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Date: 24 February 2014

Dear Member

**GOVERNANCE AND AUDIT COMMITTEE TRADING ACTIVITIES SUB - COMMITTEE -
MONDAY, 3 MARCH 2014**

I am now able to enclose, for consideration at next Monday, 3 March 2014 meeting of the Governance and Audit Committee Trading Activities Sub - Committee, the **tracked changed version** of Appendix 1 to item 7.

Agenda No	Item
7	<u>Protocol for companies in which KCC has an interest</u>

Yours sincerely

A handwritten signature in black ink, appearing to read 'Peter Sass', is written over a light blue horizontal line.

Peter Sass
Head of Democratic Services

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Protocol relating to companies in which KCC has an interest

1. In relation to companies in which the Council has an interest, it is imperative that they are set up, managed and run according to rules of good governance so that risks are mitigated. This Protocol aims to establish processes and provide additional controls to ensure such rules are in place.
2. Anyone within the Council intending to set up a company should refer to the ['Guidance on Local Authority Companies'](#) document on KNET. A robust business case must be provided which gives a cost benefit analysis, considers the accounting and tax implications for the Council and identifies any risks to the Council. The business case must go through the Governance and Audit Committee Trading Activities Sub Committee who will examine this and make recommendations. In light of the recommendations the relevant Cabinet Member shall approve the company's business case. Where the company is intending to exercise the power to trade pursuant to section 95 of the Local Government Act 2003, the business case shall contain enough detail to satisfy the requirements of this Act and be similar to that required by the Council for major capital projects.
3. This Protocol relates to the following companies:
 - (a) in the case of companies with issued share capital, those companies in which the Council's interest is more than 1% of the issued share capital, where those shares are held other than for solely investment purposes
 - (b) in the case of any company without shares, where the Council is a member
 - (c) any company of whatever sort in which the Council nominates one or more directors or itself is (or has the right to be) a company director
4. In the case of a company formed or controlled by the Council (or where the Council has, or can reasonably have, input into the wording of the Memorandum and Articles), the following provisions must appear in the company's Articles:
 - (a) The registered office shall be specified as: Sessions House, County Hall, Maidstone, Kent ME14 1XQ (care of the Corporate Director of Finance and Procurement).
 - (b) The Corporate Director (or Managing Director) within whose remit the company's business lies shall be responsible for nominating a secretary for the company from among his/her staff. A register of all company secretaries will be maintained.
 - (c) Any Member or officer of the Council who is appointed as a director or secretary of that company shall not be appointed in their own private capacity but shall be appointed as a nominee of the Council, which shall have the power to remove and replace such director or secretary as it may see fit.

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- (d) It shall be the responsibility of the Council's representative on the board [or the Corporate Director within whose remit the company's business lies](#) to make whatever arrangements may be necessary to ensure the company makes a full annual report of its activities to the Cabinet within three months after the end of its financial year.
 - (e) No Member or officer of the Council who is appointed as a director or secretary of that company (or who represents the Council at any meeting of the company or of the board) shall receive any income from the company unless the Council's Corporate Director of Finance and Procurement so agrees in writing in advance. If any income is received by a Member or officer, it must be documented in the relevant Register of Interests and published on the Council's website.
5. In respect of any company to which this Protocol applies the following rules shall also apply (even if not included in the company's Articles):
- (a) Any director of the company who is nominated by the Council (and any person authorised to represent the Council at a meeting of the company or of the board) shall be appointed by the Cabinet or relevant Cabinet Member in accordance with the decision making procedures set out in the Council's Constitution.
 - (b) Any person authorised to represent the Council at a meeting of the company (where the Council is a member of the company) or of the board (where the Council is a director of the company) shall follow such directions as to the operation of the company as may be determined by the Cabinet or relevant Cabinet Member from time to time in accordance with the decision making procedures set out in the Council's Constitution.
 - (c) Directors nominated by the Council shall (so far as permitted by law and their duties to the company as directors) follow such directions as to the operation of the company as may be determined by the Cabinet or relevant Cabinet Member from time to time in accordance with the decision making procedures set out in the Council's Constitution.
 - (d) Members or officers representing the Council on any board shall only take decisions which are in accordance with the company's articles and any Council policies that are to apply to the company.
 - (e) Where Members or officers of the Council incur expenses as a result of their involvement in the company, this shall be claimed by them from the company as the Council's Corporate Director of Finance and Procurement may direct.
6. In any situation where a Member or officer of the Council (or any member of their close family) is (in their private capacity) a member, director or secretary of a company of which the Council is also a member or director, or in respect of which the Council has the right to nominate one or more directors, then such Member or officer shall notify the Corporate Director of Finance and Procurement of this in writing as soon as they become aware of the same. These should be documented in the relevant Register of Interests or Statement of Related Party Transactions. The purpose of this is to prevent the company becoming a local authority company without the Council becoming aware of it.

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7. The Council shall only become a member or director of a company following a decision of the Cabinet or relevant Cabinet Member taken in accordance with the decision making procedures set out in the Council's Constitution. When seeking such a decision any report to the Cabinet or relevant Cabinet Member shall state:
 - (a) the Council's rights of membership and to nominate directors (or to itself become a corporate director)
 - (b) the purpose of the company and of the Council's involvement
 - (c) the identity of the initial nominated directors and secretary and any person who is intended to be authorised to represent the Council at a meeting of the company (where the Council is a member of the company) or of the board (where the Council is a corporate director of the company)
 - (d) what Council policies (if any) are to apply to the company. If no policies have been stated in the Member decision and the company directors do not formally set their own, the policies adopted should default automatically to KCC policies. Where a company adopts its own policies, assurance must be provided [to the Governance and Audit Committee Trading Activities Sub Committee](#) that adequate policies and procedures are in place, with particular reference to anti-fraud and corruption
 - (e) that appropriate due diligence has been completed which must include an evaluation of the background, experience and reputation of the company and/or the proposed and existing directors
 - (f) any other limits the Councils' Corporate Director of Finance and Procurement or Monitoring Officer recommend be placed on the activities of the company.
8. Once the decision process is completed, the company shall be formed and the Council Members and officers involved with the company shall ensure (so far as it is within their remit) that the relevant policies are applied by the company.
9. This Protocol shall also apply to companies already in existence and as regards such companies:
 - (a) a decision dealing with all the relevant matters set out in this Protocol is to be taken under the decision making procedures set out in the Council's Constitution by Cabinet or the relevant Cabinet Member as soon as reasonably practicable, and
 - (b) the Articles to such companies shall (where appropriate and reasonably practicable) be amended as soon as possible.
10. Both as regards companies already in existence and companies yet to be formed, all Members and officers of the Council should, from the date of adoption of this Protocol, act (so far as is reasonably practicable) as if the Articles had already been amended as required by this Protocol, whether or not this has in fact happened.

11. Companies in which KCC has an interest must pass a resolution of the company to provide Internal Audit with all information and explanations (in the specified format) required to perform internal audits of the companies and participate in the Audit Commission's (or successor body's) National Fraud Initiative data matching exercise. In addition, the Members and officers of the Council who are running KCC companies must seek appropriate advice from time to time to ensure that:

(a) they and the company are operating within the law, specifically where they intend to change or expand the business activities of the company

(b) they are aware of the extent of their potential personal liabilities, conflicts of interest and any indemnities or insurance cover provided by KCC that may apply to them.

12. KCC Legal Services and KCC Finance between them have produced 'Guidance on Local Authority Companies' that covers these issues in detail and will update and expand this as necessary from time to time.

13. In order that Members and officers of the Council can be fully aware at all times of the extent of KCC's interests in local authority companies and their exposure to potential legal, financial and reputational risks, the Corporate Director of Finance and Procurement shall maintain an accurate, complete and up-to-date record of all companies in which KCC has an interest, clearly identifying those that are trading. Members and officers of the Council are required to supply timely information to the Corporate Director of Finance and Procurement so as to ensure that these records can be fully and properly maintained.

14. Pursuant to Part II of the Local Authorities (Companies) Order 1995, where a company is regulated by KCC (i.e. KCC either controls or has serious influence over it) then the company must:

(a) provide any Member of the council who requests it such information as that Member reasonably requires for the proper discharge of their duties (but not so as to require breach of any law or of any obligation to a third party)

(b) (only if it is a KCC controlled company) before it first appoints any person as auditor of the company obtain the Audit Commission's (or successor body's) consent to the appointment of that person.

Note (i) A Controlled Company is a company (a) which is a subsidiary of a Local Authority or (b) in which a Local Authority controls the majority of votes at a general meeting or (c) in which a Local Authority has the power to appoint/remove a majority of the Board or (d) which is under the control of another company which is itself a controlled company.

(ii) An Influenced Company is a company (a) in which a person associated with a Local Authority controls 20% or more of the votes at a general meeting or (b) in which 20% or more of the directors are persons associated with a Local Authority (i.e. employees and members) or (c) in which 20% or more of the voting rights at Board meetings are held by persons associated with a Local Authority.

Deleted: Members and officers of the Council who are running KCC companies must pass a resolution of the company to provide Internal Audit with all information and explanations required to perform internal audits of the companies from time to time. In addition, they must seek appropriate advice from time to time to ensure that:¶
(a) they and the company are operating within the law, specifically where they intend to change or expand the business activities of the company¶
(b) they are aware of the extent of their potential personal liabilities, conflicts of interest and any indemnities or insurance cover provided by KCC that may apply to them.¶

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15. Members and officers representing the Council on the board of any company will at all times comply as appropriate with the County Council's Code of Member Conduct and the Officers Code of Conduct as set out in the Constitution from time to time.
16. Under Appendix 2 Part 2 of the Council's Constitution, the Selection and Member Services Committee is responsible (inter alia) for "making appointments and nominations on behalf of the Council to serve on outside bodies (except those needing to be made by the Leader in connection with a delegation by him of his functions, the list of those appointments to be agreed between the Leader and the Committee from time to time)". Where a decision to appoint rests with the Leader, then the formal decision of the Cabinet or relevant Cabinet Member under paragraph 6 of this Protocol shall act as such appointment. Where the decision rests with the Selection and Member Services Committee, then such appointment shall not take effect unless and until the Committee has resolved to make such appointment.
17. Company directors' duties are codified in Companies Act 2006. There are seven specific duties:
- (a) to act within powers
 - (b) to promote the success of the company
 - (c) to exercise independent judgement
 - (d) to exercise reasonable skill and care
 - (e) to avoid conflicts
 - (f) not to accept benefits from third parties
 - (g) to declare any interest in a proposed transaction
18. As a matter of general principle, the overriding duty of any director in considering an item before the company is to vote in accordance with the interests of that company. In the case of a director who is also an elected Member, or an officer of KCC, this might give rise to a conflict with the interests of KCC.
19. Directors and company officers are responsible for keeping accounts and making relevant returns to the Registrar of Companies, and in addition are required to lodge a copy of the Companies House Annual Return (showing directors and ownership) and a copy of each set of Statutory Accounts submitted to Companies House with KCC Legal Services and KCC Finance.
20. Elected Members and council officers are under a specific obligation (under the Local Authorities (Companies) Order 1995) to report back to the council through the Trading Activities Sub Committee on their involvement in outside companies to which they have been nominated by KCC. Any changes to companies' structure should also be reported to this Sub Committee.
21. Various breaches of obligation can lead to a director having personal liability or being disqualified from acting as a director. In particular, failure to declare an interest is a criminal offence.
22. KCC's insurance arrangements do not provide an indemnity for Members and officers involved with outside bodies when they act:

Deleted: provide any Member of the council who requests it such information as that Member reasonably requires for the proper discharge of their duties (but not so as to require breach of any law or of any obligation to a third party).¶

- (a) solely on behalf of an outside body
 - (b) outside their delegated powers, i.e. in a decision-making capacity rather than as advisors or observers
 - (c) outside the authority's statutory powers
23. Companies should purchase directors' and officers' liability insurance to protect their directors and officers against claims of negligence, breach of duty, trust, default, etc. Directors should liaise with the company to ensure that such a policy of insurance is maintained at all times, and covers the director as much as it can.
24. KCC may exceptionally give a wider indemnity to specific members/officers where the council specifically requires that person to become a director for KCC business reasons. KCC would insist that such a wider indemnity only dealt with anything not covered by the company's insurance.
25. More detail on indemnities and insurance can be found in the advice note "Members & Officers Indemnity" prepared by the Finance Unit to which reference should be made.
26. There can be a tendency to assume that a new venture requires a new legal entity, and that therefore a new project should be commenced in a new company. This is not necessarily the case. There is a limited number of situations where a limited company might be appropriate, namely:
- (a) Where there is trading to be carried out under the provisions of section 95 of the Local Government Act 2003. Section 95 provides a specific power to trade but the Act says that such trading must be carried out through a limited company. It must be noted that not all trading by KCC is necessarily under the provisions of Section 95. There are other cases where trading can be carried on under other powers (and where therefore a limited company may not be needed). Examples of these other powers are:
 - i. Where what is being done is the provision of goods and/or services to another public body under the provisions of the Local Authorities (Goods and Services) Act 1970, whether a particular organisation is a public body for the purposes of that Act is specified in regulations.
 - ii. Where what is being done is incidental to the main function that is being carried out. An example of this might be a library occasionally selling books as part of a promotion of reading. This power will be fairly tightly interpreted. If the main purpose of the activity is to raise money that will not be considered incidental to the original function.
 - iii. Where what is being done is use of surplus capacity. An example might be a council landscape service having raised too many plants and selling off the surplus to the public. If the activity requires the taking on of additional staff or the procurement of new services or equipment then it will almost certainly not come within this category.
 - (b) Where for some other specific reason it is advised that a limited company be formed. Typically these reasons will include the wish to take the activity out of the mainstream of KCC activity – either so as to

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encourage external funding or involvement, or to permit employment of staff outside KCC's usual terms and conditions for directly employed staff, e.g. Kent Top Temps.

27. Whatever power is being used, and whether a company is being formed or not, care must be taken not to exceed the scope of activity permitted by such powers.

28. More detail on companies generally can be found in the advice note "Local Authority Companies" prepared by the Corporate Director of Finance and Procurement and the Director of Governance and Law to which reference should be made.

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