APPENDIX 2
Group Company Governance Committee - Governance Review – CIPFA Article on Local Authority Companies

Joanne Pitt: The need for guidance about council-owned companies

25 MAY 2021 **BY** JOANNE PITT

Recent public interest reports have shown how failures around council-owned companies can have devastating consequences, writes the local government policy manager at the Chartered Institute of Public Finance & Accountancy.

The conversation about the financial sustainability of local authorities has been going on for years. To support the financial health of the sector, Cipfa has committed to producing an index of indicators that could suggest financial fragility and/or risk within authorities.

However, the local government sector is complex. Through our resilience index, we have always been clear that a single component of a council's balance sheet cannot be used in isolation to reach a conclusion about the organisation's overall financial health. However, scrutinising council finances by shining a light on individual areas of risk based on emerging trends can provide a helpful contextual understanding at the local level. It can also help identify non-financial areas of weakness that may have an indirect impact on public finances.

More recently, we have seen that council-owned companies can present increased risk to local authorities, particularly where there is a weakness in governance and scrutiny. In 2020, two high-profile public interest reports, specific to Nottingham City Council and Croydon LBC, illustrated how

failures to understand the dangers of these company arrangements could resonate throughout the council, with potentially devastating consequences for local communities.
These two reports, together with evidence from recent organisational reviews, show some common themes and issues among councils that hold portfolios of companies. The potential for issues can generally be linked to organisational governance, leadership, capacity, financial stability, and culture, including:

- **a lack of understanding of roles and responsibilities**
- **a lack of skills around commercial decision making**
- **an optimism bias that does not reflect the true position**
- **a lack of strategic rationale surrounding the creation of companies**
- **a reluctance to listen to challenges.**

These reports, along with research and stakeholder commentary like the government's best value inspection report into Liverpool City Council, provide a unique opportunity for the sector to learn from the experience of others. At Cipfa, we agree with the findings from Grant Thornton's lessons from recent public interest reports "that it is often a question of degree, and perhaps a matter of timing, that separate these from a wider pool of councils".
Building on the success of the 2019 financial management code, Cipfa plans to extend its financial sustainability work by developing additional guidance for our members on council-owned companies. While the work will be aimed at public finance professionals, Cipfa is committed to building on the idea that responsibility for corporate financial sustainability rests with those responsible for making executive decisions with the support of their professional advisers. While this future work will be guidance rather than a formal code, it will provide much needed support and assurance to those involved in the operation of council-owned companies. The guidance will be released in the autumn.

Companies can certainly be a force for good in much of the public sector. At Cipfa we recognise that some local authorities have had, and continue to have, successful council-owned companies. We will continue to encourage learning from the best examples of public-private relationships the sector has to offer.

Joanne Pitt, local government policy manager, Cipfa