

By: Neeta Major, Head of Internal Audit

To: Governance and Audit Committee Trading Activities Sub Committee – 3 March 2014

Subject: **UPDATE ON COMMERCIAL SERVICES' GOVERNANCE ARRANGEMENTS**

Classification: Unrestricted

Summary: This report provides an update on Commercial Services' Governance arrangements.

FOR ASSURANCE & DECISION

Introduction

1. In September 2012 and March 2013, papers were presented to this Committee by the Cabinet Member for Environment, Highways and Waste and the Corporate Director of Enterprise & Environment outlining the governance arrangements in place over Commercial Services from 1 April 2013.
2. The purpose of this paper is to update the Committee on further developments and progress since that date from the shareholder's perspective.
3. As a significant part of Commercial Services' business is conducted on Kent County Council's behalf, this Committee may wish to receive regular updates going forward. The Committee will need to determine how it receives these updates in future.
4. For the purposes of this paper the term "Shareholder" is used to represent the Council.

Background

5. Commercial Services ("CS") was set up nearly 70 years ago as a School Supplies Division. Since then it has grown, supplying an increasing range of goods and services to other publicly funded organisations including Local government, education, establishments, the care sector and emergency services. Prior to 1 April 2013, Commercial Services was effectively a non-budget funded division of the County Council which made a net return to KCC central funds of £7m in May 2012.
6. In 2011, the Cabinet Member for Environment, Highways and Waste and the Corporate Director for Enterprise & Environment commissioned an external

appraisal of the management, operations, governance and future business potential of Commercial Services.

7. On issue of their recommendations, Commercial Services commenced a transformation programme to improve its governance structure and focus on sustainable, viable, and profitable activity. This included simplifying its corporate structure from 1 April 2013 to operate Commercial Services (CS) trading from two legal entities, Commercial Services Kent Ltd and Commercial Services Trading Limited (which are both wholly owned by Kent County Council through an intermediary holding company – Kent County Trading Limited).
8. CS (Kent) Limited has been set up to trade exclusively with the Council as a 'Teckal'¹ compliant company under a managed service arrangement whereas CS (Trading) Limited has been set up with the intention of trading with the wider public and private sectors. The managed service arrangement includes the provision of Energy services and Education supplies, two material areas of Commercial Services' business. Given this managed service arrangement, CS (Kent) Limited maintains a separate balance sheet for those assets managed on KCC's behalf. This balance sheet is included at the year-end in KCC's financial statements.
9. As part of its transformation, Commercial Services reconfigured the existing 26 disparate business units into five client facing divisions operated by the two legal entities:
 - Education Supplies – supplying stationery, art & craft materials, furniture and office equipment to schools and nurseries
 - Care - specialising in care recruitment, home care and mobility/living aids equipment (closed in December 2013)
 - Recruitment – the Connect2Staff division deals with permanent, temporary and contract vacancies predominantly in Kent and the South East
 - Energy – dealing within the UK energy buying market to purchase energy on behalf of its public sector customers and also providing an energy broking service
 - Direct Services - comprises a number of businesses operating across a wide range of activities including landscaping, vehicle services, community equipment services, assistive care technologies and facilities management.

¹ This is a provision that allows a public body to avoid EU procurement rules and directly enter into a contract with a service provider as long as certain conditions are met.

Company Boards and Committees

10. There are four legal entities in the Commercial Services (“CS”) group:

Company Name	Holding company/ organisation	Status
Kent County Trading Limited	Kent County Council	Holding company for Commercial Services group of companies
Commercial Services Kent Limited	Kent County Trading Limited	“Teckal” compliant company providing a managed service primarily to KCC
Commercial Services Trading Limited	Kent County Trading Limited	Company providing goods and services to the private sector and wider public sector
Kent Top Temps Limited	Kent County Trading Limited	Recruitment business transferred to the two main trading companies. Bus and transport operation is in process of being wound down.

11. For the two main legal entities, a joint Company Board is in operation but separate minutes are recorded for each. The composition is the Chair (a Non-executive Director (“NED”) who has the casting vote), 2 other NEDs, the Managing Director of CS, CS Chief Operating Officer, CS Group Finance Director and CS Planning Director (who has no voting rights). Hence the majority of votes lie with the independents though the third NED appointment is yet to be finalised. Board meetings are held eight times per annum.
12. Currently there is no KCC officer or Member appointed to the Boards of these companies. Hence in order to improve accountability and governance, in February 2013, the Section 151 officer requested that an agreement be put in place between the Companies, its directors and the Council. The overall objective of the agreement was to formalise the level of delegation to Company Directors and officers thereby setting out the level of risk appetite that the Council has for these companies and ensuring greater transparency and access to information. These agreements were drafted by KCC Legal and were approved by the Shareholder Board in December 2013. They are in the process of being finalised with the Directors at Commercial Services. Once in force, they will significantly enhance and clarify the existing arrangements.

Appointment of Non-Executive Directors

13. To ensure scrutiny of the Board Directors and decision making, KCC has led a process to appoint Non-Executive Directors to the Boards of the two main legal entities, CS Kent Limited and CS Trading Limited. The formal selection panel comprised Head of Paid Service, Corporate Director of Enterprise & Environment and two Cabinet Members who also sit on the shareholder board. Two highly qualified NEDs have been appointed and interviews for a

third NED are currently taking place. One of the NEDs serves as the Chairman of the Boards.

Sub Committees

14. Two subcommittees of the Board have been very recently set up in January 2014 as follows:

Remuneration Committee – will meet quarterly and will be chaired by a NED with membership by the Chairman of the boards, the CS Group Finance Director and the CS Head of HR.

Audit Committee – will meet quarterly and will be chaired by a NED, with additional members being the Chair of the Board and the KCC Head of Internal Audit. The CS IA Manager will attend this committee routinely.

15. Terms of reference for these sub committees to the Board have been drafted and are soon to be finalised.

Shareholder Board

16. In addition to the Boards of the companies, a Shareholder Board comprising Head of Paid Service, Corporate Director of Enterprise & Environment, Section 151 officer and three Cabinet Members meets quarterly. The purpose of this Board is to inform, advise and make recommendations to the Cabinet Member responsible for Commercial Services. This Board currently receives narrative updates on CS activity including financial results. The Terms of Reference have recently been updated and are in the process of being reviewed and agreed.

Internal Audit arrangements

17. The Commercial Services Internal Audit manager (essentially the Head of IA at CS) was appointed by Commercial Services management and reports to the CS Executive Board Directors and the newly appointed CS Audit Committee. She is supported by two members of staff, (another qualified senior internal auditor and a trainee). She meets monthly with the KCC Head of Internal Audit to provide updates on emerging risks and assurance activity being undertaken by her team.
18. The KCC Head of Internal Audit annually reviews the degree of reliance that can be placed on the work of CS Internal Audit and undertakes additional reviews and risk assessments as necessary. Commercial Services are required to report all allegations of fraud or irregularity to KCC Internal Audit for further enquiries and/or investigation. This will involve CS Internal Audit and CS management as necessary. The recent introduction of the CS Audit Committee will considerably enhance the independence of the CS Internal Audit function. This in turn should increase the degree of reliance KCC Internal Audit can place on their work.

Recommendation

19. Members are asked to:

- Note the content of this report for assurance
- In light of this paper, consider what, if any, additional assurances the Committee would like in relation to governance arrangements for the Commercial Services group going forward.

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