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WALES **AUDIT** OFFICE
SWYDDFA **ARCHWILIO** CYMRU

Senior Officers' Pay and Pensions **Carmarthenshire County Council** Report in the Public Interest

Senior Officers' Pay and Pensions

This report in the public interest has been prepared in accordance with section 22 of the Public Audit (Wales) Act 2004.

No responsibility is accepted in relation to any officer, member or any other person in their individual capacity or any third party.

The Wales Audit Office team that assisted me in preparing this report comprised Richard Harries and Geraint Norman.

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This report is issued in the public interest under section 22 of the Public Audit (Wales) Act 2004. I have issued this report to draw the public's attention to a decision of Carmarthenshire County Council (the Council) that, in my view, was unlawful. The Council cannot use its powers to set reasonable remuneration for the avoidance or mitigation of the effect of pensions legislation. There were also failings in governance arrangements and inadequacies in the processes to determine the pay of senior officers which also render the decision unlawful.

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Summary

- 1** This report is issued in the public interest under section 22 of the Public Audit (Wales) Act 2004 (the 2004 Act). The 2004 Act requires me to consider whether, in the public interest, I should make a report on any matter which comes to my notice in the course of the audit, in order for it to be considered by the audited body or to be brought to the attention of the public.
- 2** I have issued this report to draw the public's attention to a decision of Carmarthenshire County Council (the Council) that, in my view, was unlawful. The Council cannot use its powers to set reasonable remuneration for the avoidance or mitigation of the effect of pensions legislation. There were also failings in governance arrangements and inadequacies in the processes to determine the pay of senior officers which also render the decision unlawful. I believe it is important that the public has a full and proper awareness of the events concerning the Council. I also consider it appropriate to give the Council an opportunity to explain the important steps it has taken to improve its governance arrangements and to ensure that the risk of such failures recurring is reduced.
- 3** In September 2012, I became aware that the Council's Chief Executive had decided to opt out of the Local Government Pension Scheme (LGPS) and take advantage of a decision made by the Council's Executive Board in November 2011. This decision agreed that 'in lieu of its contractual obligation to pay an annual employer's contribution, that a pay supplement be payable, at no additional cost to the Council'. Given the unusual nature of this decision, I informed the Council that I would review this as part of my annual audit of the 2012-13 accounts.
- 4** I have concluded that the decision by the Executive Board on 14 November 2011 to approve a 'pay supplement' for senior staff who opt out of the LGPS was unlawful. Any payment made pursuant to that decision would give rise to an item of account which is 'contrary to law'. I have concluded that the decision taken by the Executive Board is unlawful for the following reasons:

 - a** the decision was 'ultra vires' and cannot lawfully be implemented as the Council's powers to set reasonable remuneration cannot be used for the avoidance or mitigation of the effects of pensions legislation;
 - b** in making the decision, relevant considerations were not taken into account, in breach of *Wednesbury* reasonableness principles;
 - c** the Council failed to have due regard to the public sector equality duty;
 - d** the decision constituted indirect discrimination;
 - e** the agenda item was considered by the Executive Board without appearing on the agenda and without being open to inspection by members of the public; and

- f** the report was drafted and presented by a senior officer who had a disqualifying personal and pecuniary interest in the decision as he was eligible to benefit from the proposed 'pay supplement'.
- 5** In the 2012-13 financial year, the Council paid £16,353 to the Chief Executive under the 'pay supplement' scheme. A further £12,397 has been paid to the Chief Executive under the scheme in the 2013-14 financial year (up to 31 December 2013).
- 6** I have shared my legal advice with the Council. It has obtained its own legal advice in response but has declined to provide that advice to me, stating that the 'written advice is not suitable for disclosure and privilege is not waived'. In September 2013, the Council provided me with a paper which sets out its position on each of the issues raised. The Council does not accept that 'the pay supplement is intrinsically unlawful'.
- 7** On 4 December 2013 the Council's Executive Board rescinded the decision to offer a 'pay supplement' in lieu of pension contributions. The Executive Board considered the legal opinions of both the Wales Audit Office and the Council's own legal advisors. The Executive Board did not accept that the principle of the policy was intrinsically unlawful but it did accept that there may have been shortcomings in the procedures by which it had been adopted. The Executive Board, not wishing to incur further unnecessary expenditure in this matter, therefore unanimously resolved:
- a** without conceding that it is intrinsically unlawful, that the pay supplement policy be withdrawn on procedural grounds; and
- b** that any employment issues arising as a consequence of the decision be addressed by the Assistant Chief Executive (People Management and Performance).
- 8** The Council have informed me that from January 2014 no further payments under the 'pay supplement' policy will be made to the Chief Executive.
- 9** In its response the Council puts forward the view that these are not matters for the auditor. As the appointed auditor it is my responsibility to decide whether it appears to me that any item of account is 'contrary to law' before exercising discretion on whether to apply to the court for a declaration to that effect – see section 32(1) of the Public Audit (Wales) Act 2004 and my functions under section 22 and 33 of the 2004 Act.
- 10** The expression 'contrary to law' may be traced back at least to section 247(7) of the Public Health Act 1875. The decided cases since that date have clearly illustrated the grounds upon which items of account may be held contrary to law. It is best summed up in *Hazell v. Hammersmith and Fulham London Borough Council* [1990] 2 QB 697. "In short, an auditor is entitled to seek relief if he can show that an item of account is for any reason unlawful or improper".

Recommendation

Future decision making

Since the Council has rescinded the decision I make only one recommendation.

- R1** If the Council decides to take a new, lawful decision it must address the procedural weaknesses identified in this report and ensure that it demonstrates proper exercise of discretion in setting 'reasonable remuneration'.

Background

- 11** Legislation was introduced in the Finance Act 2011 to restrict pensions tax relief for individuals by reducing the 'annual allowance' from £255,000 to £50,000 in 2011-12 and the 'lifetime allowance' from £1.8 million to £1.5 million with effect from the tax year 2012-13. The lifetime allowance has been further reduced to £1.25 million with effect from 2014-15.
- 12** For employees in a 'defined benefits' scheme, such as the Local Government Pension Scheme (LGPS), a tax liability is incurred if the increase in the value of an individual's pension benefits is greater than the annual allowance. For pension savings in excess of the lifetime allowance, additional tax liabilities are incurred, usually when an individual first receives their pension. A lifetime allowance of £1.5 million is estimated to be equivalent to a pension of approximately £75,000 per annum.
- 13** In light of these changes, on 14 November 2011, the Executive Board of the Council approved a 'pay supplement' to be paid to any senior staff affected by the new tax provisions who opt out of the LGPS. The payment of the 'pay supplement' was agreed on the basis of 'no additional cost to the Council' (in effect, in lieu of employer's pension contributions).
- 14** That decision was made after receiving a report from independent consultants, Total Rewards Project Ltd (TRP), and was taken in order to allow senior staff to make alternative arrangements for saving for retirement to mitigate any impact of the restrictions on pensions tax relief introduced by the Finance Act 2011. The item of business constituted by the report did not appear on the published agenda for the meeting but was considered on the basis that the chairperson of the meeting was of the opinion that the item should be considered at that meeting as a matter of urgency 'as action was required to be taken prior to the next meeting of the Executive Board on 28 November 2011'. The report presented to the Executive Board was exempt from publication and was considered in closed session.
- 15** The TRP report was submitted to the Executive Board under cover of a report from the Assistant Chief Executive (People Management and Performance) who presented his report to the Executive Board. The Assistant Chief Executive's report recommended the Executive Board approve the recommendations in the TRP report. As a senior officer, the Assistant Chief Executive had a personal and pecuniary interest in the recommendation to pay a 'pay supplement' to senior officers who opt out of the LGPS. The report of the Assistant Chief Executive stated that there were no equalities, legal or staffing implications. Neither report identified the impact on any individual senior officers of the restrictions on pensions tax relief enacted in the Finance Act 2011.

- 16 The recommendations of TRP and the Assistant Chief Executive were adopted by the Executive Board at its meeting on 14 November 2011. The publicly available minute relating to that agenda item states that 'The Executive Board was apprised of the recommendations set out in the biennial report that the current pay freeze in relation to senior officers be extended in the light of the current pressure on public finances. Members also noted the impact of changes in the HMRC rules.' The decision was recorded in that minute as being that the Executive Board 'unanimously resolved that the recommendations set out in the report be agreed'. Publicly available information does not identify what those recommendations were, what the substance of the decision was or that a 'pay supplement' (albeit cost-neutral) was to be available to senior officers. In my opinion, the decision-making process was neither open nor transparent.
- 17 The option of opting out of the LGPS and receiving a 'pay supplement' has not been approved for, or offered to, other Council officers.

The decision taken by the Executive Board to allow senior officers to opt out of the Local Government Pension Scheme and to receive a 'pay supplement' equivalent of the employer's pension contribution is unlawful and payments made as a result of that decision result in an item of account that is 'contrary to law'

The decision taken by the Executive Board is 'ultra vires' and cannot lawfully be implemented as the Council's powers to set reasonable remuneration cannot be used for the avoidance or mitigation of the effects of pensions legislation

- 18** It is commonly known and accepted (trite law) that a local authority may only do that which it is required or empowered by statute to do. Such powers as a local authority have may only be exercised reasonably and for a proper purpose. A local authority must direct itself properly in law and must act in accordance with administrative law principles.
- 19** The Council is under a duty, imposed by section 112(1)(2) of the Local Government Act 1972 (the 1972 Act), to employ officers on such reasonable terms and conditions, including as to remuneration, as the Council sees fit.
- 20** The duty imposed by section 112 of the 1972 Act must be exercised reasonably and for the purpose for which it was given, ie to determine a reasonable level of remuneration for work to be carried out – remuneration must be the reasonable pecuniary equivalent of the service rendered.
- 21** As is the case with all statutory powers, the power to determine a reasonable level of remuneration must be exercised for the purpose for which it was given. An individual is entitled so to order his/her affairs as to avoid or minimise (but not evade) the effect on him/her of legislation. The powers of public authorities are, however, essentially different from those of a private person. Statutory power conferred for public purposes can validly be used only in the right and proper way which Parliament, when conferring it, is presumed to have intended. Avoidance/mitigation of the effect of statutory controls is not a proper purpose for which a local authority may act.
- 22** It would not be a proper exercise of the Council's power to determine a reasonable level of remuneration if the remuneration were determined for an extraneous or legally irrelevant purpose such as the avoidance or mitigation of the effect of restrictions in pensions legislation.
- 23** The decision by the Executive Board to pay a 'pay supplement' to senior staff who decide to opt out of the LGPS scheme was made to mitigate any impact on those officers of the restrictions on pensions tax relief introduced by the Finance Act 2011.
- 24** In my view, Parliament did not intend that the impact of the restrictions on pensions tax relief introduced by the Finance Act 2011 should be avoided and/or mitigated by the exercise

of the power, conferred on the Council by Parliament, to determine reasonable remuneration. Avoidance/mitigation of the effect of legislation is not a proper purpose for which a local authority may act. For that fundamental reason the decision taken by the Executive Board on 14 November 2011 is ultra vires and cannot lawfully be implemented.

- 25** The Executive Board decision is also ultra vires for the further reason that the Executive Board misdirected itself in law. Members of the Executive Board were wrongly informed and proceeded on the basis that, in consequence of the changes introduced in the Finance Act 2011, officers would be 'forced to leave the LGPS'. In addition, members of the Executive Board were wrongly informed and proceeded on the basis that the effect of the Finance Act 2011 was that 'total contributions to approved pension schemes are subject to the limit of a lifetime allowance', whereas it is the tax relief on the annual allowance and the lifetime allowance which is restricted.
- 26** The Council argues that there are many authorities bearing on the validity and propriety of local authority decisions to enter into particular financial arrangements with employees. It refers to a distinction between cases where a legitimate and rational bargain is entered into for genuine employment reasons and arrangements for the improper purpose of conferring a gratuitous or irrationally generous benefit on the employee concerned. It is the Council's view that the 'pay supplement' falls on the lawful side of the dividing line identified in the authorities.
- 27** I consider that the Council's response has not addressed the fundamental issue of lawful reasonable remuneration. My view remains that the Council's powers to set reasonable remuneration cannot be used for the avoidance or mitigation of the effect

of pensions legislation. This is a public law concern identified by the auditor as to the improper exercise of power which is different from the private law position referred to by the Council.

In making the decision, relevant considerations were not taken into account, in breach of *Wednesbury* reasonableness principles

- 28** Such powers as the Council has must be exercised reasonably taking into account all relevant consideration and leaving out of account irrelevant considerations: see *Associated Provincial Picture Houses v Wednesbury Corporation [1948] 1KB 223*.
- 29** The decision of the Executive Board is ultra vires for the additional reason that relevant considerations were not taken into account, in breach of *Wednesbury* principles:
- a** No information was presented to the Executive Board on the impact of the provisions in the Finance Act 2011 on any member of staff for whom a 'pay supplement' was approved.
 - b** One of the Council's arguments for the 'pay supplement' was to improve the recruitment and/or retention of senior staff. However, no evidence was provided to demonstrate that a failure to approve the 'pay supplement' would have adverse consequences for the Council in terms of the recruitment and/or retention of senior staff.
 - c** No information was provided to the Executive Board on the equalities or legal implications of the proposal to approve a pay supplement.

- 30** In my view, the report to the Executive Board does not provide a reasonable basis for the decision made.
- 31** The Council argues that the decision was reasonable. The Council suggests that although the report was not detailed, it was not misleading and members were not misled. The Council suggests that members were 'well aware of the impact of the changes to taxation of pension savings and were not misled'.
- 32** I have considered the Council's response but my view is that the report and minutes of the meeting do not provide a justification to support the decision made and the report does not provide a reasonable basis for the decision made. In its response, the Council has not provided any evidence to substantiate any detrimental effect on staff recruitment and retention.
- 35** As set out previously, the report of the Assistant Chief Executive to the Executive Board indicated that there were no equalities issues to consider. No assessment was made of the likely impact of the proposal under consideration on the three aims of the general duty to which the Council was under a statutory duty to have due regard. No such assessment was reported to the Executive Board, notwithstanding that the proposal under consideration (the opportunity to opt out of the LGPS and receive additional remuneration) was intended to be available to senior staff only (potentially disproportionately benefiting male employees and/or older employers and discriminating against women and/or younger employees).
- 36** The Council was therefore in breach of the public sector equality duty in failing to carry out and report to the Executive Board an assessment of the likely impact of the proposal on its ability to comply with that duty. In my opinion, the Council did not have due regard to the public sector equality duty.

The Council failed to have due regard to the public sector equality duty

- 33** Section 149 of the Equality Act 2010 (the 2010 Act) places a general duty on the Council to have due regard to three aims: the need to eliminate discrimination, the need to advance equality of opportunity and the need to foster good relations.
- 34** Specific duties are placed on the Council by the Equality Act 2010 (Statutory Duties (Wales) Regulations 2011 (the 2011 Regulations). Regulation 8 provides that the Council must make 'such arrangements as it considers appropriate for: (a) assessing the likely impact of its proposed policies and practices on its ability to comply with the general duty...'.
37 The Council refers to the discipline of the public sector equality duty lying in the quality, not the outcome, of the decision-making process. The Council argues that it is not the traditional role of an auditor to enforce discrimination law.
- 38** In considering the Council's response, my view is that the quality of the decision-making process was poor for the reasons set out above. Furthermore, the Council's response does not address my view that the Council was in breach of the public sector equality duty in failing to carry out and to report to the Executive Board an assessment of the likely impact of the proposal on its ability to comply with that duty. The Council therefore failed to have due regard to the public sector equality duty.

The decision constituted indirect discrimination

- 39 By section 39(2) of the 2010 Act, the Council as an employer must not discriminate against an employee (a) as to his/her terms of employment; or (b) in the way that the Council affords an employee or employees access or by not affording him/her access to a 'benefit, facility or service'.
- 40 The decision of the Executive Board to approve a 'pay supplement' to senior staff who opt out of the LGPS, constituted indirect discrimination (as defined by section 19 of the 2010 Act). Pursuant to section 19 of the 2010 Act, discrimination takes place if a provision, criterion or practice puts a group who share a protected characteristic at a particular disadvantage. Age and sex are protected characteristics. Both younger employees and women employees are put at a disadvantage as they are treated less favourably than older employees and male employees, in that younger employees and/or women employees are less likely to be eligible to benefit from the approved 'pay supplement'. Avoidance/mitigation of the impact of the restrictions on pensions tax relief is not a legitimate aim on which the Council might rely in order to negate a finding of indirect discrimination.
- 41 The decision of the Executive Board to approve a 'pay supplement' to senior staff who opt out of the LGPS constituted indirect discrimination (as defined by section 19 of the 2010 Act). Although it may be thought that employees in that group would be better off remaining in the LGPS, that does not provide an answer to an allegation of indirect discrimination.

- 42 The Council points out that discrimination is a statutory tort, enforceable by an individual who may (normally within three months of the act complained of) bring a complaint that they have been discriminated against. It is also the Council's view that it is not for the auditor to assert claims not made by any individual.
- 43 My view remains that the decision to approve a 'pay supplement' to senior staff who opt out of the LGPS constituted indirect discrimination and accordingly the 'pay supplement' was contrary to law.

The agenda item was considered by the Executive Board without appearing on the agenda and without being open to inspection by members of the public

- 44 Regulation 5(4) of the Local Authorities (Executive Arrangements) (Decisions, Documents and Meetings) (Wales) Regulations 2001 as substituted by regulation 2(2) of the Local Authorities (Executive Arrangements) (Decisions, Documents and Meetings) (Wales) (Amendment) Regulations 2002 requires 'an item of business may not be considered at a meeting unless:
- a A copy of the agenda including the item (or a copy of the item) is open to inspection by members of the public in pursuance of paragraph (1):
 - (i) for at least three clear days before the meeting; or
 - (ii) where the meeting is convened at a shorter notice, from the time the meeting is convened; or by reason of special circumstances, which shall be specified in the minutes,

the chairperson of the meeting is of the opinion that the item should be considered at the meeting as a 'matter of urgency'.

The Council is of the view that use of the urgency procedure 'does not matter here and should not alone lead a court to condemn an item of account as unlawful'.

- 45** The item of business constituted by the TRP and Assistant Chief Executive reports did not appear on the agenda for the Executive Board meeting held on 14 November 2011 nor was a copy of the agenda item open to inspection by members of the public. According to the minutes of that meeting, that item was nevertheless considered on the basis that the Chairperson of the meeting was of the opinion that the item should be considered at that meeting 'as action was required to be taken prior to the next meeting of the Board on 28 November 2011'. However, the minutes of the Executive Board meeting held on 14 November 2011 do not identify any action which purportedly was required to be taken prior to the next meeting of the board on 28 November 2011, only 14 days later.
- 46** Accordingly, the decision of the Chairperson to consider the said item of business without that item appearing on the agenda and without being open to inspection by members of the public, did not comply with regulation 5(4) of the 2001 Regulations and, in any event, had no reasonable basis, all the more so as the 'urgent' decision was not implemented until April 2012. Therefore, in my view, the decision taken by the Executive Board on 14 November 2011 on that item of business is unlawful on that ground.
- 47** The Council states that the Assistant Chief Executive had an 'unusually heavy workload' at the time of the report and decision. The Council is of the view that the matter was treated as an urgent item not because of the report but because of the Assistant Chief Executive's workload and future availability.
- 48** I have considered the Council's response and remain of the view that as the agenda item was wrongly treated as an urgent item and was wrongly not made available for inspection by members of the public, the decision taken by the Executive Board to offer a 'pay supplement' was unlawful on this further ground.
- 49** A person is disqualified from participation in a local authority decision-making process if there is a real possibility that he or she would be influenced by a pecuniary or personal interest in the outcome of the decision. Disqualification from participation applies to an officer providing written or oral advice to a decision-making committee or board.
- 50** Any pecuniary or personal interest has to be declared and an individual having such an interest is not entitled to participate in the decision-making process unless that interest is too remote or insignificant to matter. In general, the participation in a decision-making process of a single individual with a disqualifying interest will vitiate the decision arrived at (see the *Kirkstall Valley* case and *R v Hendon RDC ex parte Chorley* [1933] 2 KB 696).

The report was drafted and presented by a senior officer who had a disqualifying personal and pecuniary interest in the decision as he was eligible to benefit from the proposed 'pay supplement'

- 51 The decision of the Executive Board is also unlawful because the Assistant Chief Executive, who drafted and presented the covering report to the Executive Board, had a disqualifying personal and pecuniary interest in the decision as a senior officer who was eligible to benefit from the proposed 'pay supplement'.
- 52 The Council refers to section 117(1) of the 1972 Act, which requires officers to disclose in writing any direct or indirect pecuniary interest in a proposed local authority contract, other than contracts to which the officer is himself/herself a party. The Council argues that this provision does not apply – the contracts affected by the 'pay supplement' proposals were employment contracts to which the interested officers were parties.
- 53 I do not accept the argument made by the Council. The decision-making process is wider than the decision itself and includes the presence of officers at a meeting. A person is disqualified from participation in a decision-making process if there is a real possibility that he or she would be influenced by a pecuniary or personal interest in the outcome of the decision (see *R v Secretary of State for the Environment ex parte Kirkstall Valley Campaign Ltd* [1996] 3 All ER 304; *Porter v Magill* [2002] 2 AC 357).
- 54 I am satisfied that an officer took part in the decision-making process whilst having a disqualifying financial interest in the outcome of the decision thereby rendering the decision unlawful.

Next steps

- 55** The Council is now required by section 25 of the 2004 Act to consider this report at a full meeting of the Council within one month of the date of this report. At the meeting, the Council must decide:
- a** whether the report requires it to take any action;
 - b** whether the recommendation in the report is to be accepted; and
 - c** what action to take in response to the report and recommendation.

Acknowledgements

- 56** I wish to express my appreciation to officers and members of the Council for their co-operation during the audit.



Anthony Barrett

Appointed Auditor
30 January 2014