

Report under Ss.114 and 114A of the Local Government Finance Act 1988

Report to all members of Northumberland County Council

To be considered by:

The Cabinet in respect of Executive responsibilities (S.114A)

The County Council in respect of non-executive responsibilities (S.114)

Report of: **Jan Willis, Interim Executive Director of Finance and
Section 151 Officer**

Date of Report: **23rd May 2022**

1. Purpose of report and executive summary

- 1.1. I am appointed by Northumberland County Council as the Chief Finance Officer under Section 151 of the Local Government Act 1972.
- 1.2. Sections 114 and 114A of the Local Government Finance Act 1988 (the 1988 Act) require me to make a report if it appears to me that the authority, a committee of the authority, or any person holding any office or employment under the authority:
 - (a) has made or is about to make a decision which involves or would involve the authority incurring expenditure which is unlawful;
 - (b) has taken or is about to take a course of action which, if pursued to its conclusions, would be unlawful and likely to cause a loss or deficiency on the part of the authority; or
 - (c) is about to enter an item of account the entry of which is unlawful.
- 1.3. It is the obligation of the Council (and the Cabinet in relation to executive responsibilities) to consider this report within 21 days of the date it is sent to members.
- 1.4. Following careful consideration of matters which have come to my attention, I came to a view that it was likely that the Council had incurred items of unlawful expenditure. I have now taken expert advice from Nigel Giffin QC and consulted my professional body, the Chartered Institute of Public Finance and Accountancy (CIPFA). On the basis of Mr Giffin's advice, I was confirmed in my initial views. I attach to this report a redacted version of Mr Giffin's Opinion at Appendix A.
- 1.5. I am sharing this legal advice with members, as I consider it necessary and proportionate to do so, and as a matter of public interest, and under the statutory access to information provisions, this report and the attached advice are expected to be made public. However, I must emphasise that this does not

constitute any wider waiver of professional legal privilege or litigation privilege that attaches to any other documents concerning these or other issues.

- 1.6. In accordance with my statutory obligations, I commenced a formal consultation with the Head of Paid Service, and the Monitoring Officer on 25 April 2022, and I consulted the Leader of the Council, the portfolio-holder and the Deputy Chief Executive on a voluntary basis, as well as making all Group Leaders and the external auditor aware of my consultation. I have received consultation responses, and I have considered carefully all of those comments. The consultation responses and my comments on them are also attached to this report as appendix B. I would particularly draw members' attention to the consultation response from the Monitoring Officer as set out in the Appendix.
- 1.7. Together with the Monitoring Officer, I have considered and taken advice, in relation to Data Protection issues, and the Access to Information Rules applicable to Council meetings. There is guidance from the Information Commissioner's office that particularly deals with the disclosure of information relating to the remuneration of senior officers of local authorities, and of course duties under the Local Audit and Accounting regime, the transparency code, and statutory guidance issued by DLUHC (Department for Levelling Up Housing and Communities). Having regard to the regulatory framework and weighing the public interest in there being openness and transparency relating to the matters set out in this report, against the private interests of individuals, I have reached the view that the council should disclose the fullest information it possibly can. A material factor is that all of the officers identified or identifiable in this report are (or were) senior chief officers. Furthermore, the data protection legislation provides in principle for such disclosure, where the publication is necessary in the exercise of a statutory function, such as my functions as Chief Finance Officer in this case.
- 1.8. The items of unlawful expenditure that are the subject of this report concern the following matters:
 - 1.8.1. The County Council participated (alongside the Northumbria Healthcare NHS Foundation Trust – referred to in this report as 'the NHCT') as a principal in the Northumbria International Alliance (NIA). This was an unincorporated partnership established to provide international consultancy services for a commercial purpose. NIA traded commercially from at least 2018 to 2021 and did so otherwise than through a company with all of the related income and expenditure being recorded in the Council's accounts. This is a breach of Section 4(2) of the Localism Act 2011. Commercial trading activity is an executive function of the Council, and this section of the report falls to be considered by the Cabinet under S114A(2) of the 1988 Act.
 - 1.8.2. Secondly, the County Council made and continues to make payment of a special "international allowance" of £40,000 per annum to the Chief Executive. This appears to have commenced in 2017 and was initially paid to the Chief Executive in her previous role as Deputy Chief

Executive. Payment continues to be made to the present day. I am satisfied that the payment does not have proper authorisation and is in contravention of the Council's pay policy statements. This is a breach of Section 41 of the Localism Act 2011 and s112(2A) of the Local Government Act 1972. Employment generally, and the remuneration of chief officers is a non-executive function and as such, that element of this report falls within the scope of S114(2) of the 1988 Act and is addressed to the County Council itself.

- 1.9. As set out above, the purpose of this report is to bring to members' attention, as I am required to do under s114 and s114A of the 1988 Act, that it appears to me that the Council has incurred unlawful expenditure. The report does not seek to attribute to any individual blame or responsibility for actions or omissions that have led to the unlawful expenditure identified in this report and should not be read as such.
- 1.10. Members may have heard of a 'Section 114 Report' in the context of a council 'going bust'. I must emphasise that this is not the case with Northumberland County Council and it must not be inferred from the fact that I am making this report that I have any concerns about the Council's ability to balance its budget either in the short or medium term. The requirements of S.114 and S.114A also apply to the reporting of unlawful expenditure even where, as here, there are no budgetary issues.
- 1.11. The provisions of S.115 of the 1988 Act require the authority to consider this report within 21 days of the date on which it is sent to members. Following consultation with the Business Chair, he has agreed for this report to be put on the agenda for consideration at the Extraordinary Meeting of the County Council to be held on 8 June 2022.
- 1.12. S.115 (2) of the 1988 Act requires the authority to determine at that meeting whether it agrees or disagrees with the views contained in this report and what action (if any) it proposes to take in consequence of it.
- 1.13. The provisions of S.115 establish a 'prohibition period' which starts on the day on which this report is sent to members and ends on the business day following consideration of this report. During this 'prohibition period' the course of conduct I have identified as leading to 'unlawful expenditure' shall not be pursued.
- 1.14. In the case of NIA and the 'international business', it would appear from the information provided to me that the Council has not suffered any financial loss and I am satisfied that any future or on-going expenditure will now be incurred by Northumbria Integrated Consultancy Limited (NICL), a wholly owned subsidiary of the County Council and would therefore be lawful. In my opinion the prohibition period does not apply to any expenditure incurred through NICL. Nor do I believe that in all the circumstances there is any financial or public interest in seeking to void any of the contracts the Council entered into without

the necessary powers or seek recovery of any sums of unlawful expenditure incurred as a result.

- 1.15. In relation to the payment of the International Allowance, I am satisfied that the expenditure remains unlawful. The provisions of the 1988 Act will take effect to automatically stop payment of the International Allowance for a period of 21 days from the date on which this report is sent to members. This is called the 'prohibition period'. Given the detailed legal opinion provided by Mr Giffin QC, issues relating to the International Allowance, the extent to which (if at all) it could ever have been justified, or paid, and whether, and if so to what extent, the County Council could, or should, continue or resume payment of an allowance, or seek to recover the past unlawful expenditure, should in my view, be referred to the Staff and Appointments Committee for detailed consideration. I further recommend that additional legal advice on this matter be taken from Mr Giffin to inform the Committee's consideration. The recommendations of the SAC can then be reported back to the County Council, if required, in due course. In the meantime, it remains the case that there is no legal basis for payment of this allowance to be made (and nor could any proper decision to pay such an allowance be reached on the basis of the information currently available).
- 1.16. The background, legal framework, findings and recommendations are set out in this report.
- 1.17. As referenced above, in preparing the report I have taken advice from Nigel Giffin QC (paragraph numbering refers to his Opinion) who has concluded that
 - 1.17.1. *(Para 49) "...it is clear that the Council in this case engaged, otherwise than through a company, in activities undertaken for a commercial purpose. It had no powers to do so, and the expenditure incurred specifically for the purpose of those NIA activities was therefore unlawful".*
 - 1.17.2. *(para 50) "...the Council's Chief Executive was paid an allowance on top of her normal salary on account of responsibilities undertaken in connection with NIA. It is unlikely that the decision to pay such an allowance could have been validly taken by anybody other than the full council. Certainly, there is no evidence, that I have so far seen, of the allowance being decided upon or approved by anybody or person who might even arguably have had the power to do so. Accordingly, the payment of the allowance also amounted to unlawful expenditure."*
 - 1.17.3. *(para 51) "It is evident that the CFO must make a statutory report or reports on these matters."*

2. Legal framework for a section 114 report

- 2.1. Section 114(2) of the 1988 Act requires that the chief finance officer of a relevant authority shall make a report under this section if it appears to her that the authority, a committee of the authority, a person holding any office or employment under the authority or a joint committee on which the authority is represented
 - (a) has made or is about to make a decision which involves or would involve the authority incurring expenditure which is unlawful;
 - (b) has taken or is about to take a course of action which, if pursued to its conclusions, would be unlawful and likely to cause a loss or deficiency on the part of the authority; or
 - (c) is about to enter an item of account the entry of which is unlawful.
- 2.2. The process for issuing a s.114 report and the effect of it are set out in the 1988 Act. Subsection 3(A) requires the Chief Finance Officer to consult, so far as reasonably practicable, the Head of Paid Service and the Monitoring Officer. The purpose of this requirement is to ensure so far as practicable, a corporate response to the issues raised. The circumstances that have given rise to this report are somewhat unusual, in that they concern activities for which the Head of Paid Service had direct managerial responsibility and affect her own remuneration. The Chief Executive is also absent from work at present.
- 2.3. Nevertheless, I considered it practicable to consult the Head of Paid Service, and I have received consultation responses from her, the Deputy Leader, the External Auditor and the Monitoring Officer. A summary of these responses, together with my comments (informed by legal advice) is set out in Appendix B attached to this report.
- 2.4. Section 115 requires the Council (or Cabinet in relation to executive matters) to consider the report at a meeting, where it shall decide whether it agrees or disagrees with the views expressed in the report and what action (if any) it proposes to take in consequence of it. Those meetings must be held no later than 21 days beginning with the day the report is sent to members. Consideration of this report is reserved to full council in the case of a report under s114(2) of the 1988 Act and the executive (i.e. Cabinet) in the case of a report under s114A(2), it cannot be delegated.
- 2.5. In this case, the provisions of both s114(2) and s114A(2) of the Act are engaged, as the matters that are the subject of this report touch on both executive and non-executive matters.
- 2.6. The 1988 Act requires that the external auditor is sent a copy of the report and informed of the report and the time, date and place of the meeting(s) at which the report will be considered. The external auditors also must be informed of the outcome of the meeting(s) as soon as practicable.
- 2.7. The external auditor has been kept informed of the emerging position and of my proposal to issue this report. The external auditors will need to consider the

implications of the report on their statutory functions and, in particular, their opinion on the 2019/20 and 2020/21 or prior year accounts and whether any further action is required.

- 2.8. Contact has been made with the Department for Levelling Up, Housing and Communities in advance of issuing this s114 report. The Leader of the Council and Deputy Leader (as portfolio holder for finance and governance), Deputy Chief Executive (in the absence of the Chief Executive), the Monitoring Officer and Executive Directors have also been kept up to date on the emerging situation. The legal opinion from Mr Giffin has also been shared with the consultees and Group Leaders. In consultation with the Deputy Chief Executive, Monitoring Officer and Leader, and in view of the inevitable public interest, I have arranged for a copy of this report to be published on the County Council's website shortly after it is sent to members and for the local Members of Parliament and other stakeholders to be advised of its existence.

3. Background

3.1. Since my appointment as Chief Finance Officer in February 2021, I have sought assurances in relation to the lawfulness of international consultancy activities and the payment of the international allowance to the Chief Executive and in particular:

- (a) the intentions of the Council when entering into contracts to provide international consultancy activities;
- (b) the legal powers on which the Council could have relied in undertaking those activities during the period 2016 to 2021 other than the general power of competence, which is subject to the requirement to conduct commercial activities through a company
- (c) the reasons why such a company was not established until 2021;
- (d) the process by which the payment of an international allowance to the Chief Executive was approved and specifically whether that was in compliance with the requirements of s112 and 112A of the Local Government Act 1972 and s41 of the Localism Act, which requires such payments to be made in accordance with the Council's pay policy statement.

3.2. Having sought assurances from officers as to the lawfulness of these transactions, I was unable to satisfy myself and I commissioned advice from leading counsel to inform my formal opinion. That advice from Nigel Giffin QC is appended (Appendix A) and is quoted throughout this report. Mr Giffin is one of the leading experts in local government powers and responsibilities.

4. Northumbria International Alliance

4.1. In September 2016, NCC and Northumbria Healthcare Trust (NHCT) were invited by UK Trade and Investment to consider exporting models of healthcare.

The then Chief Executive agreed that NCC would provide support to the Trust in relation to these activities, including legal, contracting, finance and business development. It would appear that this was an informal arrangement, as I have not been able to locate any written agreement or memorandum of understanding setting out the services to be provided, or the basis for those activities to be undertaken or arrangements for cost recovery.

- 4.2. In February 2017, NHCT established the Northumbria International Alliance (NIA) as a “go to market” brand with the Christie NHS Foundation Trust as its initial partner. In the same month the Council appointed a Director of International Projects and System Transformation. The Council report approving the creation of this role stated that this was a joint role to be funded as part of a tripartite arrangement between NCC, NHCT and the Clinical Commissioning Group (CCG), although in the event the CCG did not contribute for reasons that are unclear, and the costs of the role were shared on a 50/50 basis by the Council and NHCT.
- 4.3. In July 2017, the Director of International Projects made a presentation to Informal Cabinet and the Board of NHCT on the business development strategy for NIA. Informal Cabinet supported the proposal to provide support functions to NHCT in support of the strategy. The overarching mission of the partnership was described as “to deliver sustainable, profitable, large-scale revenue from international activities”. Strategic objectives were described in commercial terms – for example, to build a £100m revenue stream over 5 years by focusing on multi-year income potential opportunities offering the highest contract income and profits.
- 4.4. Although the strategy referenced a number of peripheral benefits, it is clear to me that the main purpose of NIA was to act as a commercial vehicle and that the Council’s motivation in participating in NIA was to generate income.
- 4.5. This is also the view of Nigel Giffin, QC who has advised that *“On the information I have seen, I have no doubt that the Council’s predominant, and indeed perhaps its sole, purpose in pursuing the NIA collaboration was to generate a financial return which could be deployed to help fund its normal activities as a local authority.....”*
- 4.6. From the Spring of 2017 NCC began providing support services to NHCT in connection with international business development opportunities. The scope of these services and the basis on which they were provided is unclear, and since trading accounts and comprehensive records of time spent by NCC officers on international activities were not kept, it is not possible to establish the relevant costs or whether these were ever fully recovered.

- 4.7. In December 2017, the Council entered into a contract with a company incorporated and based in the United Arab Emirates. The value of this contract was £100,000.
- 4.8. In April 2018, the Council and NHCT as joint signatories entered into a contract to provide consultancy services to a company in China. The value of this contract was £646,680.
- 4.9. In August and September 2018, presentations were made to the NHCT Audit Committee and to an informal Cabinet briefing, updating them on the progress of the international consultancy strategy. Next steps outlined in the presentation included forming a new NCC wholly owned company. Subsequently, meetings took place with NCC legal advisers, Ward Hadaway LLP in September 2018 to discuss options for the form of a trading vehicle, however these do not appear to have considered the requirements of the Localism Act and the fact that the Council was already trading commercially at that point.
- 4.10. Around the same time, the then chief finance officer appears to have advised that preparatory work should be undertaken so that NCC would be ready to set up a company through Cabinet resolution should NCC come close to signing any contracts. It is unclear why officers did not recognise that the requirement to establish a company had already been triggered, given that the Council had entered into commercial contracts with a value of more than three quarters of a million pounds, at that time, with negotiations underway for further multi-million pound contracts.
- 4.11. In November 2018, NCC entered into a contract with a company incorporated and trading in the Republic of Ireland. The value of this contract was £2,954,803. The contract was cancelled prior to work commencing and the deposit of £50,000 returned to the client.
- 4.12. In December 2018, NCC and NHCT entered into an overarching co-operation agreement under which they agreed to collaborate on new commercial opportunities.
- 4.13. Further legal advice was taken from Ward Hadaway in June 2019 around company arrangements including articles of association. The advice note refers to the requirement to conduct commercial activities through a company in accordance with the Localism Act. However, it was not until almost two years later that Northumbria Integrated Consultancy Ltd (NICL) was in fact established.
- 4.14. In September 2019, a further officer briefing was provided to Informal Cabinet. Informal Cabinet were advised that the first contract with the Chinese company had a value of £600,000 was in delivery with a forecast profit of £236,644 and negotiations were underway with that company for phase 2, with a prospective value of £16m over 10 years. Informal Cabinet were also advised that

negotiations with another (different client) based in the United Arab Emirates for a contract with a prospective contract value of £39.6m were in progress with contract signature expected in January 2020.

4.15. That report stated that

"we are now at a critical time in terms of decision making should we decide to progress the next phase of development via the new UAE contract which will lead to a step change in this work and it will be necessary to form a subsidiary company to ensure that there is effective governance and oversight. Advice has been taken from Ward Hadaway in order to ensure appropriate governance is in place and a company could be established at minimal cost".

- 4.16. In February 2020, Cabinet formally approved the establishment of a group holding company with up to 10 subsidiaries to support general commercial trading activities. However, it was not until 17 September 2020 that Northumberland Enterprise Holdings Ltd (NEHL) was registered at Companies House and a further 6 months after that before Northumbria International Consultancy Ltd (NICL) was registered on 29 March 2021. In the meantime, in June 2020, NCC signed the phase 2 contract with the Chinese company with a value of £2 million. The total value of commercial contracts signed prior to the incorporation of NICL was £5.8m and the value of contracts delivered was £2.8m. This cannot conceivably be regarded as *de minimis*.
- 4.17. In summary, it appears to me that the Council engaged in international consultancy activities between, at the latest 2018 and 2021 for a commercial purpose and otherwise than through a company. Legal opinion confirms that there is no lawful basis for the County Council having done so or to have incurred the substantial expenditure occasioned as a result. In entering into international contracts directly, NCC acted unlawfully, and it therefore follows that the expenditure incurred in delivering those contracts was also unlawful.
- 4.18. The expenditure involved was significant – at least £2.2m during the financial years 2017/18 to 2020/21, thus bringing s114(A) into play. Although it does not appear that the Council has suffered financial loss, and may have made some net gain, this cannot be definitively proven as proper trading accounts and contemporaneous records of all time spent by NCC officers supporting the delivery of these contracts and other business development activities were not kept.

5. International Allowance

- 5.1. It is currently unclear precisely when the international allowance began to be paid, but it seems to have been at about June 2017, to the then Deputy Chief Executive. In email correspondence with the Director of HR at NHCT dated July 2017 Mrs Lally (who was at that time Interim Chief Executive) refers to being separately remunerated by the Council as lead on the international work. However, no reference is made to a separate allowance in payroll records prior to December 2017.

- 5.2. The County Council considered an item of business in closed session in September 2017 regarding the restructure of the Executive Management Team. On page 5 of that report, there is a note on bullet point 8, which states that the "Chief Executive [not Deputy] will be responsible for the Commercial International lead for NCC and System Transformation Support with Northumberland Commissioning Group (CCG) (separately remunerated)". This does not specify who would be paying any separate remuneration, or how much it was intended to be, or what it is for.
- 5.3. At that stage, recruitment to the role of Chief Executive in the new structure had not taken place. Importantly, the report to Council did not invite any decision on that issue or specify at what rate or by which body any such allowance would be paid.
- 5.4. The resolution at paragraph 3 of the September 2017 report is to agree the remuneration of the [new] Executive Management Team "as outlined in the report". Recommendation 5 in the report delegates responsibility for nominating a Deputy Chief Executive [in the new structure] to the [new] Chief Executive in consultation with the Leader of the Council and makes provision for that post [the Deputy Chief Executive] to receive an additional allowance. The report does acknowledge that the then Deputy Chief Executive (Mrs Lally) had responsibility for leading the nascent international business. However, there is no mention that this work was separately remunerated, as such.
- 5.5. Appendix 2 of the September 2017 report shows the [new] Chief Executive on a gross salary of £186,915 with the column showing the 'cost to the council' as £123,081, including on-costs. This is consistent with that post being 0.5FTE. The next line shows an 'allowance' for the Deputy Chief Executive of £20,000 (cost to the council £26,460) which is consistent with recommendation 5, referred to above, as the Deputy Chief Executive was not intended to be a substantive post, but rather an additional responsibility given to another Executive Director.
- 5.6. I therefore conclude that resolution 3 as set out in this September 2017 Report cannot amount to authorisation to pay an international allowance of £40,000 per annum to the new Chief Executive (whomsoever that might be).
- 5.7. In November 2017, the County Council received a further report, directly from the then Leader of the Council which resolved to appoint Mrs Daljit Lally as Chief Executive and Head of Paid Service on a joint basis with Northumbria Healthcare NHS Foundation Trust. Council agreed that she should be appointed on the basis of remuneration as set out in that report, which referred to a salary of £190,000 per annum with 50% to be funded by the Trust. That report did not make any reference to the payment of an international allowance at all.
- 5.8. In her consultation responses the Chief Executive has suggested that a draft of her proposed contract of employment or similar, showing the international allowance, was circulated at the November 2017 Council meeting as a 'pink paper' item. That would, in my experience, have been an unusual approach, not

least because the terms of the resolution do not accord with the statement of terms and conditions that were eventually agreed, and the corresponding appointment to the NHCT had not been made at that stage. Democratic Services have confirmed that they have no record of that draft being circulated, and it is not referred to in the resolution or the minutes, whereas there is a minute relating to questions asked of the Leader in relation to remuneration, which was to the effect that the only remuneration being paid to the Chief Executive by NCC was the 0.5FTE salary set out in the report. For completeness, I note that this allowance was not referred to in the Council's pay policy statement in force at that time.

- 5.9. In January 2018, it appears that terms and conditions were agreed with the Chief Executive which resulted in her being employed on two separate, parallel, contracts: one with the NHCT and the other with County Council. This appears to have been governed by a Memorandum of Understanding between the Council and NHCT, signed by the then Leader of the Council and the Chief Executive of NHCT in January 2018. It would further appear that neither Council nor the Staff and Appointments Committee were ever advised of this variation to the arrangements for the Chief Executive's employment approved in the November 2017 Council resolution.
- 5.10. The November 2017 resolution of Council specifically delegated to the Staff and Appointments Committee responsibility for on-going review of the Chief Executive's remuneration. I have checked with Democratic Services and have been unable to identify any meetings, reports to, or resolutions of, the Staff and Appointments Committee at all between January 2017 and May 2018. This includes the period in which the restructure proposals and appointment process of the Chief Executive took place. The first record that has been identified of the Staff and Appointments Committee considering any aspect of the Chief Executive's pay and conditions of service was in August 2021.
- 5.11. In December 2017, the then Executive Director of HR and OD instructed the Council's payroll team that an additional allowance of £40,000 was to be paid to the Chief Executive with effect from 1 December 2017. Email correspondence between officers suggests that the Executive Director of HR and OD obtained confirmation from some source that the then Leader of the Council had approved payment of this allowance. However, there is no record of this approval, or the rationale for, or basis of the allowance being paid. Nor is there any record of Staff and Appointments Committee ever having been consulted about or informed of it.
- 5.12. From contemporaneous email correspondence between the then Executive Director of HR and OD and the payroll team it would appear that officers were under the impression that Mrs Lally was already being paid an international allowance by the Trust, at the time of her appointment as the Council's Chief Executive. There is no evidence to support this assertion. In fact, it would appear that Mrs Lally was in receipt of an allowance for acting as executive lead for the

Council in relation to the international business before the September 2017 report to Council. There is no reference to this in payroll records for the relevant period. Nor is it clear on what basis or by whom this allowance was originally authorised and paid.

- 5.13. On 18 January 2018, the then Executive Director of HR and OD wrote to Mrs Lally confirming the offer of the position of Chief Executive and attaching a Statement of Terms and Conditions which stated that her salary would be £135,000 per annum inclusive of a £40,000 international allowance. The Executive Director of HR and OD subsequently clarified via email correspondence in September 2018 that the £40,000 was in fact not part of the Chief Executive's base salary, but a separate allowance to be paid for an indefinite period. In May 2019, the Executive Director again confirmed in email correspondence that the allowance was non-contractual and did not form part of the Chief Executive's salary, stating that this was an ad-hoc allowance approved by the then Leader.
- 5.14. In February 2018, the then Leader reported to Council on progress in implementing changes to senior management arrangements. This report was silent on the contractual or remuneration arrangements for the Chief Executive (even though they were different to those approved by Council in November 2017). Specifically, it did not refer to the payment of the international allowance to the Chief Executive.
- 5.15. The Council's 2017/18 accounts (which were published in draft form in the summer of 2018), referred to an allowance being paid to the Deputy Chief Executive from April to May 2017, and to the [interim] Chief Executive from June to December 2017. It is described as being jointly funded by NCC and NHCT. However, the amount of the allowance is not disclosed, and in the event, that allowance was not jointly funded. In any event, publication (in whatever level of detail) after the event, does not alter the fact that the allowance was unapproved, and the expenditure was therefore unlawful. The 2018/19 accounts conflate the salary and allowances paid to the Chief Executive, and merely refer to the Chief Executive as an 0.5FTE post. The 2019/20 accounts report a separate allowance of £40,000 being paid, but without explanation of what it is, or why it was being paid.
- 5.16. In November 2018, the Chief Executive made a report to Staff and Appointments Committee on further management structure changes. Again, the report did not refer to the payment of an international allowance to the Chief Executive.
- 5.17. I am advised that in order to be lawful, any payments made to the Chief Executive need to fall within s 112 of the Local Government Act 1972, which allows an authority to appoint officers "on such reasonable terms and conditions, including conditions as to remuneration, as the appointing authority think fit." By virtue of s 112(2A), this power is subject to s 41 of the Localism Act, which in turn requires

any determination relating to the remuneration or other terms and conditions of a chief officer to be made in compliance with the authority's pay policy statement under s 38 of the Localism Act.

- 5.18. The international allowance represents a very substantial enhancement (almost 40%) to the Chief Executive's base NCC salary of £95,000. It should also be noted that at the time the allowance was agreed, a full time Director of International Projects and Systems Transformation had already been appointed to lead this area of activity. In the absence of any written record of the rationale or basis for the allowance, I have not been able to form a view about whether it was reasonable to pay any such allowance, within the meaning of s112, at the time.
- 5.19. However, the more fundamental issue highlighted in Leading Counsel's advice, is that the international allowance was not paid as a result of any decision taken by a properly authorised decision maker. Matters relating to the terms and conditions of officers are non-executive decisions under the Local Authorities (Functions and Responsibilities) (England) Regulations 2000 Schedule 1, Item I37. Neither the Executive Director of HR and OD, nor the Leader of the Council had the power to approve the allowance.
- 5.20. The payment of an international allowance in addition to the Chief Executive's base salary was not consistent with the Council's published pay policy statements over the relevant period for the reasons set out at paragraphs 5.21 to 5.25 below.
- 5.21. I am further advised that under s 38 of the Localism Act 2011, the Council (and this has to be the full council) is required to prepare a pay policy statement, and this must include its policies relating to "the level and elements of remuneration for each chief officer", and "increases and additions to remuneration for each chief officer". The effect of s 41 of the Localism Act, and s 112(2A) of the Local Government Act 1972, is that a chief officer's terms and conditions must be determined in compliance with the pay policy.
- 5.22. Although the Localism Act does not require actual numerical amounts to be determined as part of the policy, the pay policy statement should identify what elements a chief officer's remuneration will contain, and how those elements will be fixed. If an authority wants to make a payment to a chief officer of a kind for which the pay policy statement does not make provision, it can only validly do so by first amending the pay policy statement.
- 5.23. Furthermore, the Council's pay policy statements have at the relevant times provided for the full council to determine salary bands, and for senior staff to be appointed to a spot point within their salary range, with the possibility of incremental increase within the range as a result of performance review. The international allowance is not of that nature. Some paragraphs in the statement

do assume that chief officers may receive fees and allowances other than basic salary, but these references are in the context of the approved salary package on appointment, and clearly do not contemplate the post-appointment addition of further allowances.

- 5.24. The advice is that the evident purpose of the Localism Act provisions is that the full council should decide, and formally record in the published statement, what the “building blocks” of a chief officer’s remuneration should be, and how they should be set. There is no reference in the Council’s pay policy statements to anything in the nature of an international allowance, and certainly no provision addressing how and by whom the amount of any such allowance should be fixed.
- 5.25. Payments have in large part been reflected in the Council’s published financial statements. However, a mere statement in the policy that allowances “will be published”, relates to what happens after an allowance has been awarded and paid, and it does not provide any lawful basis for any decision to award or pay that allowance – or justify why it should be paid – even if a properly authorised decision taker had decided to do so.
- 5.26. In summary, it is my view, supported by the opinion of leading counsel, that in the absence of any evidence that the NIA allowance was approved by the full council (or even by the SAC), it must follow that there has never been a lawful decision properly taken by (or on behalf of) the Council to pay that allowance, and that the payment of it to date has accordingly amounted to unlawful expenditure.

6. Recommendations

- 6.1. Given that the Council does not appear to have suffered any financial loss and may have been a net beneficiary of international consultancy activities and the position has now been regularised by the establishment of NICL, I do not consider that it would be in the Council’s interests to seek to unwind the previous contractual arrangements. Nevertheless, the following actions are proposed to ensure that lessons are learned, controls strengthened so that the Council does not find itself in a similar situation in future and that the current position is regularised.

In relation to trading for a commercial purpose, the Cabinet is invited to agree the contents of this report and:

- 6.1.1. Agree that Audit Committee be requested to commission a full, independent investigation into the circumstances that gave rise to the unlawful trading activities.
- 6.1.2. Note that the Chief Finance Officer will revise finance and contract procedure rules to strengthen control and oversight of commercial

- trading activities and issue updated guidance on the requirements relating to trading accounts for such activities.
- 6.1.3. Note that the chief finance officer in consultation with the Monitoring Officer will undertake a review of the Council's commercial activities to ensure that they are taking place on a lawful basis and issue further formal guidance as appropriate.
- 6.1.4. Note that the Chief Finance Officer will commission further advice and consult the external auditor with regard to any disclosures and/or adjustments that may be required to the Council's statement of accounts for 2020/21 and prior years, in respect of income and expenditure relating to international consultancy contracts between 2018 and 2021, or as between the Council and the NHCT.
- 6.1.5. Note that the Chief Finance Officer will consider whether, and if so what, disclosures should be made to HMRC in relation to corporation tax or other liabilities.
- 6.2. With regard to the payment of the international allowance to the Chief Executive (and previously to the Deputy Chief Executive) from 2017, Council is invited to agree the contents of this report and:
- 6.2.1. Note that payment of the international allowance has been stopped from the date of this report as a result of the prohibition period provisions in the Local Government Finance Act.
- 6.2.2. Agree that payment of the International Allowance will remain suspended pending consideration of further legal advice with regard to potential recovery of unlawful payments and any related issues by the Staff and Appointments Committee and any recommendations arising being reported to County Council for consideration.
- 6.2.3. Note that legal and (if necessary) actuarial advice will be taken regarding any potential adjustment of pension contributions made to the Local Government Pension Scheme in relation to the International Allowance.
- 6.2.4. Note that the Chief Finance Officer will undertake further investigation to establish whether any other unlawful payments have been made to any officers or former officers, including severance payments, which may require further reports under S114 of the Local Government Finance Act 1988.
- 6.2.5. Instruct the Director of HR in consultation with the Chief Finance Officer and Monitoring Officer to review the Council's pay policy statement to ensure that it is up to date and complies with the requirements of s38 of the Localism Act 2011 and report any required changes to the County Council.

7. Next Steps & Timescales

- 7.1. Subject to Cabinet approval, the Deputy Chief Executive will draw up terms of reference for an independent investigation into the circumstances that gave rise to unlawful trading activity. These will be presented to the Audit Committee for approval at its July meeting.
- 7.2. The Chief Finance Officer will draft amendments to finance and control procedure rules to strengthen control and oversight of commercial trading activities and prepared updated guidance on the requirement for and form of trading accounts, for approval by Council.
- 7.3. Advice is being commissioned on any disclosures or amendments to the financial statements for 2020/21 and prior years and their recommendations will be shared with the external auditor in due course.
- 7.4. Payroll have been instructed to cease payment of the international allowance to the Chief Executive with immediate effect.
- 7.5. A further legal opinion regarding restitution has been requested from Nigel Giffin QC and will be reported to the Staff and Appointments Committee for detailed consideration.
- 7.6. Advice regarding the status of contributions made to the LGPS based on the international allowance will be commissioned and Tyne and Wear Pension Fund officers have been alerted to the issue.
- 7.7. Internal audit has been requested to investigate a small number of other potentially unlawful payments to officers and to review all exit packages with a value of £100k or more over the last 2 years.
- 7.8. The Head of HR is reviewing the pay policy statement in consultation with the Chief Finance Officer and Monitoring Officer to ensure that it complies with the requirements of the Localism Act and any amendments will be submitted to the July meeting of Council.



Jan Willis

Executive Director of Finance (Interim) and S151 Officer

23rd May 2022