for a specific purpose. This would not be an issue if

control of the funds is passed to the communities as their use of the funds would be governed by a new agreement with the Developer specifying the uses to which the funding can be put.

## 2.7 Cost to the Council

2.7.1 The main cost to the Council is the staff time involved in administering the Company. This is undertaken by the Ward Manager for East Sutherland and Edderton. Based on the annual time requirement, the cost is estimated to be in the order of £1,500-£2,000 (inc. on-costs) per year. Additionally, there is a limited amount of Finance Service time required for processing payments and generating Company accounts from Oracle.

## 2.8 Conclusion

2.8.1 There is a majority community preference for the maintenance of the current position. Supporting this preference has to be counterbalanced against the issues and risks raised by the Council's Internal Audit and the cost to the Council of managing the Company. It is also of note that all of the communities have indicated that they are prepared to adopt alternate arrangements for the management of the Company should the Council decide not to maintain the current arrangements. The Developer has also indicated willingness to deal directly with communities.

## 2.9 Recommendation

2.9.1 Members are recommended to agree that the Council retains the Company, but to allow the communities of Creich and Ardgay to withdraw from the Company and administer their funds through the Kyle of Sutherland Development Trust, once agreements have been drawn up between the Developer and those two communities.

## **3. Action Plan progress**

3.1 The Director of Education, Culture and Sport has agreed a revised target date of 30 September 2014 with the Head of Internal Audit and Risk Management for the finalisation of Service Delivery Contracts (SDC) with Caledonian Community Leisure and Eden Court Highlands.

3.2 The duties of the Client Manager post within the new Care and Learning Service are under review. The purpose of the review is to allow greater focus on the key aspects of the role and less upon dealing with Community Learning and Leisure functions which have remained the responsibility of the Council. It is accepted that there is a need to make capacity for the Client Manager to more effectively fulfil the role of liaison officer with the key ALEOs. This review will be completed and implemented from September 2014.

3.3 In terms of the ALEOs themselves, High Life Highland's next audited financial statement will be for the year ended 31 March 2014. It will be submitted to the Education, Children and Adult Services Committee when finalised, as part of High Life Highland's regular reporting to the Council.

- 3.4 Caledonian Community Leisure Limited is scheduled to make a presentation to a meeting of the CLL Contracts Sub Committee in November. The draft SDC will be completed and agreed by that date. CCLL's most recent audited accounts will be included on that agenda.
- 3.5 Discussions with Eden Court are ongoing with a view to agreeing a form of SDC with the Council to complement the SDC Eden Court has with Creative Scotland. Arrangements will be made to include the most recent audited financial statement on the next occasion Eden Court is invited to make a presentation to the CLL Contracts Sub Committee and on an annual basis thereafter.
- 3.6 The Independent Museums Support Officer has been nominated as the Council's main liaison with Caithness Horizons and is in touch with the organisation on a regular basis. There are good examples of partnership working between the Council and Caithness Horizons and the organisation will be invited to make a presentation on its work to a forthcoming meeting of the CLL Contracts Sub Committee, which will include submission of its most recent audited financial statement.
- 3.7 The actions allocated to the Head of Corporate Governance have been substantially completed. The central register of ALEOs has been developed and will be maintained. A further training session for Members appointed to external organisations, including ALEOs, has been arranged for Friday, 26 September 2014.

#### **4. Implications**

- 4.1 There are potential risk and resource implications associated with the continued operation of Beinn Tharsuinn Windfarm Community Limited in its current form that are identified within the report. There are no legal, equalities, Gaelic, climate change/Carbon Clever or rural implications to be highlighted.

## **5. Recommendations**

### **5.1 Members are invited to:**

- i. in respect of Beinn Tharsuinn Windfarm Community Limited, AGREE that the Board of Beinn Tharsuinn Windfarm Community Limited should be asked to undertake a review of Memorandum and Articles of Association in order to address the risk identified at paragraph 2.5 above and
- ii. that the Council retains the Company in its current form and allows the communities of Creich and Ardgay to withdraw from the Company and administer their funds through the Kyle of Sutherland Development Trust, once agreements have been drawn up between the Developer and those two communities; and
- iii. NOTE the progress made to date in implementing the agreed Action Plan.

Designation: Depute Chief Executive

Date: 15 August 2014

Author: Stewart Fraser, Head of Corporate Governance/ Phil Tomalin,  
Ward Manager

Background Papers:

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The Action Plan contains **9** recommendations as follows:

### Description

Major issues that managers need to address as a matter of urgency.

Important issues that managers should address and will benefit the Organisation if implemented.

Minor issues that are not critical but managers should address.

Priority	Number
High	6
Medium	3
Low	0
<b>Total recommendations</b>	<b>0</b>

REPORT REF.	GRADE	FINDING	RECOMMENDATION	MANAGEMENT AGREED ACTION	IMPLEMENTATION	
					RESPONSIBLE OFFICER	TARGET DATE
3.1.1	High	The Council does not maintain a central register of all organisations that fall within the definition of being ALEOs	<p>A central register of ALEOs should be developed and maintained. The information on each organisation in such a register should include the following:</p> <ul style="list-style-type: none"> <li>Name of the organisation</li> <li>Relationship to the Council</li> <li>Members appointed</li> <li>Amount of funding including any in kind assistance</li> <li>Any other partners</li> <li>Name of Liaison Officer in the Council</li> <li>Name/contact details of Company Secretary</li> </ul> <p>Additionally, the following documents should be held on file for each company:</p> <ul style="list-style-type: none"> <li>Memorandum and Articles</li> <li>Service Level Agreement (SLA) or Service Delivery Contract (SDC)</li> <li>Property lease information (if applicable)</li> </ul>	Create Central Register to comply with recommendation of Internal Audit.	Head of Legal & Democratic Services	30/04/14

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			<ul style="list-style-type: none"> <li>• Risk Register</li> <li>• Current list of Directors and Management Team.</li> </ul>			
3.1.2	Medium	Training for Members appointed to external organisations is provided but the uptake is poor	The importance of initial and refresher training for Members should continue to be emphasised and Members actively encouraged to attend in order that they appreciate the importance of their role as a Council appointed Trustee or Director.	Board Development Days completed for CCLL, HLH, Eden Court & HOL in August & October 2013.	Head of Legal & Democratic Services	Complete
3.2.1	Medium	Beinn Tharsuin Wind Farm Community Ltd was set up by the then Area Manager to manage income received from the operators of the windfarm. All financial transactions are managed by Council staff using Council systems. The rationale behind this arrangement and the set-up of the company could not be established.	Consideration should be given to the reasons for the Council's continuing input to this company with a view to investigating the possibility of transferring it to the Community and thus effecting a saving of Council resources.	Company Secretary to consult the developer and the Company Board of Directors regarding the transfer of the Company to community control.	Corporate Manager	30/04/14 to complete investigation
3.2.2	High	The role of the Leisure & Learning Client Manager in relation to High Life Highland is not operating effectively	<p>(1) Annual financial statements for HLH should be provided to the Culture &amp; Leisure Contracts Scrutiny Sub-Committee.</p> <p>(2) The role of the Leisure &amp; Learning Client Manager needs to operate more effectively and this needs to be addressed by the following</p>	<p>Financial statements will be provided to C&amp;L Contracts Scrutiny Sub-Committee on an annual basis.</p> <p>The L&amp;L Client Manager post is currently under review in order to determine the</p>	<p>CLL Client Manager</p> <p>Director of ECS</p>	<p>When audited financial statements are available</p> <p>31/03/14</p>



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			actions: <ul style="list-style-type: none"> <li>• Documentation of the duties of the Client Manager</li> <li>• The provision of appropriate training for the Client Manager</li> <li>• Attendance at HLH Board meetings</li> <li>• Reviewing performance and financial information provided by HLH and addressing any issues as these arise.</li> </ul>	appropriate capacity to discharge responsibilities associated with the post, including the future relationships with Arms-Length Organisations.		
3.2.3	High	There has been limited financial and performance information reported to the Council by Caledonia Community Leisure Ltd.  The role of the Leisure & Learning Client Manager) in relation to Caledonia Community Leisure Ltd is not operating effectively	(1) The draft SDC should be finalised, approved and issued to CCLL at the earliest opportunity. It should incorporate detailed performance and financial information. (2) The information submitted in accordance with the SDC should be forwarded to the appropriate Service Finance Manager for analysis. A summary of this information should then be reported to the Culture & Leisure Contract Scrutiny Sub-Committee. (3) CCLL's annual Financial Statements should be reported to an appropriate Committee of the Council.	The SDC will be finalised, approved and issued at the earliest opportunity.  Agreed  Agreed	CLL Client Manager  CLL Client Manager  Director of ECS	31/03/14  As and when the SDC information is available  When audited financial statement

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			<p>(4) The role of the Leisure &amp; Learning Client Manager needs to operate more effectively and this needs to be addressed by the following actions:</p> <ul style="list-style-type: none"> <li>• Documentation of the duties of the Client Manager</li> <li>• The provision of appropriate training for the Client Manager</li> <li>• Attendance at CCLL Board meetings</li> <li>• Reviewing performance and financial information provided by CCLL and addressing any issues as these arise.</li> </ul>	The L&L Client Manager post is currently under review in order to determine the appropriate capacity to discharge responsibilities associated with the post, including the future relationships with Arms-Length Organisations.	Director of ECS	<p>s are available</p> <p>31/03/14</p>
3.2.4	High	<p>There is no reporting to a Council Committee on the financial or governance issues of Eden Court.</p> <p>No financial or governance information is published and available to the public.</p> <p>The Learning and Leisure Client Officer is the Liaison officer within Highland Council but it is not clear that his remit includes Eden Court.</p>	<p>(1) Company information (similar to that which is available for HLH) should be published on the Eden Court Website. This would allow interested parties to access performance, financial and governance information on the organisation. This is considered appropriate where an organisation is receiving substantial public funding that</p>	Discuss with Eden Court the appropriate level of financial disclosure and governance information which could be made available.	Director of ECS	<p>31/03/14</p> <p>31/03/14</p>

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			<p>enables it to remain a going concern.</p> <p>(2) The draft SDC should be finalised, approved and issued to CCLL at the earliest opportunity. It should incorporate detailed performance and financial information.</p> <p>(3) The information submitted in accordance with the draft SDC should be forwarded to the appropriate Finance Manager for analysis. A summary of this information should then be reported to the Culture &amp; Leisure Contract Scrutiny Sub-Committee.</p> <p>(4) Eden Court Theatre annual Financial Statements should be reported to an appropriate Committee.</p> <p>(5) The role of the Leisure &amp; Learning Client Manager needs to be clarified and operate effectively. This should be addressed by the following actions:</p> <ul style="list-style-type: none"> <li>• Documentation of the duties of the Client Manager</li> <li>• The provision of appropriate training for the Client Manager</li> </ul>	<p>The SDC will be finalised, approved and issued at the earliest opportunity.</p> <p>Agreed</p> <p>Agreed</p> <p>The L&amp;L Client Manager post is currently under review in order to determine the appropriate capacity to discharge responsibilities associated with the post, including the future relationships with Arms-Length Organisations.</p>	<p>CLL Client Manager</p> <p>CLL Client Manager</p> <p>Director of ECS</p> <p>Director of ECS</p>	<p>As and when the SDC information is available</p> <p>When audited financial statements are available</p> <p>31/03/14</p>

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			<ul style="list-style-type: none"> <li>Attendance at Eden Court Board meetings</li> <li>Reviewing performance and financial information provided by Eden Court and addressing any issues as these arise.</li> </ul>			
3.2.5	High	The Board of Directors of HOL is made up 9 Directors, all of whom are Council Members. Unlike HLH and CCLL, there are no independent Directors. It is, therefore, important that the Members appointed have the necessary skills to perform their roles effectively	When appointing Council Members to external organisations, the main criteria should be the skill set, expertise and qualifications that each appointee brings to the Board of the Company thereby complying with best practice as identified by Audit Scotland.	Agree Criteria to be used when making appointments to HOL Board.	Head of Legal & Democratic Services	April 2014
3.2.6	High	Caithness Horizons receives direct funding of £104,561 and rent free accommodation worth £61,000. No Memorandum & Articles or Liaison Council Officer could be identified. The funding is to continue for another 5 years and a robust reporting procedure implemented. At the time of the review it was agreed that ECS would take responsibility for the organisation.	<p>(1) A copy of the Memorandum and Articles for the Organisation and all other documentation should be requested and retained as noted at section 3.1.1.</p> <p>(2) A copy of the reporting requirement with a specific timeframe should be developed and implemented at the earliest opportunity.</p> <p>(3) Future funding of the organisation should be considered and discussed with the organisation in advance of the current end date in order that steps can be taken to decrease its dependency on public sector funding.</p>	<p>A copy has been obtained and is available.</p> <p>The appropriate reporting framework will be incorporated in the SDC.</p> <p>Discussions on future funding will be progressed over the next 15 month period</p>	<p>Completed</p> <p>CLL Client Manager</p> <p>Director of ECS</p>	<p>31/03/14</p> <p>31/03/15</p>

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			<p>(4) As ECS have now taken responsibility for the oversight of Caithness Horizons, future reports should be provided to the Adult and Children's Services rather than the PED Committee. The Council's Scheme of Delegation should be also amended to reflect this change.</p> <p>(5) The Learning &amp; Leisure Client Manager should be appointed as the Council Liaison Officer. In common with previous recommendations there should be:</p> <ul style="list-style-type: none"> <li>• Documentation of the duties of the Client Manager</li> <li>• The provision of appropriate training for the Client Manager.</li> </ul> <p>And his duties should include:</p> <ul style="list-style-type: none"> <li>• Attendance at Board meetings</li> <li>• Reviewing performance and financial information provided by Caithness Horizons and addressing any issues as these arise.</li> </ul>	<p>Agreed</p> <p>The L&amp;L Client Manager post is currently under review in order to determine the appropriate capacity to discharge responsibilities associated with the post, including the future relationships with Arms-Length Organisations.</p>	<p>Director of ECS</p> <p>Director of ECS</p>	<p>When audited financial statements are available</p> <p>31/03/14</p>
3.3.1	Medium	No evidence was identified to indicate that criteria had been set in relation to skills or expertise required of members for appointment to the	(1) Clear criteria should be set for the skills and expertise required of members being appointed to ALEO boards.	Criteria in place for HLH, to be agreed for other ALEOs.	Head of Legal & Democratic Services	30/04/14

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		<p>board of any of the ALEOs</p> <p>Council Members can be appointed to the Boards of external organisations centrally by Council/ Committee or locally at Area Committee Meetings.</p> <p>There is no comprehensive list of all organisations to which Council Members are appointed.</p> <p>Member's profiles on the Council website may not accurately reflect their responsibilities in relation to external organisations. Training needs may not be identified.</p>	<p>(2) Appointments to external organisations made at Area Committee Meetings should be notified directly to the Service with responsibility for the organisation. Prior to any appointments being made, it should be considered whether there is need for any Council representation.</p> <p>(3) A comprehensive list of all external organisations with Council representation on their Board should be compiled and maintained centrally.</p> <p>(4) Members should be reminded to ensure that their profiles on the Council's website accurately reflect their responsibilities in relation to external organisations.</p>	<p>Procedure to be agreed.</p> <p>See 3.1.1</p> <p>Letter sent to all Members every 6 months to remind them to update their register.</p>	<p>Corporate Manager/Senior Ward Managers</p> <p>Head of Legal &amp; Democratic Services</p>	<p>30/04/14</p> <p>Complete</p>