

Governance, Risk and Best Value Committee

10.00am, Thursday, 23 January 2025

Arm's Length External Organisation (ALEO) Governance Framework

Executive/routine
Wards

1. Recommendations

- 1.1 To consider the Arm's Length External Organisation (ALEO) Framework (Appendix 1);
- 1.2 To agree that a review is carried out of each Arm's Length External Organisation (outlined in paragraphs 4.11 to 4.13 of the report) following the approval of the Framework.
- 1.3 To consider the options outlined in Paragraph 4.10 of the report regarding elected member appointments to ALEO Boards; and
- 1.4 To delegate authority to the Chief Executive to make final design, layout and minor typographical changes to the Framework.
- 1.5 To refer the report to the Council

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Arm's Length External Organisation (ALEO) Governance Framework

2. Executive Summary

- 2.1 The proposed ALEO Governance Framework is designed to improve and strengthen the governance arrangements between the Council and its ALEOs.

3. Background

- 3.1 The City of Edinburgh Council operates a number of ALEOs to deliver designated services. Whilst the ALEO takes on responsibility for the delivery of service, the Council also has responsibility for the proper and prudent use of public funds and achieving best value.
- 3.2 Due to these responsibilities, it is essential that the Council has effective governance arrangements in place that support assurance within the individual ALEOs.
- 3.3 To ensure the Council has assurance that effective governance is in place within its ALEOs, a governance framework has been designed which would be rolled out throughout the Council's ALEO portfolio.
- 3.4 Details of the Council's ALEO reporting and governance arrangements have previously been reported in [June 2016](#) and [February 2020](#).
- 3.5 Additionally, a separate report on the Council's transport companies was considered by Transport and Environment Committee in [October 2023](#), which agreed changes to certain governance arrangements for Edinburgh Trams and Lothian Buses.

4. Main report

- 4.1 A new framework has been designed to ensure that there are sufficient governance arrangements across all its ALEOs and to improve the manner in which the Council manages these relationships.

Key Improvements

- 4.2 Key improvements as a result of the proposed new framework include;
- 4.2.1 A robust governance reporting structure for ALEOs,
 - 4.2.2 Consistency of governance arrangements (Service Level Agreements, Funding Agreements etc.),
 - 4.2.3 Development and improvement of the Council Observer role,
 - 4.2.4 A definition of what the Council considers an ALEO, and,
 - 4.2.5 Clear position with regard to Board member appointments to reduce the risk of elected member conflict of interests.
- 4.3 The framework has been designed to meet a number of objectives – improving how the Council manages the relationship with ALEOs, providing best practice for ALEOs, clarifying and providing greater consistency in terms of the relationship between the Council and its ALEOs, ensuring appropriate controls and assurance are in place, and providing greater support to those ALEOs and those who work with them. It is not designed to restrict ALEOs or to exert more influence on their operations.
- 4.4 It is intended that the use of the new framework will complement the existing strong working relationship between the Council and its ALEOs, will improve the efficiency, performance and sustainability of the Council's ALEO portfolio.

Board Member Appointments

- 4.5 Elected members are currently appointed to the boards of a number of Council ALEOs (Appendix 3). Appointments to outside bodies is a reserved matter for Council. In some cases, the number of appointments for a particular organisation is specified in a company's Articles of Association. For example Edinburgh Leisure's Articles state '*The City of Edinburgh Council and their statutory successors shall have the right to nominate up to five Nominated Members*'. Capital City Partnership's Articles state '*Membership shall be open only to the City of Edinburgh Council*'. From the ALEOs who currently attend the Governance Hub, plus CEC Holdings Limited, Elected Members are appointed to 6 of the ALEOs and an elected member is Chair on 4 of the ALEOs (Appendix 3).
- 4.6 There are a number of potential advantages and disadvantages of elected members being appointed to ALEOs and these are outlined in Appendix 2.
- 4.7 There is no clear position from the Scottish Government or Audit Scotland on whether elected members on boards of ALEOs is recommended. This has been the position in 2012 and in 2016 and the Council agreed to retain elected members on ALEO boards. However, since 2016 there have been a number of occasions where the interests of an ALEO and the Council has diverged, and the difficulty this put elected members in was reflected in discussion with those members who had experienced it.

4.8 The conflict between a Board Member on an ALEO and an elected member can never truly be reconciled. Whilst most of the time that conflict will not be prevalent, it is not possible to fully mitigate as elected members can never truly separate their roles as elected member and director. Fulfilling both roles can leave members in a position where they vote for something as a director because it is in the best interests of the company, but it conflicts with their political position or is not in the best interests of the Council. For example, a member may vote for remuneration when fulfilling their role as a director, but the remuneration package may not be the overall political will of the Council. Typically, the best interest of the Council will align with the best interest of the ALEO. However, when that diverges and the benefits to the ALEO has to be weighed up against the best interests of the Council then the elected members are put in an invidious position and the Council itself is at a disadvantage where some of its members may feel they can not act in the best interests of the Council because of their conflicting duties to the ALEO. The Chair of the Board, if an elected member, is in an even more difficult position and there will be considerable pressure to act in the best interests of the ALEO.

Board Member Appointment Options

4.9 It is therefore recommended in the framework that elected members are not appointed to ALEO Boards and that each ALEO should have an Elected Member/Shareholder forum. This will ensure that elected members are still able to engage in the activities of the ALEO.

4.10 It is recognised that the Council may not feel comfortable with removing elected members from Boards, even with the increased controls included in the framework. As a result, the following options are presented:

Option 1

4.10.1 Remove elected members from the Boards of all ALEOs;

Option 2

4.10.2 Remove elected members from the Boards of Council owned ALEOs;

Option 3

4.10.3 Restrict the number of elected Members appointed to boards to no more than 33% of the total number of directors; and

4.10.4 Elected members should not be appointed as chair of an ALEO Board;

Option 4

4.10.5 No change to current arrangements.

Framework Development – Phase 2

4.11 It is recommended that the proposed framework is considered by committee and referred to Council for approval, to allow officers to work closely with ALEOs to implement governance and assurance improvements.

- 4.12 If approved, officers intend to carry out a second phase of work which will concentrate on;
- 4.12.1 Reviewing all ALEOs to ensure they meet the newly adopted definition of an ALEO; and
 - 4.12.2 Reviewing the current ALEO governance arrangements to identify whether improvements or changes are required due to the framework.
- 4.13 Phase 2 will replicate the high priority on engagement with key stakeholders including ALEOs, Council Observers and Elected Members, which was essential to develop this framework.

Compliance with Regulations and Legislation

- 4.14 It is recognised that in some cases, an ALEO may have alternative governance arrangements in place which have been designed to ensure compliance with a statutory regulation (e.g. Financial Conduct Authority regulations). This framework is not intended to replace existing governance arrangements which meet such a purpose and should be used to support good governance.

5. Next Steps

- 5.1 If agreed by Council, officers will commence with phase 2, as detailed in 4.11-4.13 above.

6. Financial impact

- 6.1 Development of this framework has been delivered within existing budgets.
- 6.2 Phase 2, if agreed, will also be delivered within existing budgets. If during the process of carrying out the work relative to phase 2 creates a cost, officers will report this to members at the earliest opportunity.

7. Equality and Poverty Impact

- 7.1 There are no equality and poverty implications as a result of this report.
- 7.2 Adoption of the proposed framework will allow the Council to ensure ALEOs objectives are aligned to the Council's as much as possible. There is specific provision built into the framework to create closer policy relationships between the ALEO and the Council and this could extend to ALEOs adopting the Council's own policies on equality, poverty and environmental matters or developing their own.

8. Climate and Nature Emergency Implications

- 8.1 There are no climate and nature emergency implications as a result of this report.

9. Risk, policy, compliance, governance and community impact

- 9.1 Internal Stakeholders, ALEO Executives and Chairs and elected members were consulted during the drafting of the ALEO Governance Framework.
- 9.2 The Framework was reviewed by a legal firm to ensure that it was compliant with relevant legislation.

10. Background reading/external references

- 10.1 [Council Companies – Report by the Chief Executive](#)
- 10.2 [Arm's Length External Organisation's – Reporting to Committee – Report by the Chief Executive](#)

11. Appendices

- 11.1 Appendix 1 – ALEO Governance Framework.
- 11.2 Appendix 2 – Potential Advantages and Disadvantages
- 11.3 Appendix 3 – Current Appointments



Arms-Length External Organisations (ALEOs) Governance Framework

**The City of Edinburgh Council
2025**

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Chapter One – Administration

Definition of an Arm's Length External Organisation (ALEO)

Background

- 1.1. It is recognised that in some cases, an ALEO may have alternative governance arrangements in place which have been designed to ensure compliance with a statutory regulation (e.g. FCA regulations). This framework is not intended to replace existing governance arrangements which meet such a purpose, and should be used to support good governance.
- 1.2. Councils are under a legal duty to achieve best value in delivering services for their communities. Councils must also use public funds effectively to provide good quality services at a reasonable cost.
- 1.3. The 2018 Accounts Commission report on Councils' use of arm's length organisations detailed that Councils and Council companies must continue to apply the principles set out in the '*Following the Public Pound Code*'.¹
- 1.4. In order to achieve this, the Council can explore alternative, best value avenues to deliver services for the public which can include the use of ALEOs, outsourcing, entering into partnerships or a combination of these.
- 1.5. In some cases, it may be felt that the most effective way to deliver good quality services may involve the use of ALEOs. Operating Council-owned ALEOs within the commercial or charity sector, with strong governance arrangements in place, provides the ALEO with a level of independence allowing them to operate out with the constraints of a Local Authority.
- 1.6. Whilst the ALEO takes on responsibility for the delivery of service, the Council also has responsibility for the proper and prudent use of public funds and achieving best value.

Reasons for Creating an ALEO

- 1.7. There are a number of reasons and benefits for considering creating an ALEO:
- 1.8. **Charities** – certain activities may be best suited to operating a service or venue as a charity. ALEOs which qualify for charitable status can realise funding

¹ Audit Scotland – Following the Public Pound, March 2004

benefits, community grants and gain access to alternative resources/support streams, which are not otherwise available to local authorities.

- 1.9. **Funding** – creating an ALEO, particularly one that is focused on community interest, enables the ALEO access to different sources of grant funding that may not be available to the Council. There may be subsidy control issues regarding funding that require consideration, and appropriate legal advice should be sought if required.
- 1.10. **Commercial viability** – Some ALEOs operate in a commercially competitive environment where the ability to respond quickly and flexibly to market pressures is imperative. Operating such activities internally within the Council can remove this flexibility and subsequently put the company at a disadvantage to its competitors, ultimately putting its commercial viability at risk.
- 1.11. **Talent attraction and retention** – Attracting industry experts is vital in ensuring the success of an ALEO. By enabling an ALEO to attract the best people possible, it is sometimes necessary to pay the market rate and operate outside the Council’s pay structure.
- 1.12. **Deliver specialist services functions** – An ALEO may provide some services which require dedicated, specialist operational measures to deliver activities effectively and efficiently. The Council does not always have the right resources in place (e.g. structure, skills, experience or finances). Creating an ALEO for this purpose may provide the Council with the opportunity to deliver the service with suitable expertise whilst maintaining the necessary assurance.
- 1.13. **Financial** – In addition to some benefits for charitable organisations, limited companies can provide alternative revenue streams for the Council. Creating commercially viable organisations can support the Council’s central budget (through dividend payments) and make better use of funding and resources.
- 1.14. **Insurance** – Levels and types of insurance required will depend on the responsibilities and activities of the ALEO. Each ALEO has an opportunity to protect service delivery and also enhance offering through the placement of insurance contract/s. Independent advisors (e.g. insurance brokers) would be able to assist ALEOs with this placement
- 1.15. **Legislative** – As Councils are currently restricted in their ability to operate services for profit, charging beyond cost recovery is “trading” and therefore can only be carried out by another entity (ALEO). Therefore, the creation of a limited company for this specific purpose (even if that was an unintended consequence of the ALEOs operations) is necessary to ensure legal compliance.

- 1.16. **Delivery of key services** – It may be necessary to establish a company in order to provide a core service within a commercial setting where the third sector is not currently fulfilling the demand or providing the necessary standard of service. Providing this service through an ALEO, can allow the Council to ‘step-in’ and deliver what it considers a vital, yet non-statutory function.²
- 1.17. **Collaborative working** – Reducing bureaucratic and statutory processes can improve efficiency and effectiveness. This is particularly important when working with partner organisations and commercial parties whose processes, and speed of decision making is not aligned with Council procedures and requirements. Working collaboratively with outside organisations and industry experts give the ALEO the best possible environment in which to create a viable commercial entity.³

Current ALEO Relationship

- 1.18. The Council treats a number of organisations it has links to as ALEOs. However, the ALEOs have a range of different structural arrangements and different relationships with the Council. Some of the ALEOs are **clearly** ALEOs while others are included because of historic connections rather than because they are owned by the Council. Consideration should be given to adopting a clear definition of what the Council considers to be an ALEO. This provides greater clarity on the types of organisations which may fall under, or sit out with, the ALEO umbrella.

Lack of Statutory Definition of an ALEO

- 1.19. There is no statutory definition of an ALEO. However, some sources have attempted to provide their own explanation for what an ALEO is including Audit Scotland’s report from June 2011 titled “*Arm’s length external organisations (ALEOs): are you getting it right?*”⁴ and the Standards Commission for Scotland, Advice for Councillors on ALEOs.⁵

- 1.20. Audit Scotland noted within their report:

“We define arm’s-length external organisations as companies, trusts and other bodies that are separate from the local authority but are subject to local authority control or influence. Control or influence can be through the council having representation on the

² CIPFA - Local authority owned companies, a good practice guide: 2022 edition (pg. 12)

³ CIPFA - Local authority owned companies, a good practice guide: 2022 edition (pg. 12)

⁴ https://audit.scot/uploads/docs/report/2011/nr_110616_aleos.pdf

⁵ [1638361910211201AdviceNoteCouncillorsALEOsv1.pdf](https://audit.scot/uploads/docs/report/2011/nr_110616_aleos.pdf)

board of the organisation, and/or through the council being a main funder or shareholder of the organisation”.

1.21. An ALEO is a body which is formally separate from a Council but is subject to its control and influence. ALEOs usually take the form of companies or trusts and can register as charities if they have charitable purposes and undertake activities in furtherance of these activities. In the absence of a statutory definition, there remains a risk that some organisations which should be considered an ALEO are not and vice-versa. This presents a risk of a gap in assurance monitoring over key organisations the Council has a relationship with or interest in.

Definition of an ALEO

1.22. A Council Arms-Length External Organisation (ALEO) is a separate legal entity that operates independently of the Council and is one of the following:

(a) wholly or partially owned by the Council or is a subsidiary of a wholly or partially owned organisation, or;

(b) Council has such control and influence over the organisation to the extent that if the Council withdrew co-operation (funding or otherwise) it would mean the organisation could not operate effectively. Funding alone would not be a sufficient reason to meet this criterion.

1.23. Adoption of the definition outlined above, instead of the Audit Scotland or Scottish Government Definitions, will provide clarity on the organisations that the Council supports or invests in, that should be considered an ALEO. Clearly defining an ALEO, and therefore treating the necessary organisations as ALEOs, will have the practical impact of ensuring those companies benefit from the assurance controls built into the ALEO Governance Framework.

Impact of Adopting this Definition

1.24. It is anticipated that adopting this definition will cement the status of our current ALEOs whilst also providing the necessary clarity and flexibility to consider and review the status of other organisations linked to the Council

1.25. This will, in turn, provide the Council with the necessary assurance in their use of public funds and resources. This is vitally important but particularly where the use of those funds extends to operations in the commercial sector.

- 1.26. Additionally, the ALEO will benefit from maintaining a level of independence in its decision-making and operations from the Council, whilst benefiting from clear expectations on objectives and their governance responsibilities.

How to set-up an ALEO and ALEO Reviews

- 1.27. The creation of Council companies is a reserved matter to Council under the City of Edinburgh Council Committee Terms of Reference and Delegated Functions.
- 1.28. A report must be submitted to Council requesting approval to set up an ALEO.
- 1.29. Prior to a report being submitted to Council, the request to set up an ALEO must be signed off by the relevant City of Edinburgh Council Chief Executive/Executive Director.
- 1.30. The report to Council must include:
- a) The reason for creating the ALEO.
 - b) Identify who will fill the Council Observer role, as detailed in Chapter 3.
 - c) Confirmation of relevant Governance documentation (SLA/Shareholder Agreement etc.).
 - d) Reporting arrangements, including which Executive Committee the ALEO will report to.
- 1.31. When approval is granted to establish a new ALEO, the Governance Team must be notified to update the central ALEO Register. The Governance Team will provide guidance on incorporating a company with Companies House.
- 1.32. It is important for the Council to ensure that use of ALEOs is the most appropriate and effective method to deliver a service. The use of an existing ALEO, or creation of a new one, must be informed by the reasons detailed in paragraphs 1.7 to 1.17.
- 1.33. To ensure the Council utilise ALEOs effectively and minimise over-use or over-reliance of ALEOs, each ALEO will be subject to a review every five years. This purpose of the review will be to determine whether the conditions and rationale for establishing the ALEO still hold. During the review, the following will be considered:
- a) Financial performance.
 - b) Performance against KPIs.
 - c) If the ALEO continues to fall within the definition at 1.20.
 - d) If, since the creation of the ALEO, no other more viable alternative to deliver the service has been identified.

e) Any other issues specific to the ALEO

1.32 This 5-year review will be conducted by the relevant service area in conjunction with the Chief Executive (CEC), Head of Democracy & Governance, the Council Observer, ALEO Senior Officer/Employee (Chief Executive, etc.) and ALEO Chair,

Review out with the 5-year review period

1.33 A review of an ALEO may be required out with the five-year review period. A review will be triggered:

- a) If an ALEO does not meet its KPIs for two consecutive years
- b) GRBV Committee can request a review following scrutiny of an ALEO.
- c) Executive Committees can request a review when SLAs etc. are presented for agreement.
- d) At the request of the Chief Executive (CEC).
- e) At the request of individual ALEOs.

1.34 The outcome of all reviews and any recommendations will be reported to the relevant Committee for scrutiny and referred to Council where a decision is required.

Chapter Two – Governance Arrangements

2. This section aims to provide guidance on the governance arrangements available, that can imbed assurance across a number of risks. Provided a sufficient level of assurance can be achieved, a combination of these arrangements may be appropriate and not all would be required.

Articles of Association or Governing Document

Background

- 2.1. The organisations governance document can be defined as legal document that outlines the internal rules and regulations governing the operation of a company or organisation. They are used for several purposes to set out a structure of good governance within an organisation. This is a compulsory document that must be completed as part of the incorporation process for all companies (including those with charitable status).
- 2.2 A company may be limited by shares or by guarantee. The latter has members rather than shareholders and is mainly used for non-profit-making or charitable entities. The form of the organisation’s governing document will differ depending on the type of organisation it is. For example, an ALEO set up as a company will have Articles of Association (AoA), whereas Scottish Charitable Incorporated Organisation (SCIO) will have a constitution.
- 2.3 Templates for creating AoA for companies can be found on the [Companies House website](#). Model Articles of Association (“Model AoA”) are the standard default Articles a company can use. They are prescribed by the Companies Act 2006. If the ALEO is to have charitable status, model constitution and associated guidance can be found on the Scottish Council for Voluntary Organisations website which can be used as a starting point. It is recommended that service areas incorporating ALEOs obtain legal advice on the appropriate form of company and on the contents of the AoA. In the case of a company limited by shares, the use of a Shareholder Agreement will likely be appropriate in conjunction with the AoA. When drafting governing document for an ALEO, a minimum standard has been adopted by the Council which requires the following matters to be covered, in addition to any statutory provisions required to be set out:
- 2.4 **Governance Structure** – Defines the roles, responsibilities and powers of directors, shareholders/members, and officers within the organisation. Sets out the procedures for appointing directors, minimum quorum for holding board meetings and decision-making procedures.

- 2.5 **Regulating Shareholder/Member Rights** – Outlines the shareholder/member rights in terms of voting rights, dividend entitlements (except for charitable organisations) and procedures for transferring or selling shares (where applicable). The Council must maintain voting rights on all ALEOs, with the exception of charities which have separate governance controls in place.
- 2.6 **Defining Company Operations** – Specifies the organisation's objectives, scope of business activities and any restrictions or limitations on its operations. Outlines any financial procedures or controls, such as dividend distribution (where applicable) and capital management/investment.
- 2.7 **Objectives** – A general statement explaining how business activities will remain committed and aligned to the Council's objectives should also be included.
- 2.8 **Compliance with Legal Requirements** – The governing document will ensure that the organisation operates within legal boundaries and adheres to relevant regulatory requirements including compliance with the latest public procurement rules and freedom of information legislation. In some circumstances, an ALEO may also be classed as a 'public authority' for the purposes of the Subsidy Control Act 2022 and therefore it must ensure it complies with any subsidy control obligations (where relevant).
- 2.9 **Accountability and Transparency** – A general outline of the governance procedures in place should be included and a commitment to promote accountability and transparency within the organisation (subject to consideration of commercial confidentiality). Board members, shareholders/members and regulatory bodies should be able to understand how decisions are made and hold leadership accountable for their actions.
- 2.10 Overall, the governing document will provide a formal structure and framework for arms-length external organisations, helping to govern their operations, protect the interests of members, ensure legal compliance and promote accountability.

Remuneration Committee and Scrutiny/Audit Committee

- 2.11 Every ALEO that employs staff should establish a Remuneration Committee (see details at 2.72) and an Audit/Scrutiny committee.
- 2.12 Overall, AoA provide a formal structure and framework for arms-length external organisations, helping to govern their operations, protect the interests of members, ensure legal compliance and promote accountability.

Shareholders' Agreements

- 2.13 The purpose of a shareholders' agreement serves as a formal contractual agreement between shareholders to outline agreed principles, responsibilities and obligations. The detail contained in a shareholders' agreement may at

times also be reflected in other governance documentation within the ALEO, for example an SLA. The use of other governance documentation should be used to enhance the terms of a shareholders' agreement and not in contradiction.

- 2.14 It is a key document to be used to outline foundational and core agreements between the Council and ALEO which may cover matters such as risk management, financials, policies, business direction, executive decision making, governance structure, board composition and conflict management.
- 2.15 In the absence of a shareholder agreement, the matters ordinarily outlined and agreed should instead be set out in a contractual binding SLA or where appropriate, a funding agreement.
- 2.16 Whilst it is important to maintain flexibility in some areas of a shareholder agreement, depending on the specific make up of that ALEO, the following core principles must be included (insofar as they have not been dealt with within the organisation's governing document):
- 2.17 **Purpose** – A clear and descriptive definition of the purpose of the ALEO and the nature of the activities they are limited to engage in.
- 2.18 **Control Over Major Business Direction** – This should ensure that, where the Council holds a controlling share in the company, explicit consent must be sought on major business decisions. This may be achieved through voting rights, explicit consent requirements or assigning a certain value (£) limitation before seeking consent from the Council.
- 2.19 **Board Appointments** – Details of any requirements of Board composition should be outlined here. Appointment of Chair of the Board must be consented to by the Council prior to their appointment.
- 2.20 **Council Observer** – Right to appoint an observer to the Board in a non-voting capacity. The observer should have the right to attend all Board meetings and have access to all papers. They should be able to advise on matters at Board meetings if necessary, but they will not be an active member of the Board and cannot be involved in decisions.
- 2.21 **Senior Staff Appointments** – The Council reserves the right to consent on the appointment of the most senior officer/employee in the organisation.
- 2.22 **Remuneration packages** – All appointments to the most senior officer/employee within the ALEO shall be subject to a remuneration committee process in accordance with this framework.
- 2.23 **Compliance / Adoption of Council Policies** – The Council may reasonably require its ALEOs to adopt and adhere to certain policies which align to the Council's (and therefore, the ALEO's) objectives. It is recognised that not all policies will align and where that is the case, the Council Observer and ALEO

will engage in further discussion. The specific policies applicable to the ALEO may vary but consideration should be given to at least but not limited to the following; the real Living Wage, the Edinburgh Guarantee scheme, sustainability, economic wellbeing and, environmental pledges.

2.24 Implementing Internal Policies – There is a reasonable expectation of the Council that the ALEO implement certain internal policies. This ensures good governance throughout the organisation. Where necessary, this may be outsourced and, in such circumstances, the ALEO should initially consult with the Council to discuss whether it is appropriate for the Council to draft the policies to ensure best value in supporting the ALEO. These policies should include but not be limited to:

- a) Risk management and maintenance of a risk register
- b) Whistleblowing
- c) Bribery, anti-corruption etc
- d) Formal recruitment and selection policy
- e) health and safety
- f) Audit (non-financial auditing)
- g) Equalities
- h) Internal complaints / HR processes including complaints involving Chief Executive and senior management roles
- i) Customer service (including complaints handling)
- j) Cyber security compliance with FOIs
- k) Business continuity plans

2.25 Consent – Consent matters are mentioned throughout the framework and should be built into various governance arrangements to ensure several layers of assurance. However, the following matters in which the Council maintains consent on, should be included explicitly to ensure they are not overlooked:

- a) Chief Officer appointments,
- b) Remuneration packages including bonuses, for Chief Officers,
- c) Business direction / major operational decisions (which affect reputational, legal and financial stability),
- d) Financial decisions outside the agreed budget,
- e) All other consent matters detailed above at 2.28

2.26 Alignment with Council Objectives – The agreement should also outline how the company will align to the objectives of the Council with provision made for the Council to maintain an appropriate strategic level of control.

2.27 Financial reporting and Business Plan – Details of agreed financial reporting structures should also be included in addition to agreement on Council signing off the ALEO's business plan. It is recommended that the Council have sight of the overarching objective of the ALEO, which is reviewed on a 4-year basis and a separate annual business plan be reported to and agreed with the Council.

- 2.28 **Conflict Management and Dispute Resolution** – The agreement should have clearly defined parameters in which matters can be raised, escalated, discussed and resolved. Where matters require escalation for resolution, agreed processes should be set out. Consideration should be given to provide guidance on mediation in the first instance and arbitration thereafter.
- 2.29 **Remedial / Corrective Actions** – Avenues in which to address concerns in relation to the performance of either party or application of any agreement between the parties (e.g. the funding agreement, or SLA) should be provided. This may include penalties set out in any funding agreement, conditions placed on performance related enhancements, including measures in governing documents to overrule the Board by exercising its powers as a majority shareholder/member (where applicable).
- 2.30 **Dividends** – In some cases ALEOs are designed to offer the Council alternative avenues in which to generate revenue to assist in supporting the Council’s core and statutory functions. Therefore, each funding agreement (with the exception of ALEOs with charitable status, or ALEOs which are exempt from this requirement as agreed with the Council) should be required to contribute towards the Council’s central budget by way of dividend payments. The exact nature of the structure and value of dividend payments will vary from case to case but should be detailed clearly within the Shareholder/Funding Agreement.

Service Level Agreements (SLAs)

- 2.31 Service Level Agreements (SLAs) are contractual agreements between a service provider (in this case, the ALEO) and its client (the Council). The SLA should outline the level of service to be provided and is designed to cover a wide range of operational matters in which the Council maintains an interest, including performance, responsibilities and expectations.
- 2.32 SLAs are essential in ensuring clarity for both parties on expectations relating to relevant matters. This guidance provides indicative examples of matters in which the Council might reserve a degree of control but is not exhaustive.
- 2.33 The SLA must explain how it will align with Council objectives and details of how that will be achieved must be explained. Additionally, these objectives must be specific and measurable against what this agreement sets out to deliver.
- 2.34 The aims of an SLA are to ensure:
- 2.35 **Clarity and Transparency** – Provides clarity on the services to be delivered, ensuring that both parties have a clear understanding of expectations. This helps avoid misunderstandings and disputes regarding the scope of business operations and performance standards.
- 2.36 **Performance Management** – Facilitates performance management by providing a framework for monitoring and evaluating the ALEO's performance.

Key performance indicators (KPIs) outlined in the SLA allow the Council to assess whether the ALEO is meeting its obligations and identify areas for improvement. These KPIs should be measurable performance indicators which set out clear established targets relevant to the ALEO's business. It is important to ensure objectives/KPIs are closely aligned to Council objectives and overall policy direction.

- 2.37 **Accountability** – The SLA is a tool to ensure that the ALEO agrees to meet these targets, and the Council can hold them accountable for achieving the agreed levels of service. This ensures that the ALEO remains focused on delivering quality services efficiently. It also provides protection for the ALEO in that clear direction is received from the Council. Accountability is ultimately achieved through clear, open and transparent communication from both parties and well-structured reporting mechanisms are established through regular monitoring reports.
- 2.38 **Cost Management and Control** – Includes financial terms and conditions, such as pricing structures, payment schedules and penalties for non-performance. This helps the Council manage costs effectively and ensures that taxpayers' money is spent efficiently.
- 2.39 **Roles and Responsibilities** – The distinct role of the Council and ALEO should be outlined here. A statement should be made as to the level of involvement of the Council both operationally and financially. The responsibilities of each party should also be set out including the ALEO's primary focus in terms of delivering the objectives.
- 2.40 **Governance** – This section should set out clear agreement by the ALEO to adhere to the Council's ALEO Governance Framework. Specific mention of reporting responsibilities set out in the Framework should be made here to ensure explicit agreement to this element.

Minimum service provision

- 2.41 The specifics of minimum service provision will differ depending on the ALEO, so it is not possible to provide an exhaustive list however, where the ALEO relates to the provision of services for members of the public, the SLA must specify (a) the minimum level of service users can expect from the ALEO and (b) that a Business Continuity Plan must be in place to minimise the effect for instances where the minimum level of service cannot be provided.

Costs / Charges

- 2.42 A clear cost/charging scale for services being provided between the organisations must be set out if applicable. Detail of a process for agreeing with the Council any deviation from or amendment to the agreed charges.

Funding Arrangements

- 2.43 Where a separate funding agreement exists between the Council and the ALEO, an explicit commitment from the ALEO to adhere to the funding agreement must be included in the SLA.
- 2.44 If a funding agreement does not exist, details of any funding arrangement must be set out.
- 2.45 Agreement to the Funding Principles set out in the ALEO Governance Framework must be explicitly agreed to and details of how this will be achieved included.

Consent

- 2.46 Where not dealt with in the organisation's governing document and/or shareholders' agreement, the SLA must outline that the Council maintains explicit consent to agree, or otherwise, the following:
- a) Major spending and/or investments,
 - b) Significant infrastructure spending,
 - c) Strategic direction,
 - d) Bonus payments to employees (including chief officers),
 - e) Appointments of employees to senior roles,
 - f) Any other matters considered proportionate and necessary, depending on the business/service carried out by the ALEO.

Funding Agreements

- 2.47 Funding agreements between the Council and ALEOs are used to outline the financial support provided by the Council to the ALEO. This can be for a specific purpose or project or for longer-term funding arrangements.
- 2.48 Its main purpose is to formalise the financial relationship between the Council and the ALEO and provide assurance on the use of public funds. This is crucial in ensuring any financial support provided by the Council (public funds) are protected through delivering a proportionate agreement underpinned by transparency, accountability and alignment of objectives.
- 2.49 When designing the funding agreement specific to the ALEO, it is necessary to ensure the agreement is bespoke to that organisation and that flexibility is applied where necessary. This is important to ensure the funding needs of that ALEO are catered for and provide the best possible financial environment in which to operate.
- 2.50 There are key principles that every funding agreement must consider and adhere to (as set out below):

- 2.51 **Purpose and Scope** – The agreement should clearly define the purpose for which the funding is being provided. This could be for delivering specific services / projects or supporting the organisation's ongoing operations.
- 2.52 **Funding Amount and Duration** – Specifies the total amount of funding being provided by the Council and the duration for which the funding is applicable. This could be a one-time grant or ongoing financial support over a defined period.
- 2.53 If the funding is for a defined period (e.g. not a one-off payment), set out what this period is and any payment conditions. If it is possible that the funding will be provided by the Council beyond the duration specified, this must also be explained.
- 2.54 Where the ALEO is likely to rely on sustained (long-term) financial support from the Council (beyond the defined period), an assessment as to the likelihood of the Council being able to accommodate further funding should be clearly set out.
- 2.55 **Conditions of Funding** – The agreement must clearly outline any conditions attached to the funding. This includes any specific objectives / targets that the ALEO or the Council must meet or adhere to, to ensure eligibility for the funding. This might include reporting obligations, performance targets, compliance with relevant regulations or adherence to agreed-upon budgets and timelines.
- 2.56 All funding agreements must contain performance related conditions. Whilst this guidance doesn't outline the exact nature of the performance target insisted upon (as that will be relevant and dependent on the ALEO, nature of the activity it is engaged in and other market environment factors), the Council does insist on funding (particularly when this is long term) being performance driven. This is to ensure public funds are utilised appropriately and represent best value for money.
- 2.57 The Council can stipulate in the Funding Agreement that an ALEO must comply with a particular Council policy and/or objective(s).
- 2.58 **Service Level Agreement (SLA) and Mandatory Conditions** – There may be times where a Funding Agreement and SLA are used in tandem to support assurance of the ALEOs operational objectives. Alternatively, mandatory conditions of funding set out in the Funding Agreement may be used instead of an SLA.
- 2.59 **Accountability and Monitoring** – Provisions for accountability and monitoring must form part of the agreement to ensure that the funding is being used appropriately and effectively. This should involve regular reporting by the ALEO to the Council and commitment to providing financial audits annually, site visits where appropriate, or other mechanisms for oversight which may be relevant to the business area.

- 2.60 **Performance Review and Evaluation** – An agreement on periodic reviews and evaluations of the funded activities should also be carried out. This should assess the activity’s impact, effectiveness and alignment with the Council’s objectives. This is necessary to demonstrate accountability for the use of public funds and may inform future funding decisions and adjustments to the agreement if needed.
- 2.61 **Termination and Amendments** – Procedures should be set out for terminating the agreement or making amendments to its terms. This may be relevant in the case of failure to perform against agreed objectives, the Council being unable to provide the required funding or either party seeking to amend the terms of the agreement. Input from the Council’s legal and finance teams, as appropriate, is advised when considering how to construct such provisions.
- 2.62 **Compliance** – The agreement will also need to comply with relevant legal requirements, including any procurement rules, contract law, subsidy control legislation and internal policies of both the Council and the ALEO. The Council’s legal and finance teams should be consulted for further information on compliance queries.

Remuneration & Selection

- 2.63 It is recognised that when operating in the commercial sector, staff remuneration packages (particularly those at senior levels) are sometimes structured very differently to public sector packages. Whilst it is necessary for ALEOs to be given flexibility in their approach to remuneration packages, ultimately poor governance in this area can result in poor value for money.
- 2.64 To ensure the Council maintains assurance across all ALEO pay packages, the following principles must be considered to provide commercial viability whilst delivering best value.

Salary Benchmarking & Determination

- 2.65 Benchmarking is a vital tool for providing the Council with assurance that the remuneration packages offered to senior staff are both attractive and proportionate. It ensures that the salaries on offer are competitive to attract the right calibre of candidates and remains competitive in the market. Additionally, it provides the Council with sufficient assurance that packages are in line with market rates and are offering value for money.
- 2.66 All appointments at CEO level or equivalent should be subject to a benchmarking exercise.
- 2.67 ALEOs may wish to consider appointing independent benchmarking specialists to carry out fair, impartial and transparent job evaluation of the role. Where this is not possible, the ALEO should work with the Council to develop and administer its own benchmarking exercise.

Bonuses

- 2.68 The Council understands that salaries are required to be competitive within the industry that the organisation operates in and as a result, does not expect bonuses to be paid unless in exceptional circumstances. Therefore, bonuses should not ordinarily form part of a contract. There may be times where there is legitimate reason to consider including a bonus structure within contracts, however this will be considered as exceptional circumstances only and must, without exception, require the explicit consent of the Council.
- 2.69 In addition, where an exceptional need for a bonus to be included in a remuneration package is identified, this **must** be performance related and be tied to challenging performance objectives which are agreed in advance by the Council.
- 2.70 In terms of payment of bonuses, where the ALEO Board considers that the performance related objectives to trigger the payment of a bonus has been met, they should report this to the Council prior to the payment being made.

Pensions

- 2.71 The pension contributions and overall package offered to all staff within the ALEO, including senior officers/employees, must be reflective of the market in which the ALEO operates in.

Remuneration Committees

- 2.72 The Committee should be instructed to oversee the process of agreeing the most senior officer/employee remuneration packages. They are responsible for ensuring that best value for money is achieved. The Remuneration Committee will assist the board in fulfilling its responsibilities regarding all matters related to pay and for executive director(s) and member(s) of senior management.
- 2.73 The Council can assist the ALEO in putting together and administering Remuneration Committees, if required. Committees should be tasked with:
- a) Reviewing the terms and conditions of employment along with the compensation of senior directors and managers.
 - b) Assessing the benchmarking exercise carried out by the ALEO.
 - c) Deciding on termination payments for executive directors and,
 - d) Reassuring shareholders that remuneration is decided fairly and transparently with no conflicts of interest.

Recruitment / Selection

- 2.74 A specific policy should be adopted by the ALEO in relation to recruitment of all posts within the organisation. The Council's own Recruitment and Selection Policy may be either by used by the ALEO entirely or utilised to assist ALEOs in the development of their own policy.

- 2.75 Regardless of the policy chosen, all recruitment must be open, honest, transparent and accountable.
- 2.76 In addition, the Council reserves the right to inspect the ALEO's recruitment policy or processes at any time.

Board Member & Senior Officer/Employee Appointments

- 2.77 Appointment of Board Members is a matter for the ALEO, not for the Council and therefore the ALEO may adopt a separate policy for recruitment of Board Members, as it sees fit.
- 2.78 The appointment of the most senior officer/employee and Chair of the Board, should be subject to a selection panel, with at least one panel member being a Council officer. It recommended that this officer be the ALEO's Council Observer, or someone of their choosing.

Record Keeping

- 2.79 Ensuring that accurate and up-to-date records are created and managed appropriately is essential to maintaining effective governance as it supports the organisation to be transparent, accountable, efficient, compliant with various regulations, including the UK Companies Act 2006 and the Charities and Trustee Investment (Scotland) Act 2005.
- 2.80 The records maintained by the ALEO may also be used by the Council for its own governance purposes.
- 2.81 While the Council will maintain an overall ALEO directory of vital governance records, the ALEO is responsible for creating and managing accurate, reliable and retrievable records through good records management.
- 2.82 Good records management requires the ALEO to setup a framework of policy, procedures and guidance that govern its records. This includes:
 - 2.82.1 Policy documents that determine who is responsible for the overall management of the ALEO's records, as well as where they should be stored (i.e. cloud storage, email systems, filing cabinets, IT systems etc.) and how long for (i.e. record retention policies)
 - 2.82.2 Procedures that determine how and when records should be created and disposed of, as well how they should be tracked in terms of usage and updating – these can be incorporated into existing business and project management processes

- 2.82.3 Guidance that reinforces policy and procedures by answering specific questions (e.g. when should a text or social media chat become an email or memo?)
- 2.83 There should be a senior officer/employee who has overall responsibility for the ALEO's records and someone (or multiple individuals if the ALEO is large or complex enough) who is operationally responsible for them on a day-to-day basis. It should be clear in policy and job descriptions who these people are.
- 2.84 Basic training on what is expected of all staff when creating and managing should be in place and annually undertaken by staff. More advanced training for the operationally responsible individual(s) should also be considered.
- 2.85 Good records management is not 'just admin' but has the following benefits for the ALEO and the Council:

- 2.85.1 **Transparency**

- Good record-keeping ensures that all activities and decisions within an organisation are well-documented, making it easier to see how decisions are made, and resources are used.

- 2.85.2 **Accountability**

- By maintaining detailed records, it's possible to trace decisions and actions back those responsible, providing accountability and assurance for officers and the organisation. Additionally, good record keeping provides a clear audit trail, which is essential for internal and external audits.

- 2.85.3 **Efficiency**

- Effective records management streamlines access to important information, reducing the time and effort required to retrieve data. This efficiency supports better decision-making and resource allocation. moreover, good record-keeping ensures that institutional knowledge is preserved.

- 2.85.4 **Compliance**

- Records serve as evidence that the organization has met its legal and regulatory obligations, which is crucial in case of inspections, audits, or legal dispute. Additionally, well managed record keeping will assist the organisation in meeting its obligations under GDPR etc.

Council Responsibilities

2.86 The Council (via the Governance Team) will maintain a detailed record of ALEO documentation on behalf of the Council. This will include a directory of key information including but not limited to;

2.86.1 Ownership details

2.86.2 A record of the governance arrangements in place (e.g. SLA, Shareholder Agreement etc)

2.86.3 Chief Officer

2.86.4 Council Observer

2.86.5 Director(s) / Board Membership

2.86.6 Company Secretary

2.86.7 Details of which Council committee the ALEO should report to and when

ALEO Responsibilities

2.87 To provide the Council with the necessary information to maintain an accurate record of the ALEO, the ALEO must provide the Council with the following information:

2.87.1 A copy of the final signed and agreed governance arrangements documentation including all and any SLAs, Shareholder Agreements, Articles of Association, Funding Agreements etc.

2.87.2 Copies of all Board meeting minutes and decisions / actions logs.

2.87.3 Copies of audited and unaudited accounts – this may be substituted where included in formal reporting to the Council.

2.87.4 Copies of policies that govern the ALEO's records.

2.87.5 Copies of any internal or external audit reports.

2.87.6 An organisational structure chart including both officer structure and operational / services structure.

2.87.7 A governance reporting structure chart (e.g. any committees/boards internally which services report to).

2.88 The Council's Governance Team will provide the ALEO and CO with sufficient support to regularly review and maintain this information ensuring that it is kept up to date.

Key Performance Indicators (KPIs)

- 2.89 Effective performance measurement is crucial for any organisation to assess its progress towards its goals and objectives. KPIs serve as valuable tools in driving forward business development with structure and purpose and valuating the success of operational activities and strategic initiatives against the ALEO's objective.
- 2.90 Particularly for ALEOs, KPIs are vital in ensuring alignment of the ALEO's objectives with the Council's own. KPIs should be proportionate, relevant, and ambitious. The Council should follow key principles in establishing successful KPIs:
- a) **Establish Clear KPIs** – Clearly articulate the desired outcomes or objectives that each KPI aims to measure.
 - b) **Select Relevant Metrics** – Identify the most appropriate metrics or indicators for assessing progress towards each objective.
 - c) **Set Targets** – Ensure the established KPIs, which should be aligned with objectives, are both realistic but challenging for the ALEO. KPIs should be based on (but not limited to) industry standards or strategic priorities.
 - d) **Performance Related payments** – There may be funding agreements in place which include provisions for enhanced or additional funding paid to the ALEO by the Council, where certain performance objectives have been met. This must be clearly outlined in the relevant governance arrangements (SLA, funding agreement etc.) in addition to being included in the core KPI documentation.
 - e) **Alignment with Council Objectives** - KPIs should be directly linked to the ALEO's objectives, which in turn should be linked to the Council's own objectives. In addition to supporting Council objectives, KPIs that directly or indirectly contribute to advancing Council priorities, pledges and commitments can help the city to address key challenges or take advantage of opportunities.
 - f) **Encourage Accountability** – Ensure that each KPI reflects a tangible achievement. This will help to foster connections with objectives and generate accountability and transparency in performance management.
 - g) **Engagement with Stakeholders** – Collaborate with relevant stakeholders, including senior management of ALEOs, Council Observers, Heads of Service, and Executive Directors, to develop KPIs that accurately reflect the views of those responsible for delivering and monitoring KPIs.

Approval Process

- 2.91 ALEOs should seek formal approval from the Council for the finalised set of KPIs, operational objectives, and performance measures before implementation.

- 2.92 It is recommended that regular updates are obtained by the Council Observer with KPI monitoring reported to the Council as agreed within the reporting element of this framework.

Reporting & Scrutiny

- 2.93 CIPFA recommends that *'the local authority should ensure that its overview and scrutiny committees are able to exercise their powers in relation to the discharge of local authority functions under the relevant legislation. This should include being able to scrutinise the operation of local authority companies as part of their work programme and to provide constructive challenge'*.⁶

ALEOs reporting to Executive Committees

- 2.94 ALEOs currently report to Executive Committees. It is recommended that ALEOs continue to report to the Council but only to the Governance, Risk and Best Value Committee (GRBV) on an annual basis. This will provide greater efficiency, avoid conflicts of interest and duplication of work. However, the relevant Executive Committee is required to approve ALEO Service Level Agreements and Funding Agreements.

ALEOs reporting to GRBV

- 2.95 GRBV (or the appropriate committee as outlined in Committee Terms of Reference) should scrutinise the ALEO's financial performance, compliance with the SLA or funding agreement and any risks impacting the Council and/or ALEO.

Reporting

- 2.96 A representative from the ALEO's executive must present for consideration of report(s). The Council Observer should also be present.
- 2.97 Committee reports should include a section from the Council's Observer with any comments they have on the company, risks to the Council and the overall operation of the organisation. Reports should also include the company's annual accounts.
- 2.98 There may be occasions that some information in the report will not be able to be made public under Part 1 of Schedule 7A of the Local Government (Scotland) Act 1973 due to commercial sensitivity, although this should be kept to a minimum. More details on governance reporting structure and scrutiny are detailed in Chapter 5 of this framework.

⁶ Local authority owned companies: a good practice guide, CIPFA \ The Chartered Institute of Public Finance and Accountancy, London, 2022, p. 64.

Audit Arrangements

2.99 It is imperative that ALEOs have appropriate internal control assurance arrangements in place. The Council will work with each ALEO to review its arrangements and where necessary, develop proportionate internal control arrangements aligned to this framework requirements.

2.100 Where there is a need identified to consider internal audit providers for an ALEO, the Council should be duly considered for providing this service.

Chapter Three – Council Observer

Council Observer Role & Responsibilities

What is a Council Observer?

- 3.1 A Council Observer (CO) of an ALEO is an officer (not an elected member) who is appointed to observe how an ALEO operates and support good governance, on behalf of the Council. This can include (but not limited to) decision-making processes by the Board, operational performance of the organisation (measured against set objectives) or highlighting areas of risk or assurance gaps to the Council. If there are Council Officer(s) on the Board of an ALEO then a CO is not required, this should only occur under special circumstances and is not recommended on an ongoing basis.
- 3.2. They are also responsible for reporting back to internal colleagues (Chief Officers) on matters which may require attention and escalate matters when appropriate. This role is distinctly separate and different from the role of an Elected Member who is appointed to a Board (in the case of a charity) or an Elected Member/Shareholder forum for all other ALEOs. The service must notify the Governance Team of who is appointed to the CO role, and any subsequent changes.

Improvement

- 3.3. There are four key areas of development of the CO role which have been identified to improve assurance: Role Clarity, Training, Role Criteria and Reporting.
- 3.4 **Role Clarity** – The responsibility of the CO is multi-faceted and should include:
 - a) Attendance at board meetings (no voting rights) to observe and scrutinise board decision making and report back to internal Chief Officers on decisions, operational performance and governance matters.
 - b) Escalate and highlight, as appropriate, to senior officers in the Council, where ALEO's actions and decisions do not align with the strategic objectives and priorities set by the council.
 - c) Offer advice and support to the board in delivering governance assurance.
 - d) Act as liaison between the Council and the ALEO and provide constructive feedback and recommendations to the ALEO based on observations and discussions with the Council.
 - e) Ensure they represent the views of the Council, both in board meetings and in their day-to-day interactions with the ALEO management.
 - f) Be prepared to address conflicts of interest or disagreements between the Council and the ALEO.

- g) Monitor the performance of the ALEO against agreed-upon targets, key performance indicators (KPIs), and service level agreements (SLAs).
 - h) To ensure the view of the Council is communicated effectively to the ALEO on matters affecting the Council.
- 3.5 **Training** – Clear training plans should be set out for the CO which are both relevant to the ALEO industry and the Council directorate. Training and learning will be identified by the Council in collaboration with the ALEO. The following core skills training will be offered to all COs, in addition to any specialised training needs identified for the specific ALEO:
- a) Taxation
 - b) Companies House filing requirements
 - c) Council Strategy / Objectives
 - d) ALEO Governance Framework
 - e) Reporting requirements
 - f) Conflict management
- 3.6 **Role Criteria** – Ensure the CO is suitably placed within the Council to be able to make decisions autonomously, whilst having reasonably direct access to Chief Officers to ensure issues can be escalated efficiently, the following criteria will apply:
- a) Must be at minimum a Head of Service within the Council. It may be appropriate for some COs to be a more senior member of staff (e.g. Executive/Service Director).
 - b) Where it is considered necessary for a more senior member of staff to act as the CO, the Directorate must ensure that officer has sufficient support in place to be able to fulfil the requirements of the role, particularly with reporting (below).
 - c) Should not be the Chief Executive of the Council, Section 95 Officer or the Monitoring Officer.
 - d) Must have the necessary skills and expertise to carry out the role to best support the ALEO (e.g. focus the skills of the CO in the most vulnerable or risk sensitive area of the ALEO, in order to best compliment its operations and provide the strongest possible assurance for the Council).
 - e) The CO must be given sufficient time and space from their existing workload and responsibilities to be able to fulfil the role effectively.
- 3.7 **Reporting** – To increase awareness of ALEO operations and performance with senior managements within the Council and to improve the efficiency of how potential issues can be escalated internally. The following measures of internal CO reporting will be implemented:
- a) CLT reporting every 6 months.
 - b) Short performance update report from CO's to CLT tailored to the individual ALEO.
 - c) Provide updates on ALEOs own risk registers.

d) Annual performance update report to GRBV or the appropriate committee as outlined in the Committee Terms of Reference. This will be similar to the reporting requirements of ALEOs but will be more governance focused with emphasis on assurance and control effectiveness.

3.8 **Board Protocols and Procedures** - Given the powers of ALEO Directors, the frequency of General Meetings (as prescribed in the Companies Act 2006) are rare and ALEO decision-making is taken almost exclusively at the Board level. Board Meetings are not regulated by the Companies Act in the same way as General Meetings are. The rules relating to Board member meetings will be set out in the ALEOs Articles of Association and supplemented where necessary by procedures and protocols which the ALEO Board makes itself for the conduct of its meetings, for example how meetings are called, how notice of a Board meeting is given and the method of circulating the agenda and meeting papers. The Council Observer must be given effective oversight with regard to Board meeting protocols and any proposed changes to Board meeting protocols must include consultation with the Council Observer. The agenda for Board meetings will typically be set by the Chair with input from the ALEO Chief Executive (or most senior officer/employee) and where appropriate the Council Observer.

Chapter Four – Board Members & Appointments

Board Members & Appointments

- 4.1 Elected Members are appointed to the boards of a number of Council ALEOs. Appointments to outside bodies is a reserved matter for Council. In some cases, the number of appointments for a particular organisation is specified in an organisation's governing document.
- 4.2 There are a number of potential advantages and disadvantages of Elected Members being appointed to ALEOs, as set out in Appendix 2.
- 4.3. Appointing Elected Members to Boards of ALEOs can help foster relationships and facilitate informed discussion by Elected Members at Council/Committee. However, while positive relations are beneficial for both the Council and ALEOs, appointing Members can create decision-making challenges for both the ALEO and the Council. There are a range of skills required for a Board to be high functioning decision making body and appointing Members limits the opportunity to appoint individuals with those specific skills, industry expertise and experience. Having a Board composed of expert individuals, allows Boards to be more nimble and make quicker and more fluid decisions.⁷
- 4.4 The conflict between a Board Member on an ALEO and an Elected Member can never truly be reconciled. Whilst most of the time that conflict will not be prevalent, it is not possible to fully mitigate as Members can never truly separate their roles as Elected Member and Director. Fulfilling both roles can leave Members in a position where they vote for something as a director because it is in the best interest of the organisation, but it conflicts with their political position or is not within the best interests of the Council. There is a stronger argument for appointing Elected Members to the Board of Charities/companies the Council does not own than to companies that the Council does own.
- 4.5. The Council can influence organisations that it owns through governance levers outlined in this framework (such as Shareholder Agreements). Given the Council can utilise governance documents to influence an organisation, there is no requirement for Elected Members to be appointed to the Board in order to influence a company. This removes the conflict-of-interest element for Elected Members as they can make decisions in Council/Committee without the conflict of being a board member.

⁷ Based on feedback received from ALEOs during consultation.

Membership of Boards

- 4.6. It is recommended that due to the conflict in interest situation and the difficult position that can arise for an elected member when there is a divergence between the interests of the Council and an ALEO:
- a) Elected Members should not be board members of any ALEO, and
 - b) Each Council owned ALEO should have an Elected Member/Shareholder forum.

Elected Member / Shareholder Forum

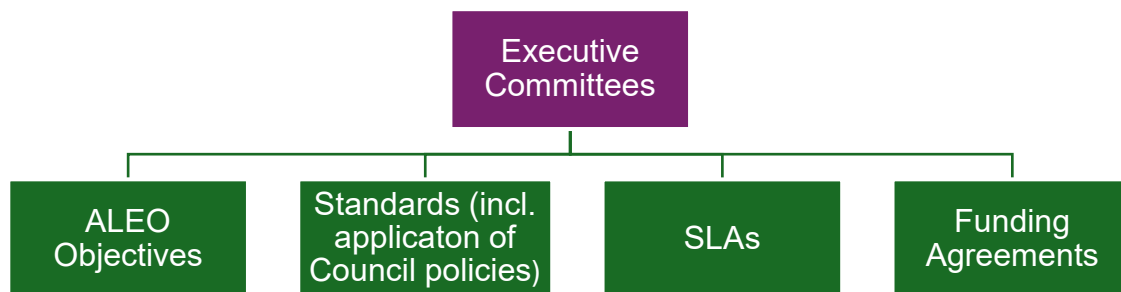
- 4.7. In order to support the scrutiny of ALEOs by Elected Members in the absence of Elected Members on Boards, an EM/Shareholder Forum will be established for each Council owned ALEO.
- 4.8. To provide consistency, this will be based on the model previously agreed for the Council's Transport Companies but will offer an appropriate degree of flexibility to suit the needs of the individual ALEO.
- 4.9. For this reason, a template for the forum is not provided for in this framework but should include details of the forum's purpose clear Terms of Reference, meeting arrangements, standing agenda items and representation/membership. The Governance Team will work closely with ALEOs and COs to develop appropriate forum structure and terms.

Chapter Five - Reporting, Scrutiny & Engagement

Governance & Scrutiny Reporting Structure

Governance Reporting Structure

- 5.1. To ensure the Council is able to meet its obligations in terms of ensuring best use of public funds and efficient delivery of services, implementing effective governance controls in relation to oversight and scrutiny of ALEOs is essential.
- 5.2. The Council’s executive committees are responsible for scrutinising ALEOs in a more operational focused approach. Therefore, the executive committees are required to approve ALEO Service Level Agreements, Funding Agreements, standards and objectives.



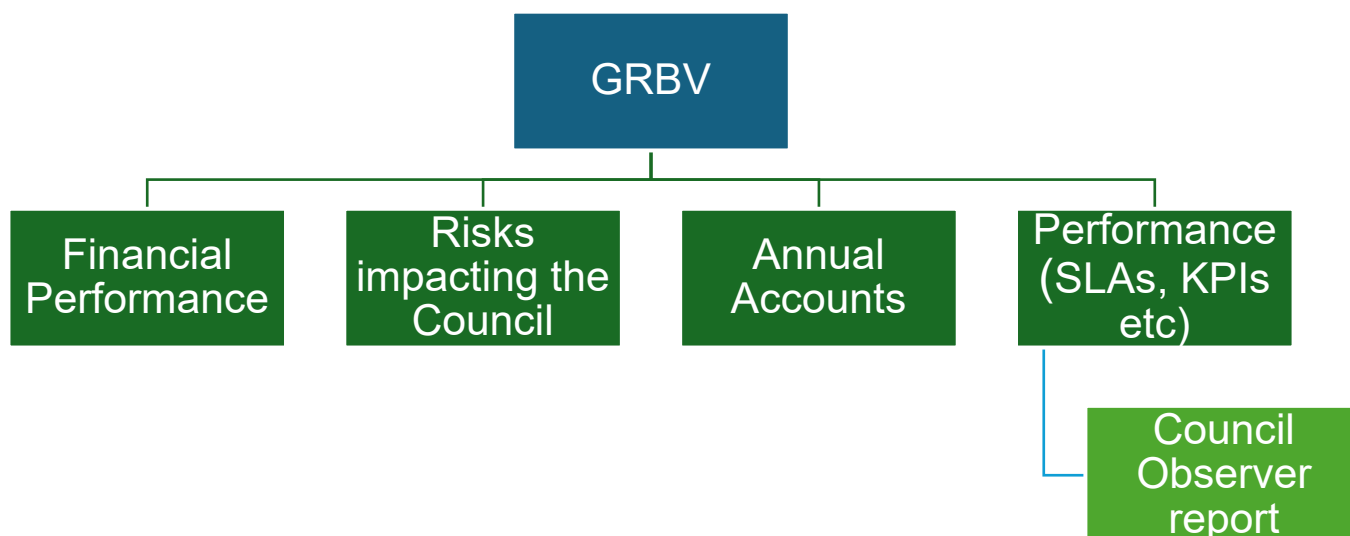
5.3. The below table details the ALEOs committee reporting lines:

Executive Committees		
Culture & Communities	Finance & Resources	Transport & Environment
<ul style="list-style-type: none"> • Edinburgh Leisure • Capital Theatres 	<ul style="list-style-type: none"> • EICC • Capital City Partnership • LPF 	<ul style="list-style-type: none"> • Lothian Buses • Edinburgh Trams

Governance, Risk & Best Value Committee (GRBV)

5.4. The core remit of the GRBV (or other appropriate committee as outlined in Committee Terms of Reference), in relation to ALEOs, is to ensure the Council is able to scrutinise the impact the performance of the ALEO has on the Council.

To achieve this, GRBV are responsible for scrutinising key areas, as detailed below.



Reporting & Scrutiny

- 5.5 The Council Observer (CO) will work closely with their ALEO to ensure that reporting requirements are met, and that duplication of reporting is avoided. It is accepted that there may be a degree of overlap of the information reported to GRBV and executive committees, but this should be avoided where possible. Additionally, it is noted that, particularly with regards to financial information, some detail may be excluded from reports where this is commercially sensitive. However, this should be kept to a minimum.
- 5.6 The Council's Governance Team and COs will work closely with the ALEOs to achieve a consistent reporting template. A representative from the ALEO's executive must present for consideration of report(s). The Council Observer should also be present.

Report Content

- 5.7 As a result of feedback from ALEOs and members, clarity of the information members want to see from ALEOs is a key improvement that future development of this framework will explore. Whilst not provided in this section, future development of this framework will potentially create template reporting tools to improve consistency in the information provided to the relevant Council committees. This will also make it easier for ALEOs to report accurately and efficiently and to make best use of their resources in generating reports.

Engagement

- 5.8 Continuous engagement between the Council and its ALEOs is recognised as an essential element of this framework. Strong engagement not only fosters a

collaborative relationship between the council and ALEOs but also provides a fundamental mechanism to ensure alignment with the council's strategic objectives, promote collective responsibility, and enhance service delivery to the community.

- 5.9 The Council's Governance Team will continue to play a key role in collaboration with its ALEOs and will support the following areas of engagement:
- a) ALEO Hub
 - b) Council Observers
 - c) Regular Ad-hoc drop in / advisory sessions for ALEOs on key topics – bringing together subject matter experts for advice and guidance where required.

ALEO Hub

- 5.10 A key element of continuous engagement is the current Governance Hub, which brings together the ALEO Chief Officers and the Council's Chief Executive.
- 5.11 Initially designed to form a mechanism of governance and assurance monitoring, this has developed into an open ideas-sharing and information exchange for Chief Officers. It is recognised that in order to best support the performance of ALEOs and to provide Chief Officers with vital, and often scarce, opportunities to reflect with their peers from a variety of industries the Council's ALEOs operate in, the more fluid nature of the group should be reinforced. Therefore, the Governance Hub will continue, but in a slightly different format, and will be renamed to the ALEO Hub to better reflect the purpose of the group.
- 5.12 New Terms of Reference for the ALEO Hub are included for information at Appendix 3, and the former governance related functions of the group will be re-directed to a more appropriate group level, a newly established Council Observers Forum (see Appendix 3).

Council Observer's (CO's) Forum

- 5.13 With the adjustment of the ALEO Hub to a more fluid and ideas exchange based forum, re-focusing of the governance and assurance monitoring elements of the former Governance Hub are required.
- 5.14 The creation of a Council Observers Forum will bring together CO's from across the Council in a space to carry out discussions with a higher focus on governance. This group will focus on the following:
- (a) Key issues emerging across ALEOs which may affect other areas of the Council.

(b) Allow discussion and ideas exchange for assurance controls and corrective action for emerging issues.

(c) Recognise and escalate more pressing issues which may require attention of Chief Officers.

(d) Share best practice ideas on a number of ALEO governance functions including:

Record keeping

Training,

Reporting,

Board actions and scrutiny.

5.15 This forum will also allow COs to support each other with their other duties as detailed in Chapter 3 of this framework.

Chapter Six – Assurance

6.1. This section aims to provide a general overview of the various governance controls in place between the Council and the ALEOs. Additionally, a route map of the interactions between the ALEO and the Council are explained to show how this supports and underpins assurance as various stages.

Assurance Controls Overview

6.2. The ALEO and Council share common assurance goals but carry out specific functions separately to achieve assurance across a number of risks. The following table sets out a clear delineation of assurance controls. The list of controls is not exhaustive, and some controls are not explicitly covered in this framework but are achieved through day-to-day interactions between the Council and ALEOs. Those recorded here are to provide a general overview of controls in place across various mechanisms.

Assurance Controls	
ALEOs	Council
Governing Document - compliance	Governing Document - drafting
SLAs - compliance	SLAs - drafting
Shareholder Agreement	Funding Agreement
Remuneration & Selection	Record Keeping - central directory / database
Record Keeping internally	KPI - setting & monitoring
KPI - reporting	Scrutiny
Reporting	Council Observer
Board rolling action log	ALEO Hub
Business plan	CO Forum
Audit arrangements	

Assurance Process and Route Map

6.3. Continuous open dialogue between the Council and ALEOs is important to ensure that both can be adaptable, and able to react quickly, to change.

Policy

6.4. The Council and ALEOs will interact with each other via a number of different routes. It is the role of elected members to approve governance documents (as

detailed in Chapter 5) which will provide members with the opportunity to ensure an organisation complies with any specific Council policies. Elected Members will also have an opportunity through the Shareholder Forum to raise policy matters, although the Shareholder Forum is not a formal decision-making body (as detailed in paragraphs 4.7 to 4.9)

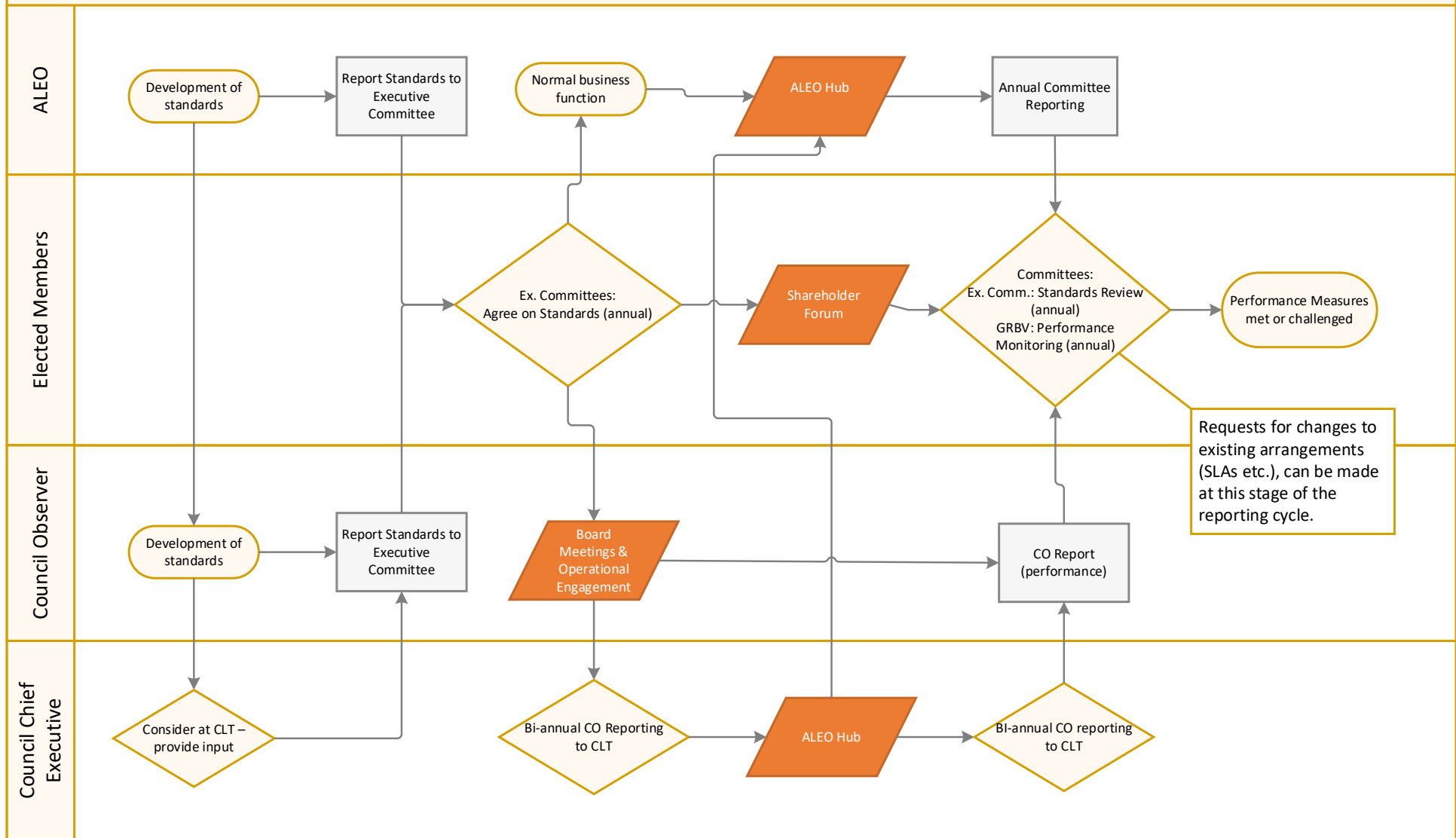
- 6.5. The Council Observer (as detailed in Chapter 3) is appointed to carry out primarily an observational role but also to support good governance of the ALEO. However, the CO will develop a relationship with the ALEO and have an understanding of the ALEOs direction and will therefore be able to report back to the Council on matters of policy, or report matters of policy directly to the ALEO.
- 6.6. ALEOs will be able to raise policies at the Shareholder Forum that they may wish the Council to consider are included in future governance documents. The purpose of the forum is to provide a space that will facilitate dialogue and relationship building between ALEOs and elected members and it is recommended that policy matters is a standing agenda item at the Shareholder Forum
- 6.7. ALEOs can also raise issues or opportunities with the Council out with the Shareholder Forum. This may be done through contacts in the service area or through the Council Observer. If ALEO officers are raising issues with the service area representative, they should copy the Council Observer into all correspondence. Significant issues should also be communicated to the relevant executive director.

Monitor ALEO Performance

- 6.8. Elected Members will scrutinise the performance of ALEOs annually at the Governance, Risk and Best Value Committee (as detailed in Chapter 5) or the appropriate committee as outlined in the Committee Terms of Reference. ALEO's reporting in terms of the Annual Governance Statement is reported through assurance schedules being submitted to their relevant directorate. The relevant executive director then determines whether they feel it is appropriate for any issues highlighted to be included in their assurance schedules and reported in the Annual Governance Statement.
- 6.9. The Council Observer will monitor the performance of ALEOs by being given a copy of board meeting papers and attending board meetings. It is also part of the COs role to contribute to the ALEO reports for Council's committees.

- 6.10. ALEOs will scrutinise their performance at their board meetings and by having an audit/scrutiny committee in place (as detailed in paragraph 2.11). It is also recommended that performance reports are considered at the Shareholder Forum.
- 6.11. There are a number of methods in which ALEOs, COs and elected members can interact with each other to influence and respond to changes in circumstance. The following figure aim to set out how each stakeholder interact with each other:

Interaction Flow Chart



Appendix 2

Appointments to Boards	
1. Potential Advantages	2. Potential Disadvantages
<p>(a) Elected Members on Boards can improve the relationship between the Council/Elected Members and the ALEO.⁸ Elected Members sitting on Boards can allow for relationship building and be conducive to positive working relationships.</p>	<p>(a) The additional workload of being appointed to an ALEO Board can bring additional demands to an Elected Member's already diverse and challenging role.⁹</p>
<p>(b) Elected Members can bring an insight into the ALEO and its objectives to the Council as well as bringing the Council's insights into the ALEO.¹⁰</p>	<p>(b) Elected Members may lack the knowledge and skills required for the role.¹¹ Whilst it is recognised that Boards should have a balance of skills and experience,¹² appointments should be based on merit and objective criteria.¹³</p>

⁸ Local authority owned companies: a good practice guide, 2022; p.50

⁹ Local authority owned companies: a good practice guide, 2022; p.50

¹⁰ Local authority owned companies: a good practice guide, 2022; p.50

¹¹ Local authority owned companies: a good practice guide, 2022; p.50

¹² The Effective Board: Building Individual and Board Successes, 2010

¹³ UK Corporate Governance Code, 2024, p.11

<p>(c) There is an advantage that Elected Members understand the policy picture greater at Committee/Council because they are involved in an ALEO in the same industry.</p>	<p>(c) There is a risk of conflict of interest between their role as Elected Member and ALEO appointee.¹⁴ These conflicts can become more stark if an ALEO gets into difficulties.¹⁵ Under the Companies Act 2006 and Charities and Trustee Investment (Scotland) Act 2005 Directors/Trustees have a fiduciary duty to act in the best interest of the company/charity. This may conflict with the best interest of the Council. The Standard Commission's 2021 Code of Conduct for Councillors includes a section on Appointments to Outside Organisations.¹⁶</p>
<p>(d) Elected Members can gain valuable experience of service issues and different sectors¹⁷ as well as bringing their knowledge of the Council and its services. Being directly involved with the work of an ALEO can enhance an Elected Member's skillset and allow them to fulfil their role as an Elected Member with more knowledge and skills.</p>	<p>(d) In the Edinburgh Tram Inquiry Report, Lord Hardie described the governance and oversight of 'Tie Ltd' as an arms-length company to the Council and the role of Elected Members on the company board. Lord Hardie noted the role of Elected Members on the Board was ineffective and did not satisfy the purposes for which it was carried out and gave rise to a false feeling of confidence.¹⁸ The effect on the project of the requirement of directors to act according only to the company's interests (as above) was that the presence of Elected Members as directors did not mean that it was necessarily possible to give effect to the interests of the Council in decision-making.</p>

¹⁴ The City of Edinburgh Council, Internal Audit, Arm's Length External Organisations; p.12

¹⁵ Audit Scotland, Council' use of arm's-length organisations, 2018; p.20

¹⁶ Code of Conduct for Councillors, 2021 '*abide by the rules of conduct and will act in the best interests of that body or organisation and be responsible for identifying, and taking advice on, any conflicts of interest that may arise between the company/charity and the Council*', p. 11

¹⁷ Local authority owned companies: a good practice guide, 2022; p.50

¹⁸ Edinburgh Tram Inquiry Report, 2022, p.821

<p>(e) Councillors bring their experience as elected community representatives.¹⁹ As well as bringing their knowledge of the Council and its services to an ALEO, in their role as Elected Members also understand what different community needs are.</p>	<p>(e) There is a continuity risk and succession planning difficulties for ALEOs if Elected Members lose their position within the Council or seat.</p>
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¹⁹ Audit Scotland, Council' use of arm's-length organisations, 2018; p.22

Appendix 3

ALEO Hub Terms of Reference		
Chair:	Chief Executive, City of Edinburgh Council (CEC)	<p>Core Membership</p> <p>As below or suitable deputy:</p> <p>Chief Executive - City of Edinburgh Council. Executive Director of Corporate Services – CEC. Executive Director of Place – CEC. Head of Democracy & Governance - CEC.</p> <p>Edinburgh International Conference Centre - Chief Executive. Lothian Buses – Operations Director. Edinburgh Trams – Managing Director. Capital Theatres – Chief Executive. Edinburgh Leisure – Chief Executive. Capital City Partnership – Chief Executive. Lothian Pension Fund – Chief Executive.</p>
Lead Officer/Secretariat:	Head of Democracy & Governance	
Admin Secretariat:	Governance Officer(s) CEC	
Location	Rotational	
Frequency	Quarterly	
Duration	2 Hours	
Remit:	<ul style="list-style-type: none"> • To provide regular updates on delivery of services by ALEOs • To ensure that the Council is aware of any new and emerging risks • To allow for the opportunity to provide expertise briefings to or from ALEOs, for general awareness of a subject relevant to the group. • To aid discussion on exploring opportunities to collaborate on projects, issues and joint ventures. • To raise any issues or concerns directly with the Council. 	
Escalation	CEC Corporate Leadership Team and/or GRBV/Pensions Committee/Council	
Review	These Terms of Reference will be reviewed annually.	

Appendix 1

Appointments to Boards	
Potential Advantages	Potential Disadvantages
<p>1.1 Elected Members on Boards can improve the relationship between the Council/Elected Members and the ALEO.¹ Elected Members sitting on Boards can allow for relationship building and be conducive to positive working relationships.</p>	<p>1.2 The additional workload of being appointed to an ALEO Board can bring additional demands to an Elected Member's already diverse and challenging role.²</p>
<p>1.3 Elected Members can bring an insight into the ALEO and its objectives to the Council as well as bringing the Council's insights into the ALEO.³</p>	<p>1.4 Elected Members may lack the knowledge and skills required for the role.⁴ Whilst it is recognised that Boards should have a balance of skills and experience,⁵ appointments should be based on merit and objective criteria.⁶</p>
<p>1.5 There is an advantage that Elected Members understand the policy picture greater at Committee/Council because they are involved in an ALEO in the same industry.</p>	<p>1.6 There is a risk of conflict of interest between their role as Elected Member and ALEO appointee.⁷ These conflicts can become more stark if an ALEO gets into difficulties.⁸ Under the Companies Act 2006 and Charities and Trustee Investment (Scotland) Act 2005</p>

¹ Local authority owned companies: a good practice guide, 2022; p.50

² Local authority owned companies: a good practice guide, 2022; p.50

³ Local authority owned companies: a good practice guide, 2022; p.50

⁴ Local authority owned companies: a good practice guide, 2022; p.50

⁵ The Effective Board: Building Individual and Board Successes, 2010

⁶ UK Corporate Governance Code, 2024, p.11

⁷ The City of Edinburgh Council, Internal Audit, Arm's Length External Organisations; p.12

⁸ Audit Scotland, Council' use of arm's-length organisations, 2018; p.20

	<p>Directors/Trustees have a fiduciary duty to act in the best interest of the company/charity. This may conflict with the best interest of the Council. The Standard Commission’s 2021 Code of Conduct for Councillors includes a section on Appointments to Outside Organisations.⁹</p>
<p>1.7 Elected Members can gain valuable experience of service issues and different sectors¹⁰ as well as bringing their knowledge of the Council and its services. Being directly involved with the work of an ALEO can enhance an Elected Member’s skillset and allow them to fulfil their role as an Elected Member with more knowledge and skills.</p>	<p>1.8 In the Edinburgh Tram Inquiry Report, Lord Hardie described the governance and oversight of ‘tie Ltd’ as an arms-length company to the Council and the role of Elected Members on the company board. Lord Hardie noted the role of Elected Members on the Board was ineffective and did not satisfy the purposes for which it was carried out and gave rise to a false feeling of confidence.¹¹ The effect on the project of the requirement of directors to act according only to the company’s interests (as above) was that the presence of Elected Members as directors did not mean that it was necessarily possible to give effect to the interests of CEC in decision-making.</p>
<p>1.9 Councillors bring their</p>	<p>1.10 There is a continuity risk and</p>

⁹ Code of Conduct for Councillors, 2021 ‘*abide by the rules of conduct and will act in the best interests of that body or organisation and be responsible for identifying, and taking advice on, any conflicts of interest that may arise between the company/charity and the Council*’, p. 11

¹⁰ Local authority owned companies: a good practice guide, 2022; p.50

¹¹ Edinburgh Tram Inquiry Report, 2022, p.821

<p>experience as elected community representatives.¹² As well as bringing their knowledge of the Council and its services to an ALEO, in their role as Elected Members also understand what different community needs are.</p>	<p>succession planning difficulties for ALEOs if Elected Members lose their position within the Council or seat.</p>
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¹² Audit Scotland, Council' use of arm's-length organisations, 2018; p.22

Appendix 3

ALEO	Ownership	Members on Board	Chair
CEC Holdings Limited	100% owned by CEC	3 Cllrs	Cllr Chair
EICC	100% of voting rights held by CEC Holdings Limited (other non-voting shares in issue)	5 Cllrs	Cllr Chair
Capital Theatres	CEC is a member (Private company limited by guarantee without share capital)	2 Cllrs	Non-Cllr Chair
Capital City Partnership	CEC is sole member (Private company limited by guarantee without share capital) (Articles of Association approved on 20 January 2012 state that membership is only open to the City of Edinburgh Council)	3 Cllrs	Cllr Chair
Transport for Edinburgh*	100% owned by CEC	4 Cllrs	Cllr Chair
Edinburgh Trams	100% subsidiary of Transport for Edinburgh Limited	None	Non-Cllr Chair

Lothian Buses	91.01% Transport for Edinburgh Limited/5.47% Midlothian Council/3.13% East Lothian Council/0.39% West Lothian Council	None	Non-Cllr Chair
Edinburgh Leisure	CEC is a member (Private company limited by guarantee without share capital)	5 Cllrs	Non-Cllr Chair
*Transport for Edinburgh closing in its current form.			