

Local Government and Regeneration Committee

Written Evidence - Inquiry into Arms Length External Organisations (ALEOs)

1. Introduction

The Local Government and Regeneration Committee (the Committee) are undertaking a brief inquiry into the governance arrangements for ALEOs. The Committee has put out a call for written evidence asking specific questions, as well as seeking any general comments on ALEOs.

The Scottish Charity Regulator (OSCR) is established under the Charities and Trustee Investment (Scotland) Act 2005 ('the 2005 Act') as a Non-Ministerial Department (NMD) forming part of the Scottish Administration. OSCR is the registrar and regulator of over 23,700 charities in Scotland, a small number¹ of which we have identified as Arms Length External Organisations (ALEOs).

Our evidence is informed by a recent review we conducted into [charitable ALEOs](#) - the report was published in January 2015. It also follows on from the information provided previously to the Committee in May 2015 on the [Codes of Conduct which apply to persons sitting on ALEOs](#).

In this written evidence we outline:

- The legislative requirements on charitable ALEOs under the 2005 Act.
- How and what concerns can be raised with OSCR about charitable ALEOs and the action that can be taken.
- A summary of the key findings from our review of charitable ALEOs, including good practice recommendations.

2. Evidence

2.1 Legislative requirements

ALEOs can be registered as charities if they pass the charity test set out in the 2005 Act. To do so they must have only charitable purposes and provide public benefit in furtherance of these purposes.

A recent OSCR review exercise identified 64 ALEOs registered as charities in Scotland, with a combined income in 2013 of over £550 million. The majority operate

¹ OSCR Report Arms Length External Organisations identified 64 registered charities as ALEO's.

leisure and culture services, but they are also used to undertake activities such as community safety, employability and regeneration.

All bodies which are registered as charities must comply with the 2005 Act. This sets out requirements for charities and also for charity trustees.

Charity trustees are the people in overall control and management of a charity. They are responsible for the charity's governance and strategy and making sure that the charity is administered effectively. The charity trustees of a charitable ALEO will generally be the people who sit on its board; this includes both councillor and non councillor board members. Charity trustees are subject to the statutory charity trustee duties (set out in section 66 of the 2005 Act). A charity trustee must:

- 1 Act in the interests of the charity and in particular:-
 - Ensure the charity acts in a manner which is consistent with its purposes.
 - Act with the care and diligence that it is reasonable to expect of a person who is managing the affairs of another person and
 - In circumstances of conflict of interest between the charity and any person responsible for the appointment of the charity trustee, put the interests of the charity before those of the other person.
- 2 Ensure that the charity complies with the provisions of the 2005 Act.

In support of these duties, OSCR has published [Charity Trustee guidance](#) setting out their duties and responsibilities in more detail.

2.2 Raising concerns about ALEOs

Members of the public can raise directly with OSCR concerns about charitable ALEOs. Concerns raised will be reviewed in line with [our Inquiry Policy](#). In general, we only deal with serious concerns that relate to charity law or governance, for example where charity trustees have breached their duties or where there is serious or sustained misconduct by those in management and control of a charity. Where we find misconduct or mismanagement we can take action including suspending charity trustees, directing them not to take certain actions or petitioning the Court of Session to exercise the powers given it by the 2005 Act.

OSCR has previously received concerns about charitable ALEOs and, following on from these, has conducted inquiries. Specifically we undertook inquiries and published reports into Glasgow East Regeneration Agency and Shetland Charitable Trust.

Broadly, the key issues which arose in these inquiries were in respect of charity governance. Within Shetland Charitable Trust there was no clear distinction between the running of the charity and the usual local authority business. Within GERA there was a lack of independent thought and decision making allowing decisions to be made

to the detriment of the charity resulting in significant charitable funds being lost. A number of recommendations to the trustees of each charity were made following these inquiries and lessons identified about the constitutional models for charitable ALEOs (for further details see the [ALEO study](#)).

2.3 Charitable ALEOs Review

Following on from these concerns and wider interest from the sector about these bodies we conducted a detailed review into charitable ALEOs in late 2014. This review included detailed analysis of 11 of the 64 charitable ALEOs identified. The review examined a number of issues including having the local authority as sole member, the balance between councillor and independent trustees, funding arrangements and the dependence on local authorities, all covered in detail within the [final report](#). We covered two areas in particular which may be of interest to the Committee: motives for setting up ALEOs and conflict of interest and this is detailed further below.

2.3.1 Motives for setting up ALEOs

We identified a number of reasons why local authorities set up ALEOs:

- Rates relief - Where a charity occupies premises for charitable purposes they are entitled to claim a mandatory 80% rates relief and the local authority can choose to top this up with a further 20% discretionary rates relief. Rates are collected by the local authority and then paid over to central government. Where a body is charitable and does not pay rates, this shortfall is financed by central government and, consequently, the local authority makes a saving on rates relief.
- User benefits – The leisure and culture ALEOs we spoke to considered there to be clear benefits for service users from delivering services through ALEOs. Services which had previously been part of a wider department were now more focused and this led to improved response to user needs and opportunities for innovation. They also felt that the ability to recruit specialists to ALEO boards also led to improved understanding of user needs and service delivery.
- Funding - Some ALEOs did access other routes of funding which they may not have accessed within the local authority. This funding was for specific projects and allowed ALEOs to undertake services which would not have been possible as departments of the local authority itself.

One further point made by stakeholders was in respect of procurement. We were informed that where the local authority is the sole member of the charity this may allow the local authority to take advantage of the exception in EU procurement law known as

the 'Teckal exception'. If the relationship between the authority and the ALEO can be shown to be sufficiently close the authority may be able to avoid conducting a competitive tendering exercise for provision of the services in question. Some of the charitable ALEOs also considered that there were benefits to them from this exception, in that their contracts are more stable and they can therefore ensure a continuity of service to their beneficiaries.

2.3.2 Conflicts of interest

Charity trustees must act in the interest of the charity and they must put the interest of their charity before their own or those of any other person or organisation. During our study of charitable ALEOs we looked at how councillor trustees in particular coped with this duty, reviewing the actions that councillors had taken at meetings and also conflict of interest policies and registers of interest.

We found that councillor trustees did not generally withdraw from discussions where the general relationship or business with the local authority was discussed. We noted that the relationship is unavoidably close and it would not be practical for councillors to remove themselves from all discussions pertaining to business with the local authority.

However the report does advise there are situations where councillors must withdraw in order to exercise their charity trustee duties appropriately. These would be situations where it was clearly not possible for councillors to put their duties towards the charity before those of the local authority. Our report notes an example where the trustees of a charitable ALEO were discussing whether or not to accept the local authority as a sole member, and the councillor trustees acted appropriately in removing themselves from the discussion.

2.3.3 Overall conclusion

Overall we were satisfied that charitable ALEOs are operating satisfactorily, within their unique environment, but we made six recommendations for them to consider (see Annex A), reflecting examples of good practice we had found. We will continue to monitor ALEOs in line with our Targeted Regulation programme.

4. Conclusion

I hope the Committee finds this helpful evidence to inform its inquiry into ALEOs. If you have any further questions about this evidence please contact Nicola McBain, Engagement Manager (Policy & Partnerships) at nicola.mcbain@oscr.org.uk.

Annex A – Recommendations from ALEO Review

- **Memorandum of Understanding** – We accept that the sole member structure may be preferable to both bodies due to procurement legislation and also to ensure that, ultimately, statutory services are protected. However, this power should only be exercised in exceptional circumstances and a memorandum of understanding would set out these circumstances more clearly.
- **Robust induction procedures** – Councillor trustees may change regularly due to the election process. Charitable ALEOs should ensure that their induction processes are robust to manage this change effectively and ensure that new trustees fully understand their duties.
- **Councillor trustees selected by skills set** - Trustee boards should contain an appropriate mix of skills. While independent trustees were appointed on the basis of their skills, the selection process for Councillor trustees was less robust. Charities should consider how the Councillor trustees are selected, and consider applying skills matrix equally to these trustees.
- **Regular reviews** – Many of the ALEOs we met with were changing or expanding services. They should ensure that these services fit with their purposes or, where necessary, seek our consent to amend their purposes. As the ALEO develops they must ensure that the ALEO board and its objects continues to be fit for purpose.
- **Separation from the local authority** – Where Councillors sit on scrutiny or finance committees within the local authority, we would recommend that these are not the same committees which deal with the ALEO they act on. Where there is a cross-over, the effectiveness of scrutiny would be diminished.
- **Sub committees** – We have seen sub-committees being used successfully within many of the ALEOs. These tend to be headed by independent trustees, allowing for a greater assurance of independent operation. We would recommend that if the size of the charity and the board allows, sub-committees should be utilised.