



Council name	COTSWOLD DISTRICT COUNCIL
Name and date of Committee	AUDIT COMMITTEE – 28 JANUARY 2021
Report Number	AGENDA ITEM 15
Subject	CHANGES TO GOVERNANCE ARRANGEMENTS AT SWAP INTERNAL AUDIT SERVICES LTD
Wards affected	All
Accountable member	Cllr. Mike Evely Deputy Leader and Cabinet Member for Finance
Accountable officer	Jenny Poole, Chief Finance Officer Jenny.Poole@cotswold.gov.uk 01285 623313
Summary/Purpose	For Members to receive details of changes to governance arrangements taking place in SWAP Internal Audit Services.
Annexes	Annex A – Amendment to SWAP Internal Audit Reserved Matters
Recommendation/s	<i>That the Committee:</i> <i>a) Notes the changes to the SWAP Governance arrangements; and</i> <i>b) Recommends to Cabinet that delegated authority is granted to the Chief Executive to sign the updated Members Agreement.</i>
Corporate priorities	Ensure that all services delivered by the Council are delivered to the highest standard.
Key Decision	No
Exempt	No
Consultees/ Consultation	The Council's Chief Finance Officer is a director of SWAP and was involved in the development of the proposals to the SWAP Member Board. The Chair of the Audit Committee represents the Council and attended the SWAP Owners Board meeting on 16 December 2020 when the proposed changes were considered.

1. BACKGROUND

- 1.1.** This Council is a Member of SWAP Internal Audit Services, which operates as a Teckal company and provides the Council's internal audit service. SWAP was incorporated in 2012, and since then has attracted a large number of new Members, both additional councils and police Members.
- 1.2.** SWAP was incorporated in line with good governance practice with documentation enshrining the key oversight role of the Member authorities. This role primarily included two strands of control; firstly, the ability for each Member to appoint a director to sit on the board, and secondly the referral of 'reserved matters' back to the Members for decision. The Council's Chief Finance Officer is a SWAP director and the Chair of the Audit Committee represents the Council on the Members Board.
- 1.3.** As a result of the number of Members increasing, the number of attendees on the board became difficult to manage and in July 2017 SWAP amended its articles to allow new classes of Members who would collectively appoint a single director. This change has now impacted upon police Members to date. Despite this amendment, SWAP now has 19 directors registered at Companies House and has had 32 resignations since incorporation.
- 1.4.** The nature and scope of SWAP has changed significantly since its incorporation, and to ensure that it is operating within best practice and in a way which is conducive and supportive of its continued service delivery, SWAP has approved a change in the governance structure of the company.
- 1.5.** The new structure has been designed to offer concise and strong decision making, allowing adaptive and resilient business management while retaining the Member control required to meet the Teckal/Regulation 12 test and allow the Members to directly appoint SWAP as their audit provider without undertaking a competitive process.

2. MAIN POINTS

- 2.1.** SWAP has approved the following changes to its governance arrangements.
 - 2.1.1.** The maximum number of directors for the SWAP Board of Directors will be 9.
 - 2.1.2.** The mechanism for appointing directors will be a reserved matter.
 - 2.1.3.** The maximum number for independent directors will be 3.
 - 2.1.4.** The mechanism for appointing independent directors will be a reserved matter.
 - 2.1.5.** Police Members will going forward receive individual Member votes.

Board of Directors

- 2.2.** The number of directors is reduced to 9, to make it easier to call and manage director meetings and to allow for greater oversight of matters for those directors who are appointed. The directors will comprise of a maximum of four from the Partners, two from SWAP and three independent Non-Executive Directors.
- 2.3.** In order to show the necessary control elements required for Teckal exemption on a smaller board, the appointment of non-executive directors will be undertaken collectively by the Members.
- 2.4.** The appointment of directors will be a new decision to be taken by the Members made as a reserved matter, requiring agreement of 50% of Members.

- 2.5. The introduction of independent directors can increase the diversity of skills within the board and ensure that the company is benefitting from a wide variety of views. This will also help SWAP to ensure that the skills gap that currently exists on the Board of Directors is filled.
- 2.6. Independent directors will be appointed following an open recruitment process. A person specification will be developed, based on skills required for an effective Board of Directors, advertised and interviews undertaken to choose the most appropriate independent directors.
- 2.7. The recruitment process will be undertaken by directors, but the interview panel and approval of the appointment will be undertaken by the Members, as for non-executive directors as set out above.

Reserved Matters

- 2.8. Since the drafting of the reserved matters in 2012, the scope, value and frequency of corporate transactions undertaken by SWAP have increased significantly. As a result, the values set within the reserved matters no longer reflect the risk profile of the company and the SWAP Owners Board approved an increase to the levels.
- 2.9. Matters relating to the appointment and management of staff, and minor accounting elements have also been removed from the reserved matters, making them decisions for the board of directors.
- 2.10. Some 'Special Reserved Matters' requiring unanimous agreement of the Members have been changed to 'Reserved Matters'. These changes are set out in full in **Annex A** to this report.
- 2.11. Browne Jacobson have advised that, because none of these reserved matters affect the overall control of the company, these amendments may be made without affecting the Teckal compliance of the Company.

Process for Amendment

- 2.12. Incorporation of the amendments set out in this report will require changes to both the Articles of Association and the Members Agreement.

Articles of Association

- 2.13. The procedure to amend a company's Articles of Association is laid out in the Companies Act 2006 and is subject to any bespoke rules that the company has created itself. SWAP's existing Articles have created additional procedural requirements and made adjustments to voting rights.
- 2.14. Once the proposed amendments to the Articles have been drafted, the directors must convene a Board meeting to formally agree on the amendments and to propose that the revised Articles are put to the members for approval and adoption.
- 2.15. To obtain member approval, the directors will need to decide whether to call a general meeting or to circulate a written resolution.
- 2.16. Section 21(1) of the Companies Act 2006 states that any amendments to the Articles must be approved by the members of the company by special resolution (e.g. a 75% majority). However, clause 10.2 of the Members Agreement (which applies Schedule 2, Part 1, Paragraph 2) makes any alteration to the Articles a 'Special Reserved Matter' requiring unanimous agreement of the members.

Therefore, the purpose of this clause is to amend the standard position as set out in section 21(1) of the Companies Act 2006 and so SWAP should seek to obtain unanimous agreement from its members to adopting the new Articles.

2.17. The new Articles will be formally adopted and take effect on the date that the all members have signified their agreement.

2.18. Within 15 days of unanimous agreement being obtained, a copy of both the new Articles and a memorandum confirming the unanimous agreement must be filed with Companies House.

Members Agreement

2.19. The Members Agreement is a contractual arrangement between all of the members of SWAP. The agreement has been entered into in the form of a Deed. Clause 20 states that the Members Agreement may be varied by writing that is duly signed by the members and SWAP. Unanimous agreement will be required, and the variation could be recorded in a deed of variation.

2.20. The “Members” of SWAP are defined as those existing organisations who were members at the time the Members Agreement was entered into, plus any new members who have since joined. Therefore, the members will be those organisations whose details are recorded in the register of members at the time the variation is to take place.

2.21. As the Members Agreement is contractual relationship entered into between all of SWAP’s members, in this instance, each member must individually signify their agreement to the variation as a ‘party’ to the Members Agreement.

Key milestones and timetable

Item	Responsible Body	
Consideration of proposed amendments and formulation recommendation to Owners	Board of Directors	30 November 2020
Consideration of recommendation by Owners	Owners Meeting	16 December 2020
Redrafting of corporate documents in accordance with Owners Decisions	Browne Jacobson	8 January 2021
Adoption of amended Articles of Association	Owners	Anticipated circulation date 29 January 2021
Signature of Amendment to Members Agreement	Owners	Return date (to be set in circulation) mid-February

Filing amended Articles and resolution at Companies House	Company Secretary/Browne Jacobson	End of February
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- 2.22.** The Audit Committee is responsible for oversight of the Council's internal audit service. The Committee is asked to note the change of governance arrangements, which has already been approved by the SWAP Members Board and recommend to Cabinet approval. The Committee is further requested to recommend that authority is delegated to the Chief Executive to sign the new Membership Agreement, updated to reflect the changes set out in this report.

3. FINANCIAL IMPLICATIONS

There are no financial implications from this report.

4. LEGAL IMPLICATIONS

The legal implications have been set out within the body of this report.

5. RISK ASSESSMENT

- 5.1.** SWAP has identified the following risks:

1. One or more partners do not wish to transfer to the new governance model. Rating: Medium

Members may resist losing their ability to appoint their own director. It will be important to present the benefits of the new arrangement to the Members fully to ensure that this is seen as a positive progression for the company borne out of its success rather than a removal of control from the Members. If the Members are not in agreement the board of directors may need to consider alternative options to modernise the governance of the company.

2. The company loses its Teckal/Regulation 12 exemption. Rating: Low

The Teckal exemption has been codified in Regulation 12 of the Public Contract Regulations 2016 and permits local authorities to directly award services contracts to companies in which they share joint control without having to go to open tender under European directives. Case law specifically supports the appointment of directors in this way as a compliant approach to secure good governance of a company owned by multiple local authorities. SWAP will need to ensure that 80% of its activities remain, as now, in providing services to its partners.

3. Continuation of Existing Arrangements. Rating: Medium

If new governance arrangements cannot be agreed then the company must continue to operate under the current mechanism. This mechanism is Teckal compliant which is the core focus for the company. While this does not represent the most efficient method of governance, retaining the current mechanism would not prevent the company from continuing its service delivery.

4. Maintaining good standards of corporate governance. Rating: Low

A number of local authority trading companies have received criticism of their governance arrangements in the public interest reports, in particular the Robin Hood Energy Company and the implication from the Brick by Brick investment as referenced in the wider Corydon Council report. Criticisms relate to lack of quality and variety of experience of directors as well as lack of clarity around business planning and financial management. Reduced directors numbers and the inclusion of independence experts in some areas will promote the strength and breadth of the board for SWAP to ensure it is working in the best possible way.

6. ALTERNATIVE OPTIONS

- 6.1.** The Audit Committee could decide not to support entering into the new Membership Agreement with SWAP. SWAP has recognised this in the first risk in section 5.

Amendments to Reserved Matters

Schedule 2 Part 1 Reserved Matters	
which require the consent of at least 50% of the Membership vote (in respect of a Membership Group, acting via its Nominated Representative) in general meeting or in writing).	
	Admit any person as a new member of the Company (save as otherwise permitted in the Deed or the Articles).
	sale / lease / license per trans £100k unless in business plan.
	purchase / lease / license per trans £100k unless in business plan.
	Appointment or approve the Remuneration of Auditors.
	Appoint / remove CEO or member of the Senior Leadership Team.
	Enter into contract with any members or directors or connections / associations / interests.
	Change the name of the Company.
	Form any subsidiary of the Company or acquire shares.
	Give guarantee or indemnity to secure liabilities of any person or assume obligations of that person.
	Otherwise than in accordance with Financial Regulations incur any item or series of items of capital expenditure of more than £100,000 unless provided for in the Business Plan.
	Consolidate / amalgamate with / acquire any company / business / person.
	Change accounting / reporting practices apart from following standards.
	License / assign or dispose of Intellectual Property Rights owned by Company.
	Commence, settle or defend any claim, proceedings / litigation against the Company (exception debt collection).
	Enter into any contract to do any of the things referred to in this schedule.
	Approve or sign the annual accounts of the Company.
	Alter the Company's accounting reference date.
	Appoint or remove any director (both Partner Directors and independent Directors) of the Company otherwise than in accordance with the Deed or Articles, this will include the mechanism for appointment.

Schedule 2 Part 1 Special Reserved matters

(Matters which require the consent of all the Members (in respect of a Membership Group, acting via its Nominated Representative) in writing or the consent of all the Members (in respect of a Membership Group, acting via its Nominated Representative) present in person or by proxy in a general meeting).

	Adopt the Business Plan.
	Amend the Business Plan / articles / rights attached to Membership interests.
	Make any capitalisation, repayment or other distribution of any amount standing to the credit of any reserve of the Company.
	Create any encumbrance over the undertaking / assets of company.
	Extend its activities outside the scope of the Business or cease to carry it on.
	Appoint or remove any director of the Company otherwise than in accordance with the Deed or Articles.
	Agree the form and content of the Financial Regulations or any alteration thereto.
	Enter into contract to do any of the above.
	Resolve to wind up the Company.