

# By mutual agreement

Severance payments to  
council chief executives

Local government report  
March 2010



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# Summary and recommendations

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## Executive summary

### **Three in every ten departing council chief executives receive compensation for the early termination of their contract.**

- Over the 33-month study period,<sup>i</sup> there were 37 cases where chief executives received payments following the mutually-agreed termination of their contract.
- These cases account for nearly one-third of all chief executive departures from councils in this period.<sup>ii</sup>
- One in nine councils paid a chief executive to leave. Among single tier and county councils (STCCs), the rate was one in seven councils.
- It appears the incidence of mutually-agreed departures with payments has grown in STCCs in recent years.

### **Rapid re-employment in local government is unusual.**

- In six of the 37 cases, a chief executive took up a senior management post at another council within 12 months.
- In 31 cases (over 80 per cent) the chief executive has not yet returned to employment in local government.

### **Costs of severance payments for councils are high; there can also be indirect costs and reputational damage.**

- Severance payments from mutually-agreed terminations had a direct cost to councils of £9.5 million in the study period.<sup>iii</sup>
- Within this, the cost of paying unreduced pensions was £3.8 million (40 per cent).
- The average cost of payments to councils was 1.8 times the chief executive's annual basic salary. In four cases, it was more than three times the basic salary.
- Costs from recruiting a new chief executive were also incurred, as well as disruption during the vacancy period.
- Councils can suffer reputational damage from making severance payments, especially when a former chief executive rapidly takes up employment at another council.

<sup>i</sup> The study covered the period January 2007 to September 2009. This time span covers the period from the introduction of new severance regulations at the end of 2006, through to the start of the research in October 2009.

<sup>ii</sup> This excludes all departures from councils involved in the 2009 local government reorganisation. These councils are not included in the analysis in this report.

<sup>iii</sup> Not all of this sum is directly paid to chief executives as it includes payments made by councils to meet the strain on pension funds. Chief executives also pay income tax on settlements over £30,000.

### **Agreeing a severance to secure a contract termination is attractive to councils, whatever the underlying problem.**

- The most common cause of a mutually-agreed severance payment is a breakdown in the relationship between chief executives and senior members; in many cases these are the result of deep-seated issues.
- However, severance payments are also made to secure contract terminations where there is simply a personality clash or a new administration wishes to replace a chief executive associated with a previous leadership.
- Actual or perceived poor performance by chief executives has led directly to mutually-agreed severance payments. Poor performance can also lead to relationship breakdowns with senior members.
- Weak performance management arrangements mean that where there are genuine performance concerns councils often lack evidence to mount a case for dismissal.
- One in seven payments were made in cases where there had been alleged misconduct by chief executives.
- To enable them to operate as officers of the whole council, chief executives have enhanced statutory protection, in addition to the usual employment rights, but the associated processes are expensive and time-consuming.

### **Some councils manage arrangements for severance payments poorly.**

- No severance payments in this period were found to be unlawful by auditors. However, in 18 per cent of cases, auditors reported formally to councils concerns about the way councils' have dealt with terminations and payments.
- The quality of advice and information provided to members is often not good enough for sound decisions to be made.
- Members sometimes agree a payment without having considered the full range of options and the costs of each.
- Occasionally, the actions of members give chief executives grounds for claiming unfair dismissal, thereby creating a potential liability for the council.

### **Making a severance payment may be in the best interests of councils and the taxpayer, but the formal processes are not working well.**

- A severance payment is often less burdensome for a council than the damage inflicted by dysfunctional relationships, or the costs and disruption of formal disciplinary action.
- The special statutory employment protection fails to provide job security where members seek to remove chief executives for personal or political reasons. It also acts as a disincentive to dismissal in performance and conduct cases.
- This means that some competent chief executives lose their jobs unnecessarily, while a smaller number of less effective ones are paid-off rather than dismissed.
- These failings increase the number of unnecessary exits, the frequency of severance payments and the cost to the taxpayer.

## Recommendations

### The government should:

- increase the transparency of early contract terminations and severance payments for chief executives by requiring that:
  - any proposal for a severance package is reviewed by a cross-party committee, such as a remuneration committee, before a final decision is made; and
  - councils publish the details of each package within a short, set time period following the payment.
- require councils to have a formal appraisal process for chief executives; and
- review the statutory employment protection mechanisms for chief executives,<sup>i</sup> considering whether the current system should be reformed or replaced.

### Councils should:

- take steps to address relationship problems at an early stage. Mediation should be used more widely and should take place when problems start, rather than as a last resort;
- improve decision-making. There are aspects of local decision making that should be routine but are often not present, or not of a sufficient standard. Councils should ensure that:
  - costed option appraisals are available to members; and
  - robust cases are made for the award of discretionary sums, and that members do not treat them as automatic.
- formally adopt and implement the national model of performance appraisal as set out in the Joint Negotiating Committee's (JNC)<sup>ii</sup> conditions of service for chief executives (Ref 1), recognising the model may require development;
- consider the implications for severance payments when agreeing the basic salary of a chief executive; wage restraint will reduce the cost of severance payments to councils;
- avoid using severance payments as a reward for poor performance or misconduct;
- consider whether to include clauses in chief executives' contracts that specify termination arrangements and the nature of any payment; and
- ensure that, during the negotiation of mutual agreement cases, members do not give grounds for claims for unfair dismissal. Councils should provide awareness training for senior members on relevant aspects of employment law.

<sup>i</sup> This will also have implications for section 151 officers and monitoring officers.

<sup>ii</sup> This is the national negotiating body for pay and conditions of service for chief executives in local government. More information is provided in para 33.

**The Local Government Association Group<sup>i</sup> should:**

- examine options open to councils to recoup elements of severance payments where an individual is rapidly re-employed in local government, and provide advice to councils on affected employees, the elements that are recoverable and how pension arrangements would be affected;
- discuss with the government whether changes to the statutory framework are required to enable recovery of elements of severance payments;
- consult with councils and bodies such as Chartered Institute of Public Finance Accountants (CIPFA) and the Association of Local Authority Chief Executives (ALACE) to assess whether the performance appraisal model for chief executives set out in the JNC conditions of service (Ref 1) is sufficient or whether amendments are required;
- improve advice and guidance to members and officers on the technical and legal aspects of contract terminations and severance negotiations for chief executives, including option appraisals;
- provide training and guidance for members on performance managing chief executives and handling contract termination negotiations; and
- work with bodies such as ALACE to improve public understanding of the responsibilities of chief executives and the challenges they face.

**The Audit Commission will:**

- review its guidance to auditors in relation to severance arrangements and payments for council chief executives in the light of any changes to the regulations or to the arrangements for statutory protection.

<sup>i</sup> LGA Group includes the Local Government Association, Local Government Employers, the Improvement and Development Agency and the Leadership Centre for Local Government.

# Introduction

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## Background

**Senior pay in the public sector has been a focus of media attention and public concern. This has included severance payments – compensation received by employees for early termination of their contracts. High-profile cases of council chief executives receiving large pay-offs have raised questions about whether taxpayers’ interests are being protected.**

**1** In September 2009, the Secretary of State for Communities and Local Government asked the Audit Commission to investigate severance payments to council chief executives. The request identified two specific areas of concern:

**‘That public money is being used to fund pay-offs to chief executives for reasons of convenience, rather than in the best interests of the taxpayer’; and**

**‘How best to protect the taxpayer in connection with pay-offs for chief executives where they are subsequently re-employed by another authority’.**

**2** These are important issues involving the use of public money. But they raise wider issues relating to the management of relationships and performance at senior levels in local government. These involve competing public interests, and have significant implications for running major public services efficiently and effectively.

**3** This report examines severance arrangements for council chief executives in this wider context.

## Severance payments for council chief executives

**4** Severance payments are often used at senior management level in both the public and private sectors. When dismissal is not appropriate, such payments make it possible to change the leadership of an organisation. This may be needed when a new strategic direction is required, or when a change in governance arrangements means that the leadership role has changed.

**5** Even when dismissal is a possibility, for example on grounds of poor performance or misconduct, severance payments can contribute to the replacement of a chief executive without risk of the reputational damage and cost to an organisation that can come from exposure at an employment tribunal.

**6** Severance payments in public bodies cause dilemmas that do not apply to private firms; but the unique characteristics of councils create even more. This is particularly so in relation to arrangements for chief executives. There are a number of challenges.

- **When is a severance payment in the public interest?** Reducing the number and size of severance payments may appear to be in the best interests of taxpayers, but quick, agreed departures can save public money. Dysfunctional relationships, or drawn-out legal disputes at the top of organisations, can have substantial negative effects on services. So, councils are permitted to agree payments on contract terminations as being in the 'efficiency of the service'.
- **What is the right level of a payment?** Councils have the discretion to reach settlements that they consider suitable, provided they are reasonable and within the scope of their powers. However, councils also face other competing demands for their resources. Large, albeit lawful, payments can undermine public trust and damage councils' reputations.
- **Does the special statutory protection for chief executives also protect taxpayers?** Council chief executives have a degree of additional statutory employment protection to allow them to work effectively in a political environment (Refs 2, 3). Chief executives serve the council as a whole, so must be independent of the political leadership. They need to feel they can challenge, or report on, the actions of senior members without fear of dismissal. This protection benefits chief executives, and potentially helps councils work effectively. This will also benefit taxpayers. But there are aspects that are less to taxpayers' advantage. There are concerns that the procedures in place to secure statutory protection are expensive and encourage councils to negotiate settlements, rather than initiate action that could lead to dismissal on the grounds of poor performance, or misconduct. The disciplinary mechanisms may also drive up the size of settlements where they are awarded.
- **Does the performance management of chief executives by members affect severance payments?** Chief executives are directly accountable to elected members for their performance, but cannot be subject to the same performance management processes as other employees. This is similar to private firms where a chief executive will be accountable to the chair and board. But elected members may have little experience of holding senior executives to account. If a council has an ineffective accountability process, then its negotiating position will be weak if a chief executive's performance is inadequate.
- **Does local discretion protect taxpayers' interests?** Councils have discretion over chief executive employment decisions and, within

authorised limits,<sup>i</sup> the value of any severance payment. Governance arrangements for agreeing each severance are also determined by each council. However, discretion gives rise to variations in approach. Some councils will manage these processes well, but some may simply get them wrong.

**7** Overall, these issues mean that the frequency and size of severance payments provide only a partial view when considering whether they provide value for public money.

**8** The following chapters examine patterns of council chief executive severance payments in the light of these dilemmas. They aim to explain the drivers underlying the payments, rather than simply to comment on their size.

## Methodology

**9** The research underpinning the report is drawn from a number of sources (see Appendix 3 for a full methodology):

- A public consultation exercise conducted in September 2009. Appointed auditors were also consulted.
- A data collection exercise by auditors on all chief executive moves that occurred in the study period (January 2007 to September 2009).<sup>ii</sup>
- Interviews with stakeholder organisations.

**10** The backgrounds to severance payments are complex and their causes are often contested by the parties involved. Auditors are independent of councils and have provided information to us on these issues.

## This report

**11** The report is in six further sections:

- **The system for severance payments** – sets out the arrangements for chief executive severance payments.
- **The number of severance payments** – provides a quantitative analysis on the number of council chief executive severances and cases of rapid re-employment.
- **Cost to councils of severance payments** – presents financial data on severance packages and their make up.
- **Causes of terminations with severance payments** – examines the factors underlying mutually-agreed cases and the extent to which these take account of the interests of taxpayers.
- **Management of terminations with severance payments** – explores local oversight and governance arrangements for chief executive severances.
- **Conclusions.**

**i** There are limits on the value of certain discretionary payments councils can make to chief executives (see para. 19)

**ii** Data was also collected on severances resulting from the 2009 local government reorganisation. However, all councils subject to reorganisation have been excluded from the current analysis.

# The system for severance payments

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**Arrangements for severance payments for council chief executives differ from those for other employees in a number of important ways. This chapter sets out the arrangements for all employees in England, before discussing the arrangements for local government staff. It then considers the specific arrangements for council chief executives and concludes with a comparison between local government and the NHS.**

## **Severance in England<sup>i</sup>**

**12** This section applies to all employees in England. There are special arrangements for severance payments in place for council chief executives, but their system is based on that in place for the wider workforce.

### **What are severance payments?**

**13** Financial compensation is often paid when a contract of employment is terminated early. These payments are referred to as ‘severance payments’ – a broad term covering all types of termination and redundancy payments made to employees.

### **When are severance payments made?**

**14** Contracts can only be terminated lawfully in a set number of circumstances:

- retirement (including ill-health);
- resignation by the employee;
- redundancy;
- dismissal by the employer in compliance with employment law; or
- mutual agreement between the employer and employee.

**15** Compensation on termination is rarely paid where there is a voluntary resignation or lawful dismissal, so severance payments are most common on redundancy or by mutual agreement.<sup>ii</sup>

<sup>i</sup> The same general employment laws also apply in Wales.

<sup>ii</sup> Payments are made on the early termination of contracts due to early retirement, but these are not viewed as relevant for the purposes of this research.

**16** Mutual agreements may be made when an employer wishes to terminate a contract, but is unable to do so by dismissal or redundancy. In these cases, a compromise agreement will often be made between the employer and employee. This agreement is likely to include compensation for loss of employment. It is likely that the employee will agree not to pursue any legal claims and there may well be confidentiality clauses. In the private sector there may also be clauses constraining future business activities.

**17** Where payments are made, the level of payment is usually at the employer's discretion.

## Severance payments in local government

**18** The section applies to all local government employees.

### Discretionary enhancements in local government

**19** The compensation that a council can offer an employee for early termination of contract is set out in regulations (Refs 4, 5). Where employees are made redundant, or have their contracts terminated in the interests of the efficient running of the authority, a council can choose either to:

- pay a lump sum of up to 104 weeks pay; or
- increase an employee's membership of the local government pension scheme by up to ten years.

**20** Councils can also award an additional pension of not more than £5,000 per annum alongside either a lump sum, or an increase in pension years.

**21** Efficiency of the service cases are those where it is in the interests of the efficient running of the council to terminate the contract – for instance, if the council requires a change in direction and it is considered that the incumbent chief executive is not the person to lead the change.

**22** A severance package may also include payments to counter any legal claims; agreement over any pay in lieu of notice (PILON); funding for any training to help an employee find further employment; agreements over leased equipment such as computers or cars; and details about confidentiality terms.

**23** The pension regulations also provide for unreduced pensions<sup>i</sup> to be paid to employees over the age of 55 where the termination is on the grounds of redundancy or business efficiency. There are different arrangements for ill-health terminations.

**i** When pensions are awarded early, they are usually reduced in amount to reflect the fact that they will be paid over a longer time period and will, therefore, place a greater strain on the pension fund. Where a pension is paid early, but is not reduced in amount, the strain on the pension fund has to be met by the employer.

## Arrangements for council chief executives

### The role of chief executive

**24** Chief executives have wide-ranging responsibilities within councils including leading management teams and ensuring effective delivery of council services and programmes (see Appendix 4 for full list).

**25** In recent years their activities have had a higher profile and have become more complicated. *Tougher at the Top?* (Ref 6) identified four key aspects to this.

- Effective political and managerial leadership by councils and government are seen as increasingly important components in creating high-performing local authorities.
- A new, more facilitative style of leadership is required to deliver local government's leadership role.
- The increase in external assessment means that local authority performance can be compared with previous years and with other authorities.
- There have been changes in the scope and complexity of the role of chief executives.

**26** Overall, the role of chief executive has become increasingly important as a driver of improvement, more dependent on the quality of relationship between the political leader and the chief executive, and subject to greater levels of scrutiny and accountability.

**27** Council chief executives have also had to face this new environment while managing a complex relationship with elected members. This is not a challenge shared by other public bodies such as the NHS.

**28** Chief executives are appointed by the full council and are directly accountable to members. They serve the council as a whole, not just the ruling administration. Dismissal of a chief executive is the responsibility of politicians.

**29** This creates a series of challenges for chief executives. They are required to engage in a close working relationship with, yet remain independent from, the political leaders. This has the potential to bring them into conflict with the leadership, particularly in the context of the new environment set out above, as their duty is to the council as a whole.

## Employment protection for chief executives

**30** To reflect the specific challenge of working in a political environment faced by chief executives, they have additional statutory protection to ensure they cannot be removed from office without good reason (Refs 2, 3). This protection allows them to challenge, or report on, the actions of senior members without fear of dismissal. The same protection is provided to section 151<sup>i</sup> officers and monitoring<sup>ii</sup> officers.

**31** This protection is normally secured through a two-stage process. The first requires a council to carry out a preliminary investigation to consider whether there is sufficient evidence to appoint an independent person to investigate alleged misconduct.

**32** The second stage, where it takes place, involves an independent investigation conducted by a Designated Independent Person (DIP).<sup>iii</sup> Both the chief executive and the council must agree on the independent person; in default, the DIP is appointed by the Secretary of State. DIPs are required to carry out a full investigation and collect a range of information, data and evidence to help make their recommendations, which can range from no action to dismissal. The council is prohibited from dismissing or taking other disciplinary action unless recommended by the DIP.

**33** This process is set out in the conditions of service for chief executives produced by the joint negotiating committee (JNC) for local authority chief executives (Ref 1). This is the national negotiating body for pay and conditions of service for chief executives in local government. The JNC includes Joint Secretaries from both the employer and employee sides; elected members nominated by the Local Government Association (LGA); and chief executives nominated by the Association of Local Authority Chief Executives (ALACE). The conditions of service also include guidance on performance appraisal, conciliation and salary frameworks.

- i** This is a statutory position – the responsible financial officer. This is usually the treasurer or chief financial officer.
- ii** The monitoring officer is a statutory position. They are responsible for advising the council on the legality of its decisions and on the conduct of members.
- iii** This protection was first given to chief executives in 1993 and later extended to cover section 151 officers and monitoring officers in 2001. Regulations were the same in England and Wales, but in 2006 new Standing Orders were introduced in Wales. These included introduction of an investigation committee and specified timescales in which the report and recommendations have to be made by the DIP.

**34** Some aspects of the processes laid out in the JNC conditions of service are statutory, others are best practice. Many local authorities use the conditions of service as the basis for determining chief executives' terms and conditions. However, as with all of the national agreements for staff in local government, the conditions of service are not compulsory, and local authorities are free to negotiate and develop their own local agreements.

**35** Individual councils are responsible for determining the salary of their chief executive. However, the Joint Secretaries agree annual cost of living increases. They also provide a national guidance framework to support salary reviews. This contains minimum and maximum salaries from other councils to provide reference points and also sets out factors for consideration in any review (Ref 1).

## **Management of severance payments by councils**

**36** Authorities are required by regulation to publish policies on early terminations and discretionary payments (Ref 4). Policies and governance arrangements vary between councils but, in general, decisions are made by a human resources (HR) sub-committee or an equivalent.

**37** Councils, and council members, should have due regard for legal processes and the council's policies on severance, discretionary benefits and early retirement. They are expected to seek specialist HR and legal advice.

**38** It is the responsibility of councils to put in place proper arrangements to secure value for money and to ensure proper stewardship and governance. Councils therefore have a duty to consider fully the financial implications of any severance package, including any pension costs the authority might have to cover. Non-monetary considerations, such as damage to the authority's reputation or the difficulty of recruiting a replacement, should be taken into account.

**39** Councils' procedures for ensuring compliance with legal requirements, including in relation to severance arrangements, must be fair, reasonable, and compatible with employees' rights. Councils must take into account all, and only, relevant factors. This means that decisions must be based on appropriate and sufficient information.

**40** Within local government, there is a new requirement<sup>i</sup> for authorities to publish in their statements of accounts the individual financial details of any severance payments to all senior officers earning over £50,000. Those

<sup>i</sup> This is contained in an amendment to the 2003 Accounts and Audits Regulations that comes fully into effect on 1 April 2010.

earning over £150,000 are to be identified by name, with all others by post title. These provisions form part of a wider requirement to publish all aspects of remuneration of senior officers, such as salaries and bonuses, and come into effect fully on 1 April 2010.

## Severance payments in local government compared with other sectors

- 41** The NHS and the civil service provide some useful comparisons to policies applied in local government.<sup>i</sup> For example:
- Each NHS body is required to seek approval for proposed severance payments from its strategic health authority.<sup>ii</sup>
  - The NHS recently introduced policies to restrict notice periods to no more than six months. This helps to reduce payment in lieu of notice (PILON) - one of the most significant costs of severance in NHS bodies – and reflects recent efforts by the NHS to reduce the scale of payments.<sup>iii</sup>
  - NHS bodies are required to include in severance agreements provision to allow part of a termination payment to be recovered if the chief executive is employed by another NHS body within a certain time.<sup>iv</sup>
- 42** Within the civil service there is a similar clawback mechanism that can be used when an employee finds new employment in the civil service within 28 days of receiving a severance.
- 43** An element of most severance payments in both the civil service and the NHS is to offset future loss of earnings, and where this does not occur it is appropriate that public money is recovered. Clawback mechanisms are not used in local government, however. But councils do have pensions abatement regulations in these instances (see Figure 1).

- i** No data on the number or scale of severance packages is available for any of these sectors or the private sector. It is possible that the rate of mutually-agreed severances may be lower in the civil service and NHS relative to councils as senior managers can be moved ‘sideways’ within the same national organisations.
- ii** In some cases proposed severance payments may then be referred to the Department for Health, or where proposed payments are very high or there is a high public profile, to a Health Minister.
- iii** Previously chief executives of NHS bodies often had long notice periods – sometimes up to 12 months. The bulk of NHS severance payments is often made up in PILON. In contrast, council chief executives have much shorter notice periods, and severances are composed largely of discretionary lump sums or pension increases.
- iv** This occurs where officers are re-employed by any NHS body before the expiry date of their fixed term contracts or contractual notice periods.

**44** Confidentiality clauses are widely used in compromise agreements across all sectors. While they are not legally prohibited, the NHS discourages their use.

Figure 1: **Comparison of severance arrangements between local government and NHS bodies**

	<b>Local Government</b>	<b>Health</b>
<b>Relevant regulations / directions</b>	<p>The Local Government (Early Termination of Employment) (Discretionary Compensation) (England and Wales) Regulations 2006</p> <p>Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007</p>	<p>Health Service Circular 2004/01</p> <p>NHS Pensions Regulations 1995</p> <p>NHS (Compensation for Premature Retirement) Regulations 2002</p> <p>NHS Finance Manual</p>
<b>Oversight Processes</b>	<p>Council sets policy</p> <p>Responsibility lies with HR sub-committee or other similar body</p> <p>Decisions on dismissals of chief executives will go to full council</p>	<p>NHS bodies have to seek approval from the Strategic Health Authority (SHA) and possibly the DoH, Treasury or in very large or high profile cases, a health minister.</p>
<b>Clawback</b>	<p>No clawback mechanism provided in the regulations for non-pension elements of severance payments. Clawback provisions for discretionary added years of pension have gone. However, the administering authority must have a public statement of policy on pension abatement where an individual returns to local government employment.</p>	<p>NHS bodies are able to recover part of the termination payment for senior managers if they secure employment within the NHS and within their notice period.</p>
<b>Confidentiality clauses</b>	<p>From 1 April 2010, severance details to be published for all senior managers earning over £50,000. Managers receiving severances and earning over £150,000 will also be named.</p>	<p>Generally prohibited</p> <p>NHS bodies also publish remuneration reports with their annual financial statements. These disclose compensation for loss of office.</p>

# The number of severance payments

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**This chapter provides an analysis of the number of severance payments for council chief executives in the period from January 2007 to September 2009. It also examines the incidence of rapid re-employment within local government.**

## **The number of mutually-agreed severance payments**

### **Relevant departures**

**45** For the purposes of this research, we have defined severance payments as any payment made in compensation for early termination of a contract of employment, excluding payments made as a result of requests for early retirement. Using this definition, there were 75 severance payments made to council chief executives in the study period.

**46** However, we have focused specifically on those cases where public money has been used to compensate chief executives by mutual agreement. Just over half of the total number of severance payments were awarded on grounds of redundancy, largely resulting from the 2009 local government reorganisation (LGR) (see Appendix 5).<sup>i</sup>

**47** This leaves just under half the cases where the contract has been terminated early by mutual agreement, other than due to early retirement requests from the chief executive. These cases are mutually-agreed severances that fall within the remit of the research.

### **Council chief executives often leave with a severance payment**

**48** In the study period, over a third of councils saw a chief executive depart for any reason. There were 122 departures in total, excluding LGR cases.

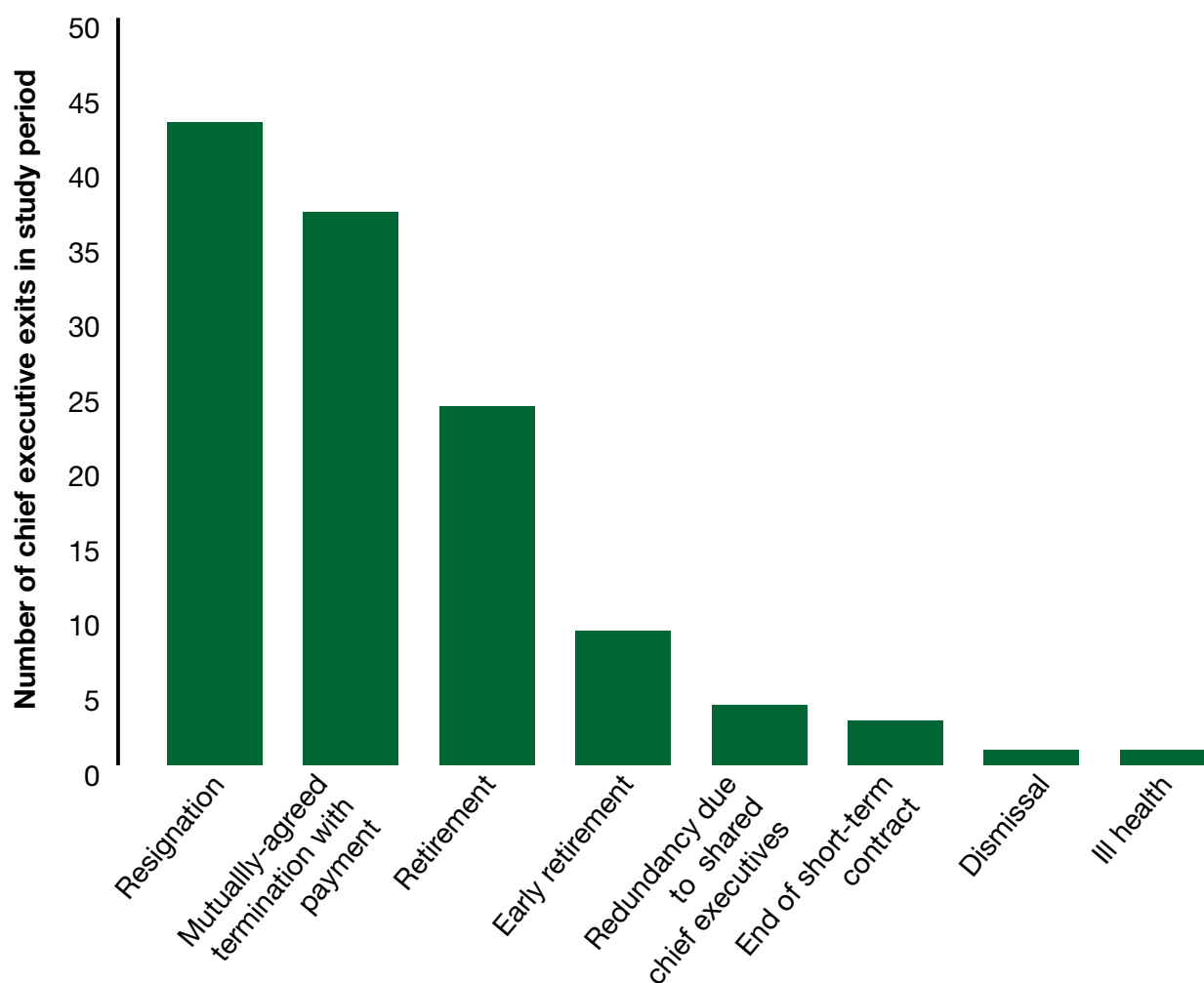
**49** Of these, 37 were mutually-agreed contract terminations with severance payments – accounting for 30 per cent of all departures in the period (see Figure 2). Only resignations were more common (35 per cent of departures). Almost all resignation cases were career moves and the chief executive went directly to a new post elsewhere.

**50** This means that, in the 33 months covered by the study, 11 per cent of councils paid their chief executives to leave. No council paid more than one mutually-agreed severance in the study period.

**i** All exits due to the 2009 LGR are excluded. All councils involved in the LGR are excluded from all analysis in this report including the base for the total number of councils used in any calculations. The one exit due to death has also been excluded from the analysis.

Figure 2: **Chief executive exits by type**

Nearly a third of all departures by chief executives are by mutual agreement with a payment.



(Source: Auditor data) (Base: 122 departures in the study period)

**51** Limited public reporting of severance payments means that, before this report, it was difficult to gauge their full extent. For instance, the Local Government Association Group (LGA Group), in its submission to the consultation for this research, conducted an analysis of press coverage of chief executive exits since 2007. Based on this evidence, it found that only 16 per cent of exits were likely to have been on the grounds of mutual agreement with a payment.<sup>i</sup> This is about half the actual rate, reflecting the under-reporting in the press of this type of exit.

### **Mutually-agreed severance payments are most common in single-tier and county councils**

**52** The pattern of chief executive departures was markedly different between single-tier and county councils (STCCs) and district councils (DCs). The rate of chief executive exits of all types was higher in STCCs (44 per cent) compared to DCs (28 per cent). Figure 3 shows that these differences were driven by higher rates of both resignations and mutually agreed contract terminations among STCCs.

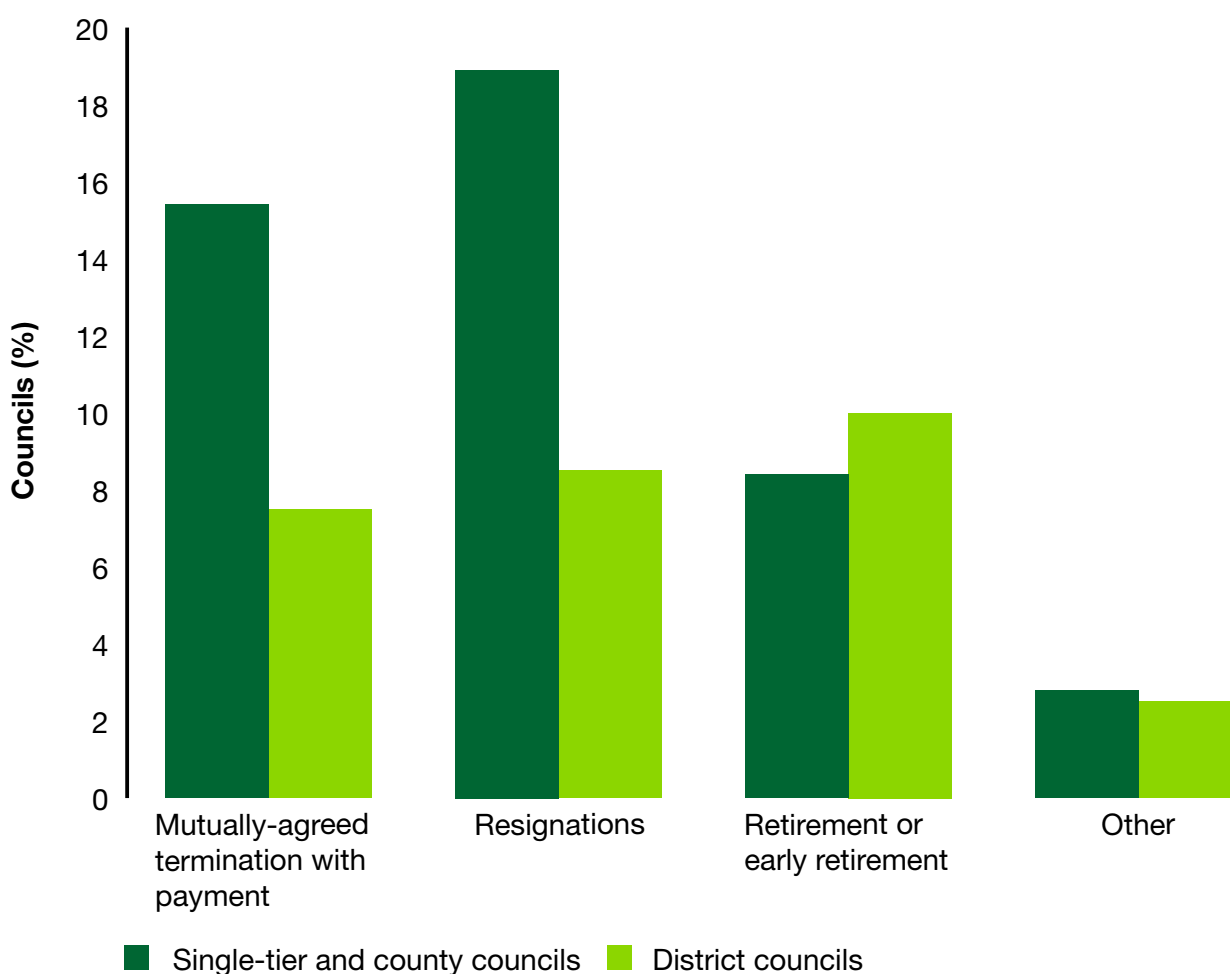
<sup>i</sup> Excluding LGR cases

**53** The higher rate of resignations reflects the tendency for STCCs to recruit chief executives from other similar councils (Ref 6). STCC chief executives are also in demand for posts in other public sector bodies. There appears to be less demand of this type for DC chief executives and the resignation rate is correspondingly much lower.<sup>i</sup> It is also likely that the 2009 local government reorganisation suppressed movements across the DC sector over the study period.

**54** The factors underlying the higher rates of mutually-agreed terminations with severances in STCCs are less clear.

Figure 3: **Councils experiencing different types of chief executive departures<sup>ii</sup>**

Mutually agreed severance payments are more frequent in single tier county councils than district councils.



(Source: Auditor data) (Base: 65 STCC departures from 143 councils and 57 DC departures from 201 councils in the study period)

- <sup>i</sup> Twenty four STCC chief executives out of 143 resigned in the study period to take up a post either as a chief executive at another council or to work for another public body. Only 15 DC chief executives out of 201 resigned to work in senior management at another council or for another public body. There were three other resignations amongst STCCs and two for DCs.
- <sup>ii</sup> The ‘other’ category includes exits due to shared chief executives, ill health, dismissals and the expiry of short-term contracts.

## **The number of mutually-agreed severance payments in STCCs has probably increased**

**55** There is no data on rates of severance payments before 2007. However, for STCCs, it is possible to make an assessment of trends in severance payments by looking at wider trends in contract terminations amongst chief executives.

**56** Excluding resignations to take up employment elsewhere, comparison between the current research period and earlier ones<sup>i</sup> shows that there were:

- 27 departures in STCCs in the three year period 2000 to 2002;
- 26 between 2003 and 2005; but
- 38 chief executive exits in the 33 months covered by this report.<sup>ii</sup>

Twenty two (58 per cent) of these were mutually-agreed departures with severance payments.

**57** This analysis shows that the current number of mutually-agreed departures with payments is similar to that of all non-resignation moves five years ago, a group that also includes all forms of retirement. This strongly suggests that the rate of payments has increased in STCCs over the last decade.

**58** Growth in the number of mutually-agreed terminations with severance payments in recent years in STCCs may well be a consequence of steps taken by government to put pressure on councils to improve their performance. *Tougher at the Top?* (Ref 6) demonstrated a statistical link between council performance as measured by comprehensive performance assessment (CPA) and departures by chief executives.

**59** While comparative data is not available, the picture is likely to be different for DCs. Chief executive turnover dropped from an annual rate of 13 per cent in 2005-2007, to 10 per cent in the study period.<sup>iii</sup> This fall in the total number of exits makes an increase in the number of severance payments unlikely.

### **No gender dimension to mutually-agreed severance payments**

**60** Figure 4 shows that the incidence of female chief executives departing with a mutually-agreed severance payment was similar to that for men. Even accounting for the different total number of women chief executives

- i** See Appendix 3 for data sources and definitions.
- ii** The current study period covers 33 months. To make them comparable, there would have been 40 exits in a full 36 months period with 23 mutually agreed. If mutually-agreed severances payments occurred in the earlier three year periods at the same rate as in the current research, there would have been 16 in each. Figures for the earlier periods are based on 150 STCCs, while only 143 are included in the current study. Adjusting for this would further increase the number of 'modelled' mutually-agreed exits in the study period.
- iii** The figures given are percentages that account for the reduction in the number of DCs in this period due to LGR. The fall in turnover may be related to the disruption across the wider DC labour market caused by the 2009 LGR.

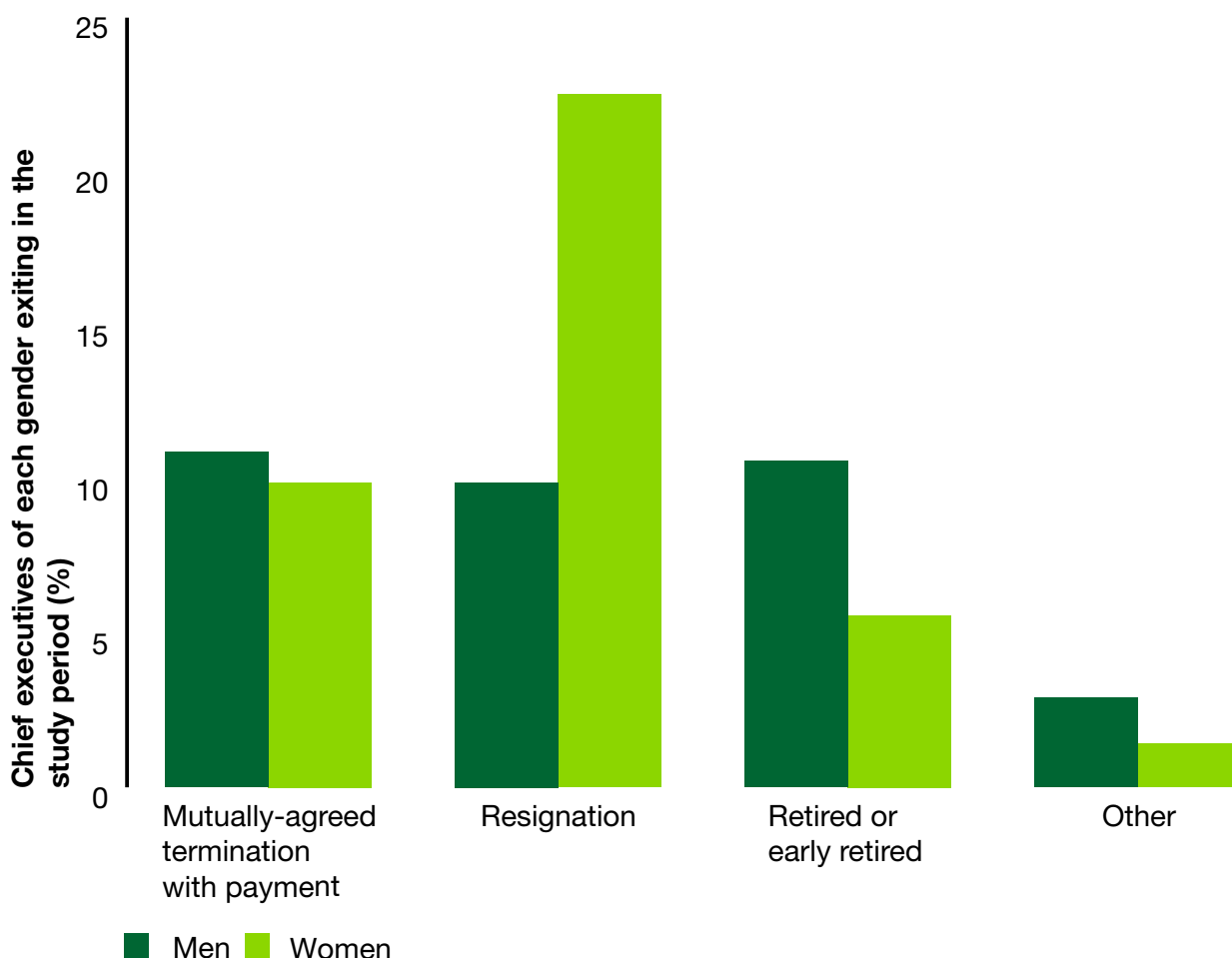
compared with men, there is no statistical evidence that gender plays a role in the incidence of payments.

**61** Gender is a factor in other exits, however.

- Retirements without payment are more common among men, reflecting the fact that many female chief executives have only recently taken up their posts.
- Women are much more likely to resign.<sup>i</sup> This is being driven by women taking up employment outside local government. In the study period, 13 per cent of all female chief executives in post in January 2007 resigned to work outside local government. For male chief executives, the figure was less than 2 per cent. The reasons for such a marked difference are not clear.

Figure 4: **Share of male and female chief executives leaving for different reasons (%)**<sup>ii</sup>

Gender is not a factor in mutually agreed severance payments, but it is in resignations.



(Source: Auditor data) (Base: 94 male chief executives departed out of 273 in January 2007 and 28 female chief executives left out of 71)

- <sup>i</sup> The differences in resignation rates by gender are statistically significant at the 99 per cent level (Pearson Chi-square Asymp. Sig=0.005). They are not simply a function of the smaller number of female chief executives.
- <sup>ii</sup> The 'other' category includes exits due to shared chief executives, ill health, dismissals and the expiry of short-term contracts.

## Patterns of rapid re-employment

**62** Relatively few chief executives receive a mutually-agreed severance payment and then rapidly take up employment at another public sector body:<sup>i</sup>

- Of the 37 chief executives who left by mutual agreement, six had been employed in another council within 12 months.
- The research did not identify any chief executive who departed by mutual agreement and took up an executive post within 12 months at a public body other than a council.

**63** The great majority of chief executives (82 per cent) that left by mutual agreement were not employed in the public sector 12 months after their departure.

**64** In the minority of cases where departing chief executives were re-employed in local government, most took up their new posts between six and nine months after their departure.

**65** This research has not tracked the career paths of former chief executives other than those that re-entered local government, but, where evidence was available, consultancy work and non-executive posts seem the most common options.

<sup>i</sup> See Appendix 3 for full definitions and methodology.

# Cost to councils of severance payments

## This chapter provides an analysis of the cost of severance payments to councils. It also examines the component elements of severance packages.

**66** All figures relate to the cost to councils of the payments. These are often greater than the actual cash sums paid to the chief executives, as councils often make payments direct to the pension fund, reflecting the increased pension the executive will receive.

### The cost of mutually-agreed severance payments

#### Total cost

**67** The total cost to councils of mutually-agreed severance payments in the study period was approximately £9.5 million<sup>i</sup> (see Figure 5). The bulk of this (72 per cent) was paid by STCCs. This was partly due to the higher rate of mutually-agreed cases in these councils and partly to the higher basic salaries of their chief executives.

**68** This difference may also be driven by the fact that basic salaries for STCC chief executives have increased rapidly in recent years while growth for DC chief executives has been less marked (Ref 6).

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#### Figure 5: Cost to councils of mutually-agreed severance payments in study period

Severance payments in STCCs account for nearly three-quarters of the total cost to councils.

	Total cost	Average cost to councils per severance
STCCs	£6,801,674	£309,167
DCs	£2,674,182	£178,279
<b>All councils</b>	<b>£9,475,856</b>	<b>£256,104</b>

(Source: Auditor data) (Base: 21 STCC and 15 DC mutually agreed severances)

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<sup>i</sup> This figure includes all components of severance costs, including the actuarial strain on pension funds. Not all aspects of these are payable immediately by councils. Councils have five years to make good the actuarial strain of unreduced pensions. Financial data was available for only 36 of the 37 cases.

**69** The direct cost of the severance payment is only part of the full picture. In addition, these cases also have a range of other tangible and intangible impacts including:

- the recruitment costs of a new chief executive – frequently at a higher salary (Ref 6);<sup>i</sup>
- disruption to the council during the vacancy period;
- the costs of recruiting to other senior management posts, should the new chief executive be appointed from this pool; and
- possible consequent exits by one or more senior managers.

**70** With the exception of this last example, where other senior staff may leave when there have been relationship breakdowns at the top resulting in the departure of the chief executive, these costs are not specific to severance cases and relate to all types of chief executive exits. Nonetheless, they are costs that should be taken into account when considering whether to terminate a chief executive's contract.

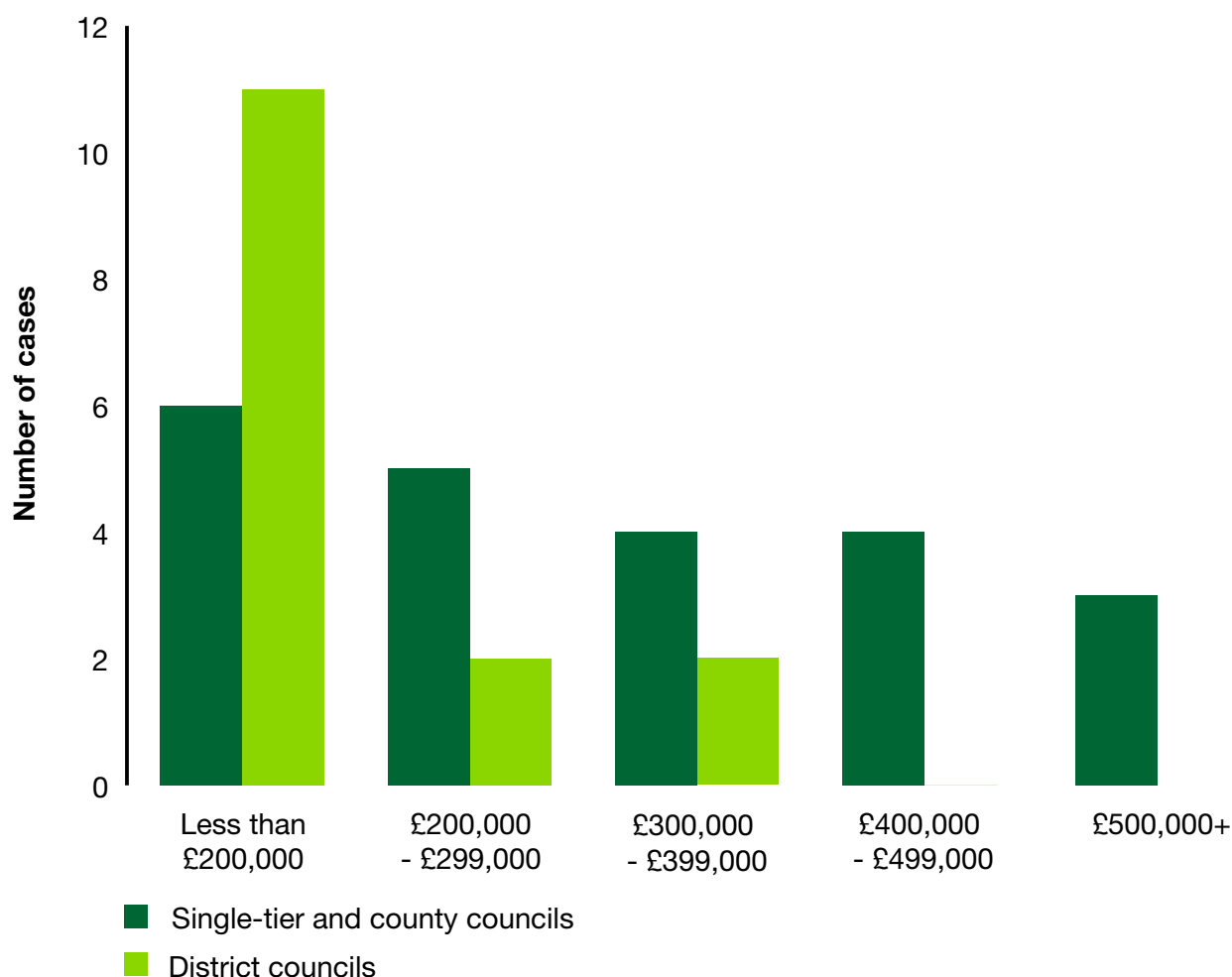
### **Individual packages**

**71** Figure 6 shows the direct cost to councils of individual packages including, unreduced pension costs in absolute terms. Overall, there were 13 packages (34 per cent) that cost councils over £300,000 each. Three of these were over £500,000.

<sup>i</sup> *Tougher at the top?* (Ref 6) showed that in the period 2003 to 2006 councils that retained their chief executive saw an average increase in basic salaries of 28 per cent. Councils that had replaced their chief executive with a candidate promoted either internally or externally saw a 35 per cent increase, and councils that replaced their chief executive with chief executive from another council saw a 42 per cent increase.

Figure 6: **Cost to councils of mutually-agreed severance packages**

Thirteen severance packages cost councils over £300,000 each



(Source: Auditor data) (Base: 21 STCC and 15 DC mutually-agreed severances)

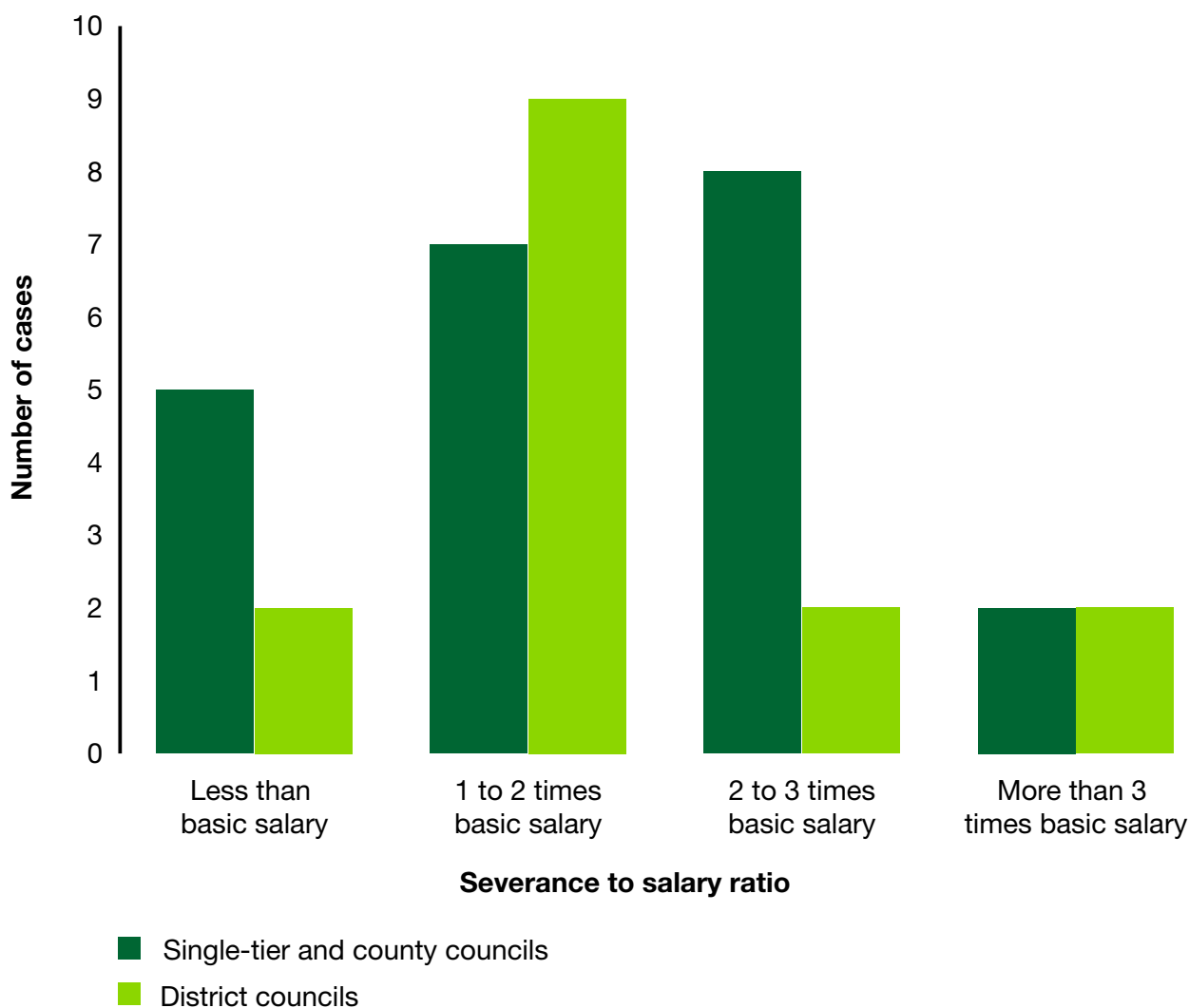
**72** Basic salaries are the key building block for calculating severance payments.<sup>i</sup> Basic salaries vary substantially, however, making comparisons between different settlements is difficult. The ratio of the cost of the settlement to the basic annual salary removes the effect of the basic salary and provides a better measure for comparing between settlements.

**73** The average settlement cost to the council, including unreduced pension costs, was 1.8 times the basic salary.<sup>ii</sup> There was no difference in the average between STCCs and DCs, but Figure 7 shows that there was a difference in the distribution.

- i** Payments such as discretionary lump sums, increased pension years and PILON are all based on basic salary.
- ii** If unreduced pension costs are removed, then the average severance was 1.1 times the value of basic salary with no marked differences between council types.

Figure 7: **Ratio of cost of severance package to basic annual salary**

Thirty nine per cent of payments cost councils more than twice the basic annual salary of their chief executive.



(Source: Auditor data) (Base: 21 STCC and 15 DC mutually-agreed severances)

**74** Subject to authorised limits, the size of each settlement is determined according to each council’s policies and is dependent on the specific circumstances of each case.<sup>i</sup> Analysis shows that:

- The length of a chief executive’s tenure is not statistically related to the severance to salary ratio – chief executives in post longer do not necessarily receive higher severance to salary ratios.
- Gender is also unrelated to the severance to salary ratio.<sup>ii</sup>

**75** However, cases relating to alleged misconduct by a chief executive have markedly lower ratios than those linked to relationship or performance issues.

- <sup>i</sup> These relationships remain the same regardless of whether unreduced pension costs are included or not.
- <sup>ii</sup> Data for the age of each chief executive was not available. It will be linked to settlement size in a complex way depending on whether the chief executive was aged 55 or over and whether an unreduced pension was paid.

## Unreduced pension costs are the biggest component

**76** Severance packages have a variety of components. Some of these are automatic, such as entitlement to an unreduced pension for those who meet the age requirements. But councils also have discretion within the statutory limits, and packages are negotiated individually. The package is likely to reflect, for example, compensation for agreeing to give up rights to go to an employment tribunal.

**77** The impact on future employability and any expected loss of future earnings may also be taken into account. Councils are able to reflect these circumstances in the discretionary payments – lump sums or increased pension years - they make to chief executives where termination is on grounds of redundancy or business efficiency.

**78** Seventy per cent of cases included either lump sums or increased pension years. These accounted for 39 per cent of the total costs (see Figure 8). Compensation for loss of future earnings is not the only factor underlying these calculations, however, so it accounts for some but not all of the costs attributable to these discretionary payments.

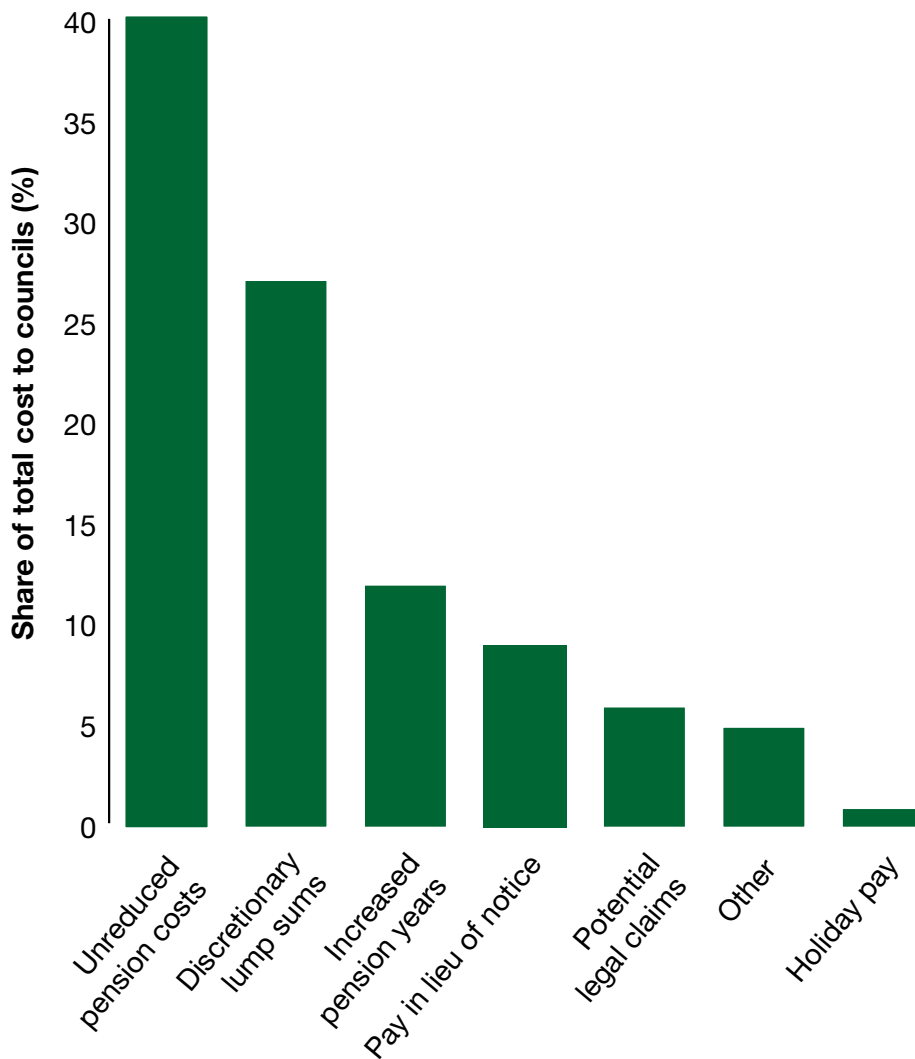
**79** Figure 8 also shows that unreduced pension costs are the most significant component (40 per cent) of total costs to councils. They were paid in 49 per cent of cases.

**80** The structure of packages differed slightly between STCCs and DCs:

- Unreduced pensions were a larger component of total costs in STCCs (45 per cent compared to 28 per cent).
- There were few awards of increased pension years in STCCs. They accounted for only 6 per cent of total costs in these councils. A number of large settlements in DCs meant that it accounted for 24 per cent of total costs. Where awarded, the average number of increased years given by STCCs was 1.7 years, whereas for DCs it was 5.7.
- Payments to prevent future legal claims were markedly higher among DCs (accounting for 12 per cent of total costs) compared to STCCs (4 per cent).

Figure 8: **Share of total costs to councils of severance payments by component**

Unreduced pension costs are the largest component of the cost to councils of severance payments



(Source: Auditor data) (Base: 36 mutually-agreed severances)

**81** Forty six per cent of packages also included an agreed press statement. In 38 per cent of cases, the chief executive was given an agreed reference.

# Causes of terminations with severance payments

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Causes of mutually-agreed departures	35
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**This chapter examines the causes of mutually-agreed terminations, and the extent to which the interests of the taxpayer were protected in awarding payments. It begins by analysing the factors underlying departures, before assessing the extent to which severance payments are appropriate in relationship-based cases. The final section examines the grounds on which payments were awarded in conduct and performance cases.**

## **Causes of mutually-agreed departures**

**82** There are three main causes<sup>i</sup> of mutually-agreed terminations in which severances are paid for council chief executives:

- relationship breakdowns – these cover a range of interpersonal difficulties between chief executives and senior members, from clashes of personality to members seeking removal of the chief executive to suit political purposes;
- concerns over performance – either the competence of chief executives in performing their functions, or broader concerns linked to the performance of the council as a whole; and
- concerns over misconduct.

**83** Auditors were asked to provide information on the causes that authorities gave for each mutually-agreed case. In many instances, auditors reported that authorities identified more than one cause.<sup>ii</sup> Interviewees and consultation respondents also provided evidence on underlying causes.

**84** Relationship breakdowns include cases where the members terminated the contract as they felt the chief executive was not the right person to take a council in a new direction. This reflects information from auditors that, in general, these cases were based on personality or political issues, rather than any genuine capability issue relating to the chief executive.

- <sup>i</sup> The causes of contract terminations in mutually-agreed cases are never more than unproved allegations. In using these three categories we are not implying any criticism of chief executives or members.
- <sup>ii</sup> Data on the causes of mutually-agreed terminations was provided by auditors for 33 (89 per cent) of the 37 cases. See methodology in Appendix 3 for explanation.

## Relationship breakdowns are a key driver

**85** There was agreement among the consultation respondents and interviewees that relationships were often at the heart of mutually-agreed terminations. The Association for Council Solicitors and Secretaries (ACSeS), for instance, referred to severance payments resulting from chief executives ‘falling out of favour with their political masters’.

**86** The Society of Local Authority Chief Executives and Senior Managers (SOLACE), stated that:

**‘The truth is that severances arise in the vast majority of cases not because of any genuine performance issue, but because a council leader wants a change in personnel.’**

**87** Auditors reported many cases in which authorities had identified alleged personality clashes and breakdowns in relationships as factors in mutually-agreed settlements. Across all councils, relationship issues were the most frequently cited problem and auditors linked them to 63 per cent of cases (see Figure 9).

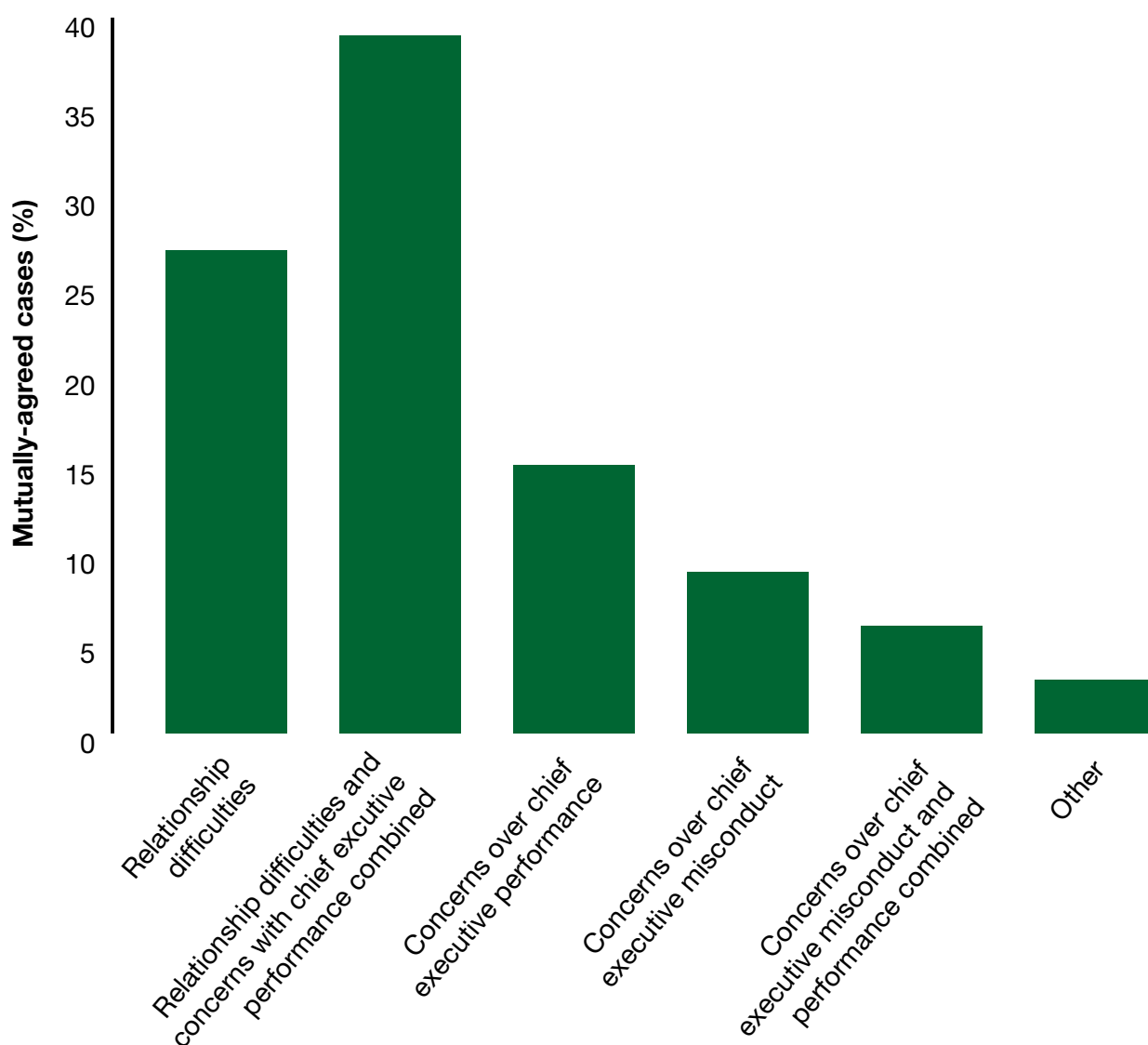
**88** There was a distinct overlap between relationships and performance, with 39 per cent of cases involving both. In many cases, these were based on a loss of confidence in a chief executive following poor performance by the council, which undermined relations with the political leadership.

**89** However, there were a significant number of cases (27 per cent) where auditors reported that authorities identified that relationship breakdown was the sole cause of the departure.

**90** The arrival of a new leadership was a trigger for relationship difficulties. In 36 per cent of mutually-agreed departures there had been a recent change in the council leader. However, in only 21 per cent of all cases had there been a change in political control. This means that in 15 per cent of cases, one in six, the departure was associated with a change in leader, but not in political control.

Figure 9: **Factors underlying mutually-agreed departures as reported by auditors**

Relationship issues, often linked to poor performance, are key drivers of departures



(Source: Auditor data) (Base: 33 mutually-agreed severances)

### Conduct and performance are contributory factors

**91** Concerns over performance and, to a lesser extent, conduct are also drivers of mutually-agreed departures. Cases have been precipitated by:

- poor inspection or assessment reports and scores;
- mismanagement of major projects;
- poor overall administration of council finances and affairs; and
- cases of alleged misconduct.

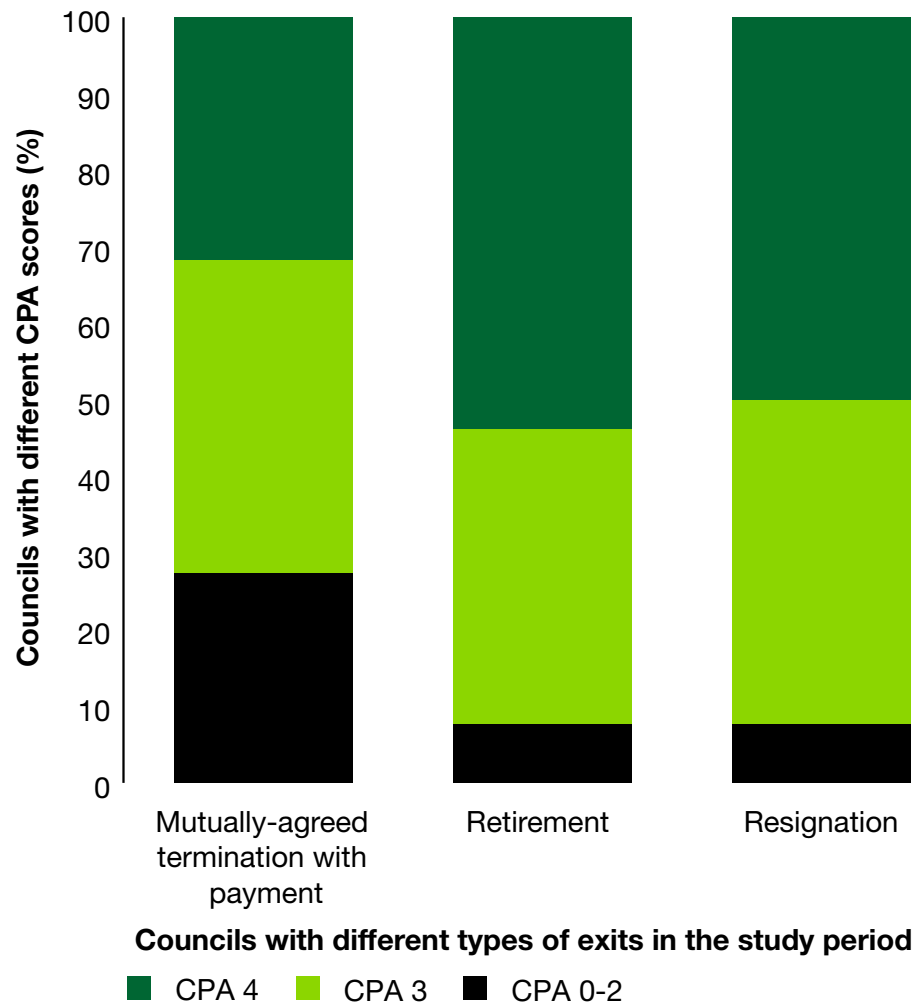
**92** Fifteen per cent of all mutually-agreed departures involved concerns over conduct. In 9 per cent, it was viewed as the sole cause (see Figure 9).

**93** Overall, performance concerns were present in 60 per cent of cases, but in only 15 per cent were they the sole cause (see Figure 9).

**94** Evidence from CPA scores for STCCs also supports the view that performance may be a factor. Analysis of chief executive exits shows that the profile of councils' CPA scores (in the preceding year) was markedly different in mutually-agreed cases from resignations or retirements (see Figure 10).

**95** Most noticeably, CPA scores of 0-2 occur at more than three times the rate in mutually-agreed departures than where chief executives have left due to retirement or resignation.

Figure 10: **CPA score in year preceding chief executive exit (STCCs only)**  
Weak CPA scores of 0-2 were three times as common where chief executives had been paid to leave rather than retiring or resigning



(Source: Audit Commission data and auditor data) (Base: 22 mutually-agreed severances, 13 retirements and 26 resignations)

**96** Bodies representing council chief executives do not accept that conduct and performance are significant factors:

- SOLACE argues that mutually-agreed terminations are almost exclusively driven by relationship issues and the wishes of local politicians; and
- ALACE stated that, based on its experience of many severance deals, ‘neither performance nor competence has any correlation to the likelihood of severance’.

**97** ALACE has argued that it is unusual for severance payments to result purely from the under-performance of a chief executive. Rather, it suggests that chief executives are often held responsible for the poor performance of the council, which may in fact result from the failure of members to take difficult decisions.

### **Clear differences between STCCs and DCs**

**98** There were differences in the causes underlying departures in STCCs and DCs.

- Relationship breakdown was prevalent in STCCs, with this being cited as a factor in 70 per cent of cases. They contained a large proportion driven solely by relationships, with 40 per cent being due to this cause alone. A further 30 per cent were due to a combination of performance and relationships.
- Relationships were also an issue in DCs and cited as a factor in 62 per cent of cases. However, in contrast to STCCs, relationships were the sole cause in only 8 per cent. Relationship issues were much more likely to be linked to allegations of poor performance, and in 54 per cent of cases they were cited as an accompanying factor.

**99** Overall, this suggests that there are different dynamics underlying mutually-agreed departures in the two types of councils. STCC cases appear far more focused on relationship issues, perhaps reflecting the higher profile nature of both the role and the political leadership. For DCs, however, the issues appear to be more managerial, with a much stronger focus on performance concerns. Where relationship issues emerge, they appear to be linked to performance.

### **Two main issues**

**100** From this analysis it is clear that:

- poor relationships are behind some terminations, which are costing public money; and
- in almost all cases where there are concerns over performance and conduct, chief executives leave with a pay-off.

## Poor relationships are costing public money

**101** Poor relationships are a driver of mutually-agreed departures. This means that factors such as personality clashes cost public money, as does the desire of a new leadership to replace a chief executive associated with the previous leadership. Contrasting arguments are made about this spending:

- that it is incurred for the sake of convenience, and is a poor use of public money; and
- that it is justified to avoid further cost and disruption.

### Payments for convenience's sake?

**102** One view is that members behave in a way that is convenient to them, rather than in the best interests of the taxpayer. The Secretary of State, in correspondence with the Commission relating to this research, argued that:

**'Council leaders should not be in a position where they can decide to offer expensive termination deals to chief executive officers simply because they don't get on, or because they'd prefer to work with someone else. In particular, just because a chief executive may have served a previous administration well does not mean that a newly formed council leadership should freely use taxpayers' money to replace them'.**

**103** SOLACE echoed these concerns, referring to 'whimsical or illegitimate dismissal by politicians'. It also stated that, 'Some local politicians seem to regard the costs of severances as an acceptable use of public monies'.

### Payments to avoid further cost and disruption?

**104** However, the view that payments are for convenience's sake was countered by the view that relationship breakdowns are complex, and often have fault on both sides. In these cases, a mutually-agreed severance payment may be the most cost-effective and least disruptive solution.

**105** The LGA Group stated that:

**'In these situations individual positions become polarised, relationships quickly deteriorate and the management of the local authority is seriously affected. The longer these cases drag on the more damage is done to the organisation and the quality of the services it provides'.**

**106** The Association of Local Authority Treasurers' Societies also identified that mutually-agreed settlements mean councils avoid the risk of lengthy, disruptive and potentially costly litigation if these cases were to go to tribunal.

## **There is evidence to support both arguments**

**107** Given the complexity of individual cases, and the vested interests on both sides, it is difficult to establish the true position. However, it is clear that across the sector:

- there are instances where personality clashes have precipitated mutually-agreed terminations with accompanying severance packages; and
- some leaders have sought the removal of a chief executive for personal or political reasons, often when first taking office.

**108** However, emerging relationship problems were often accompanied by a perceived performance or competence issue. Difficulties in some activity, programme or inspection often place a strain on relationships. If left unchecked, this can lead to an irrecoverable breakdown. In these cases, while it is ultimately a dysfunctional relationship that leads to the contract termination, it is not simply a case of poor behaviour by either or both parties.

**109** In cases driven by relationship difficulties, councils are often not in a position to mount a case for dismissal through the two stages of the disciplinary procedure. Consequently, they negotiate a settlement with the chief executive. These cases represent the majority of instances where mutually-agreed severance payments are made.

**110** Some councils have sought to resolve relationship issues through mediation, as recommended by the JNC (Ref 1). However, the research was only able to identify cases where mediation has failed, or leaders and chief executives were unwilling to enter mediation.

**111** However, both the LGA Group and ALACE agree that mediation should be used more widely by councils. Crucially, this should take place at an early stage before problems become intractable. In the unsuccessful cases identified in the research, problems were longstanding before mediation was attempted.

## **Compensation is almost always paid in performance and conduct cases**

**112** Where performance or conduct issues arose, they were almost always addressed through the negotiation of mutually-agreed settlements, rather than through statutory disciplinary procedures.

**113** For chief executives, the disciplinary route requires the appointment of a Designated Independent Person (DIP). During the study period, there were only two instances where a DIP was appointed, and only one of these led to dismissal<sup>i</sup> – the only instance in which a chief executive left involuntarily without compensation.

- i** The DIP case that did not lead to dismissal was resolved through a negotiated settlement before the DIP investigation was completed.

**114** It is possible that chief executives with conduct or performance issues may have voluntarily resigned or retired without a severance. However, analysis of the data shows there was only one case where this might have happened.

**115** There are two main reasons for the lack of DIP appointments in cases where councils have genuine performance and conduct concerns:

- deficiencies in performance management arrangements for chief executives; and
- shortcomings in the DIP process.

### **Performance management is poor**

**116** There is a widely held view that the performance management of chief executives by members is weak. ALACE, for instance, stated that:

**‘In many instances local authorities are not very good at this and members seem to find engagement in the process problematic’.**

**117** Local Government Employers (LGE) echoed these views and referred to the difficulties of performance management of professionals by ‘lay people’.

**118** Performance management arrangements for chief executives are very different from those for all other local government employees. Chief executives are performance managed by elected members rather than officers. Members have varying levels of performance management experience. This has two potential implications:

- the absence of performance management frameworks means that improving chief executive performance and avoiding contract termination is more difficult; and
- a lack of appraisal evidence means that in some cases of alleged poor performance the council is unable to mount a case for dismissal.

**119** This suggests that, in the absence of a framework to improve a chief executive’s performance or to demonstrate shortcomings, members may see mutually-agreed termination with a severance payment as the most straightforward option.

**120** While there are problems in the way that individual councils are pursuing performance management and appraisal of chief executives, a sector-wide model does exist and is set out in the JNC’s conditions of service (Ref 1). This provides guidance about setting regular and formal meetings, engaging external support and setting clear targets and expectations. The guidance suggests that the appraisal is conducted either by a small cross-party committee or by members of the controlling group. However, the guidance is clear that, whichever model is adopted, the appraisal needs to reflect the fact that the chief executive serves the council as a whole.

**121** These conditions are included in the contracts of many chief executives, and councils therefore ought to engage in a formal process of performance management. However, the clear message back from the LGA Group, ALACE and auditors is that, despite this, performance management of chief executives by members is not of a sufficiently high standard.

### **There are problems with the operation of the DIP system**

**122** The statutory protection afforded to chief executives means that dismissal is only possible on the recommendation of a DIP, following a full investigation.

**123** There are concerns about the way this system operates. LGA Group made this case most strongly arguing that:

**‘In practice the system has placed local authorities, as the employer, at a great disadvantage in comparison to the position of the employee’.**

**124** The LGA Group cites two major areas of concern:

- the length of time required – appointing a mutually-agreed DIP and then undertaking the investigation is time consuming. LGA Group estimates four months at a minimum while ALACE suggests an average of 12 months. The one DIP case to reach completion in the study period took 16 months; and
- the cost of the process – LGA Group describes the process as ‘increasingly legalistic’ and estimates a minimum legal cost to a council of £100,000, excluding the cost of the investigation, preparing the case and briefing lawyers. Salary costs for a suspended chief executive will also have to be met by the council. The one DIP case that reached a conclusion cost the council over £420,000 in legal fees and salary costs for the suspended chief executive.<sup>i</sup> The case was in a DC and the cost is higher than any of the severance payments made to DC chief executives in the period.

**125** The research identified several cases relating to both conduct and performance, in which councils had rejected the DIP route on the grounds of cost and disruption. There were also a number of instances where councils had compared the cost of the DIP process with a negotiated settlement and found in favour of the latter.

<sup>i</sup> Data provided by relevant council.

**126** Councils' perception of the DIP process as costly and time-consuming has two effects:

- it strengthens the position of chief executives in severance negotiations, which may increase costs. Councils look to settle at a cost below their estimation of the cost of the DIP process. Since that is often high, this is to the chief executive's advantage; and
- it reduces the likelihood that councils will try to dismiss chief executives, where they have a case for doing so, increasing the frequency of negotiated settlements. Even in cases where there are genuine performance or misconduct issues, the costs and delays of the DIP process mean that councils will almost always try to negotiate a termination with a severance payment. This means that poorly performing chief executives, or those facing misconduct allegations, are sometimes paid to leave.

**127** We should be clear that this problem is not as significant as the exits and payments arising from relationship breakdown. But nonetheless, councils' unwillingness to pursue performance and conduct dismissals through the DIP process does generate additional payments.

# Management of terminations with severance payments

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**Decisions to employ a particular chief executive, and the terms of any severance payment when necessary, are the responsibility of individual councils. However, there are concerns about some councils' arrangements for severance negotiations and payments, particularly the extent to which decisions are well-informed. There are also misconceptions about the role of the auditor. Finally, transparency for the public has also been a concern.**

## **Local management of terminations and severance payments**

### **Ensuring informed decisions**

**128** There are concerns about the quality of knowledge, information and advice for members to support decision-making. Issues include:

- members not routinely receiving appropriate legal, financial and HR advice;
- some officers having insufficient knowledge of the law; and
- reports to members regarding contract terminations and severance packages often lacking key information.

**129** Overall, there is a concern that;

**'Members who approve packages are untrained in such matters and decisions can be led by officers who are using the flexibility of the regulations to get the packages agreed without effective challenge.'**

### **Audit Commission Appointed Auditor**

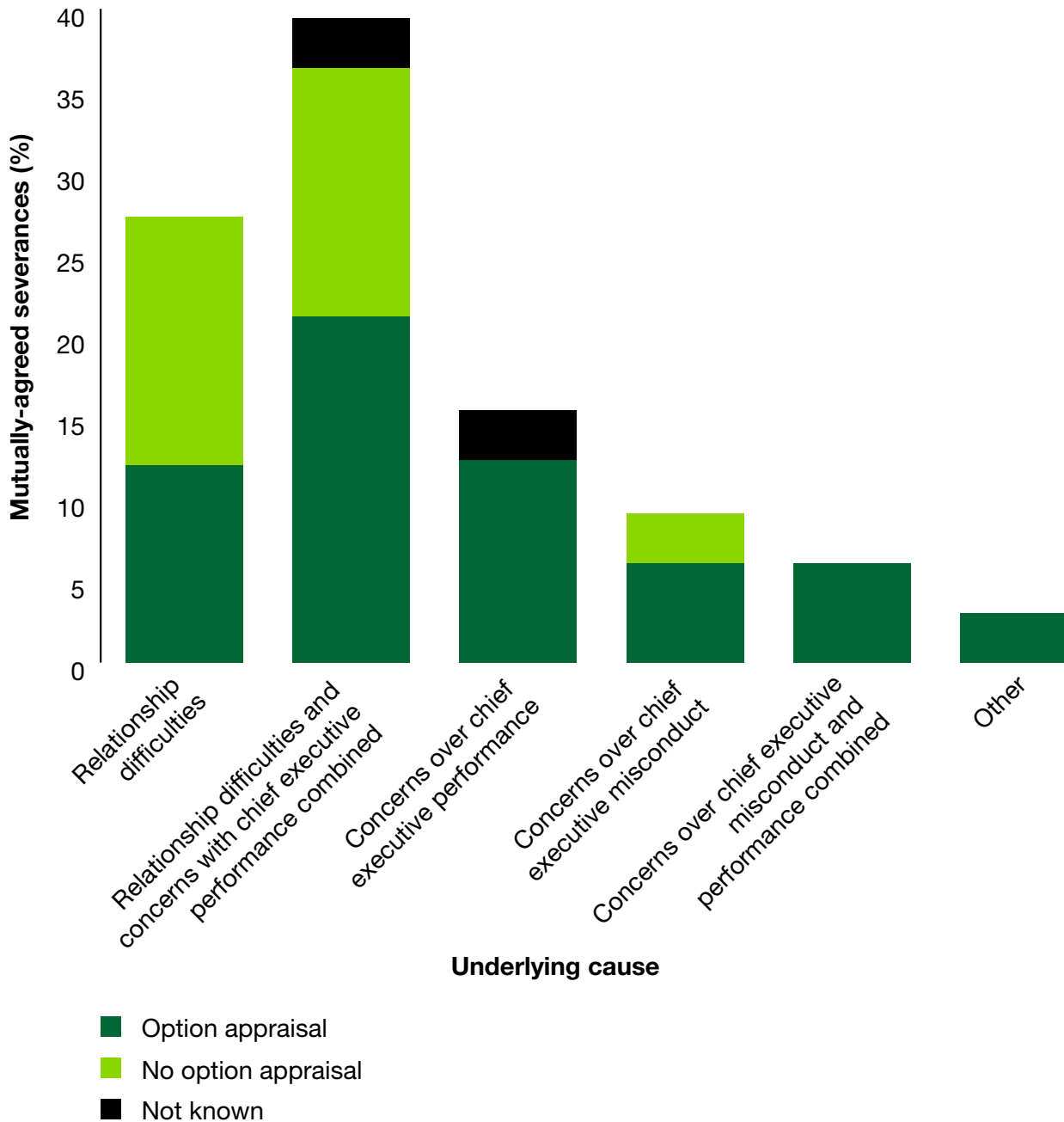
**130** There is often no option appraisal, setting out the different choices open to the council, to inform members' decision-making. Each option should be fully costed to allow members to assess the implications of particular courses of action for the taxpayer.

**131** In 61 per cent of cases option appraisals were undertaken. However, in one-third of cases they were not.<sup>i</sup> In these cases members were not formally made aware of the different courses of action open to them and the potential costs of each.

<sup>i</sup> In 61 per cent of cases an appraisal was undertaken, in 33 per cent they were not and in 6 per cent supporting papers were not available to the auditor.

**132** Option appraisals were much less likely for terminations driven by relationship issues – see Figure 11. Arguably, in cases of relationship breakdown, there are fewer options available. Nonetheless, this apparent lack of consideration of alternatives and their costs, raises questions about the extent to which the interests of taxpayers were taken into account.

**Figure 11: Prevalence of option appraisals in early terminations with severance payments**  
 Many severance payments resulting from relationship breakdowns were awarded without full option appraisals



(Source: Auditor data) (Base: 33 mutually-agreed severances)

## Concerns over members' behaviour

**133** By agreeing to terminate a contract and signing a compromise agreement with chief executives, councils secure a chief executive's departure without further legal liability arising. This protects councils from claims such as unfair or wrongful dismissal, which could cost more if they were taken to an employment tribunal.

**134** Members need to be fully aware of the implications of their actions in contract terminations, as their behaviour can inadvertently provide grounds for unfair dismissal claims before any agreement is finalised. This gives chief executives greater leverage in the negotiation process, driving up the cost to the taxpayer.

**'Independent action by members and the statements they often make to chief executives can, and usually do, create the circumstances whereby the chief executive can claim for unfair dismissal.'**

### **Audit Commission Appointed Auditor**

**135** The leadership of one council announced, before any discussions, that they wished the chief executive to depart, increasing the risk of an unfair dismissal claim.

## The role of the auditor

**136** Auditors often consider chief executive severance payments. Both the LGE and ALACE indicated that they believe that auditors have played an important oversight role in recent years. However, some representative bodies and councils appear to have a misconceived idea of the role of the auditor in the severance process.

**137** Auditors have a responsibility to satisfy themselves that the council has proper arrangements to secure value for money and to report if these are not in place. However, auditors are not required to consider whether all aspects of the council's arrangements are operating effectively, or to consider routinely all severance payments that come to their attention.

**138** When planning their work, auditors often consider whether councils' handling of chief executive severance cases is likely to be a significant risk to their conclusion on councils' overall arrangements for value for money. Consequently, 94 per cent of mutually-agreed severance payments were considered by auditors. But it is not the function of auditors to provide specific assurance to councils on individual cases. Councils are responsible for taking their own advice on the legality and value for money of their decisions.

**139** In the majority of cases considered by auditors, they were satisfied that severance arrangements and associated payments did not give rise to significant issues on which they needed to report. However, in 39 per cent of cases, auditors identified matters they needed to bring to the attention of the council, including issues relating to:

- the value of the packages;
- the basis of terminations;
- the lack of option appraisals; and
- other weaknesses in the procedures followed by the council.

**140** In some cases auditors raised concerns, for example through a letter to the audit committee, which meant that subsequently the council took action and the auditor did not need to report more formally. But in 18 per cent of cases, auditors were critical of councils in:

- annual governance returns (two cases);
- annual audit letters (three cases); and
- one public interest report.

## Transparency

**141** Involvement in a mutually-agreed termination could cause reputational damage to both sides, so confidentiality can have benefits for one or both parties. Some 79 per cent of mutually-agreed severance payments had a confidentiality clause.

**142** There are significant sums of public money at stake, and the grounds for terminations are often personal rather than performance-based. However, arrangements to date have not been transparent enough to the public. Confidentiality agreements have allowed large severance payments to be agreed that may have been difficult to defend in public.

**143** New requirements to publish officer remuneration from 1 April 2010 will bring a different dynamic to the negotiation of settlements for council chief executives. It may place councils under greater pressure to account for their actions.

# Conclusions

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Issues to be addressed

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**Severance payments arise from a complex mix of competing interests. The political leadership has a democratic mandate and wants a chief executive who will help implement its policies. But chief executives work for the whole council, not just the political leadership and have a right to fair treatment and protection from political interference. Finally, taxpayers expect their money to be spent appropriately.**

**144** Reconciling the interests of members, chief executives and taxpayers is difficult. A constructive working relationship between the chief executive and senior members is important for running the council well. If this relationship breaks down, a quick departure may be in the public interest. The cost to the taxpayer needs to be weighed against the negative impact of a dysfunctional relationship at the top of the council and the leadership vacuum that may result.

**145** But some exits and severance payments could be avoided. Decisions by members to pay off the chief executive, often following a change in leadership, are not always justified. Elected politicians should not seek to remove chief executives simply because they served a previous leader, or for working in the interests of the whole council rather than just the current leaders.

**146** Nor should severance payments be a reward for failure, or a substitute for sound performance management. Currently, councils regard the disciplinary arrangements for chief executives as complex and expensive, so they look to negotiate settlements even in genuine performance and misconduct cases, rather than pursue dismissal. Poor performance management by members compounds this, as they lack appraisal evidence to mount robust cases where performance is genuinely in question.

## **Issues to be addressed**

**147** There are a number of issues that should be addressed:

- Many chief executives lose their jobs as a result of the personal wishes of members. This imposes an unnecessary cost on the taxpayer and means that councils lose competent officers.
- The procedure for dismissing chief executives in performance and conduct cases is too expensive and complex.
- Performance management of chief executives is not of a high enough standard.
- There are areas in which councils can reduce the costs of severance payments.

**148** There are several possible interventions that will help address these issues.

### **Greater openness**

**149** To address the issue of members pursuing personal or politically-motivated objectives, the process of contract termination and the negotiation of severance payments should be open to greater scrutiny and challenge within a council. Requiring all severance decisions to be reviewed at a cross-party committee, such as a remuneration committee, would provide a sterner test to justify cases. Such a requirement would force members to be more circumspect when seeking early contract terminations. Where severance payments are awarded, this mechanism would also ensure that the costs were fully justified.

**150** Greater public transparency would also help to shape members' actions and may keep costs down.

**151** The new requirements to publish the costs of severance payments are a step forward. However, publication is not required until the final accounts are published up to six months after the end of the financial year in which a payment was made. This means there could be a delay of 18 months<sup>i</sup> between a severance payment and its publication, too long for adequate accountability to the public; this is long enough, for instance, for the political leadership to change. Requiring publication of the costs shortly after a decision is taken, as well as in the accounts, would address this.

**152** Government should also consider making the publication of severance payments more prominent through the introduction of remuneration reports for councils. These should be published alongside their financial statements and should include details of the council's remuneration policy as well as details of salaries and severance payments. While the JNC national salary guidelines for chief executives form the framework for setting and re-negotiating chief executives' salaries, councils still have a degree of discretion within these. This would be reflected in these reports.

### **Review statutory protection mechanisms**

**153** The disciplinary mechanisms in place for statutory protection are perceived as lengthy, legalistic and expensive, and councils are reluctant to invoke them. Instead, poorly-performing chief executives, or those with poor conduct records, are paid off rather than disciplined or dismissed.

<sup>i</sup> Though a statement of accounts will be placed on deposit a month or so before final accounts are published. This means the accounts will be presented to council and maybe placed on the council's internal intranet.

**154** There is an argument to abolish the DIP process as this would ease the process of performance and conduct-based dismissals. Alternatively, the LGA Group has made a number of suggestions that may go some way to lessening the burden of the DIP process (see Appendix 6). ALACE has also indicated that the DIP process could be simplified.

**155** However, simplifying the process for dismissals is only part of the issue. There are also questions over the extent to which the current statutory protection mechanisms protect chief executives where conduct and performance are not a consideration.

**156** The extent to which the current system gives chief executives the confidence to challenge members on a day-to-day basis is not clear, while the system's capacity to prevent politically-motivated terminations is limited. As it currently functions, the statutory protection mechanisms provide greater financial rather than job security; chief executives are still losing their jobs for personal and political reasons at a significant rate, but they leave with a larger pay-off. Taxpayers have to meet these costs while also losing competent chief executives.

**157** Given this context and the concerns over the role of the DIP process in rewarding failure, it seems important to review the mechanisms in place for statutory protection before any reform or replacement. Ultimately, what is required is a mechanism that provides greater job security in relationship cases, but is less restrictive in performance and misconduct cases.

### **Address performance management**

**158** Despite the existence of a model for the appraisal of chief executives in the JNC conditions of service (Ref 1), it appears that councils' processes are weak. Councils have not generally implemented effective processes, the government may, therefore, need to consider legislation or regulation to ensure that proper chief executive appraisal is undertaken by all councils. The LGE and ALACE should also consult on whether the current JNC appraisal model is sufficient or whether amendments are required.

### **Wage restraint, managing expectations and clawback**

**159** Basic salaries form the building blocks for the calculation of severance payments. Basic salaries for chief executives have increased significantly faster than for the wider local government workforce in recent years, particularly in STCCs (Ref 6). Larger basic salaries mean larger severance payments. Pay restraint across the sector will slow the growth in the size of severance packages to some extent.

**160** Councils should consider potential severance payments when agreeing basic salaries with newly appointed chief executives. This may not appear relevant at the time, but there is a strong possibility that the chief executive will leave with a payment. This research has shown that nearly one in three departures involves a payment.

**161** Councils should consider whether to include pre-agreed arrangements or clauses in chief executives' contracts that specify grounds on which early termination may be sought and the nature of any payment. These arrangements are often referred to as 'pre-nuptial' agreements. Councils are not able in law to set settlement values in contracts that are payable, regardless of circumstance. Nonetheless, they are able to insert special clauses that set out a preferred amount. While these may, or may not, be enforceable in law, they are likely to be helpful in managing expectations on both sides. If so, they may reduce both the cost and the disruption of terminations. Councils would need to be aware of how these would fit with wider contractual agreements and general employment law.

**162** An element of most severance payments is to compensate for future loss of earnings. Where alternative employment is secured, and the negative impact on future earnings is therefore mitigated, there is a question as to whether compensation for the initial departure remains reasonable. The government, the LGA Group and individual councils considering chief executives' contracts should consider what measures could be put in place to recover components of severance payments in cases where a chief executive is rapidly re-employed in local government, or even elsewhere in the public sector.

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## Appendix 1: References

- 1 Joint Negotiating Committee for Local Authority Chief Executives, *National Salary Framework and Conditions of Service Handbook*, JNC, 2009
- 2 *Statutory Instrument 1993 No. 202 The Local Authorities (Standing Orders) Regulations 1993*, HMSO, 1993
- 3 *Statutory Instrument 2001 No. 3384 The Local Authorities (Standing Orders) (England) Regulations 2001*, HMSO, 2001
- 4 *The Local Government (Early Termination of Employment) (Discretionary Compensation) (England and Wales) 2006 Regulations*, The Stationery Office, 2006
- 5 *The Local Government Pension Scheme (Benefits, Membership and contributions) Regulations 2007*, The Stationery Office, 2007
- 6 Audit Commission, *Tougher at the Top?*, Audit Commission, July 2008

## Appendix 2: List of Abbreviations

- ACSeS – Association of Council Secretaries and Solicitors
- ALACE – Association of Local Authority Chief Executives
- ALATS – Association of Local Authority Treasurers' Societies
- CE – Chief Executive
- CIPD – Chartered Institute for Personnel and Development
- CLG – Department for Communities and Local Government
- CPA – Comprehensive Performance Assessment
- DC – District Council
- DIP – Designated Independent Person
- DoH – Department of Health
- HR – Human resources
- LGA – Local Government Association
- LGE – Local Government Employers
- LGR – Local government reorganisation
- JNC – Joint negotiating committee
- PILON – Payment in lieu of notice
- PPMA – Public Sectors' People Management Association
- SOLACE – Society of Local Authority Chief Executives and Senior Managers
- STCCs – Single-tier and county councils

## Appendix 3: Methodology

### Main methodology

Data collection was carried out between September 2009 and January 2010. This involved qualitative and quantitative methods. These included:

- a public call for views on the rules and regulations relating to severance payments for council chief executives;
- interviews with relevant organisations;
- a quantitative survey of the appointed external auditors for councils in England; and
- analysis of cases of rapid re-employment.

#### Public consultation

Throughout September 2009 the Commission ran a public call for evidence into the severance arrangements. Some 14 responses were received; nine from members of the public and five from stakeholder organisations. These included:

- Association of Local Authority Chief Executives – ALACE;
- Association of Local Authority Treasurers Societies – ALATS;
- Association for Council Secretaries and Solicitors – ACSes;
- Local Government Association Group – LGA Group; and
- Society of Local Authority Chief Executives and Senior Managers – SOLACE.

ALACE also submitted a second document in response to some additional questions from the Commission.

#### Interviews

The following organisations were interviewed in the course of the work:

- ALACE;
- Local Government Employers – LGE;
- Bates, Wells Braithwaite Solicitors;
- Department of Health;
- FDA;
- Standards for England
- Chartered Institute of Personnel and Development – CIPD; and

- The Public Sector People Manager Association – PPMA.<sup>i</sup>

#### Data collection from auditors

In October 2009 data collection tools were sent to appointed auditors of councils where a chief executive departure had occurred in the study period. Information was collected on the type of exit, the nature of any severance payments, the background of the termination and recommendations for improvements to the system.

Financial data was provided by the current auditor, while background information was collected from the auditor responsible for the audit at the time of the exit.<sup>ii</sup> There were two cases where auditors did not examine a severance and a further two where auditors in post at the time of an exit have left the Audit Commission or one of its private suppliers. Financial details were nonetheless available in three of these four cases. Figure 12 sets out the implications of these responses.

Figure 12: Number of data returns

Data area	Cases in which data was provided (out of 37 cases)
Payment of a severance	37
Precise financial details of payment	36
Underlying causes or termination	33

This difference in base numbers means that it is not possible to use absolute numbers throughout the report. Data in Chapter 3 is based on a 100 per cent census, while Chapter 4 contains data on 36 of the 37 cases. In both these instances it is reasonable to use absolute numbers. However,

- <sup>i</sup> Contact with PPMA was via written correspondence.
- <sup>ii</sup> In 73 per cent of cases the current auditor was also responsible for the audit at the time of the exit.

chapters 5 and 6 use data from 33 of the 37 cases (89 per cent). While this data is likely to be representative of the population it is misleading to include the absolute numbers as these are for a sample rather than the population as in the previous chapters, and are therefore likely to be lower than in the population as a whole. Consequently, percentages are used in these chapters.

Follow-up interviews were held with auditors responsible for 19 mutually-agreed cases. Seven auditors also responded to the public consultation.

### **Rapid re-employment**

The data provided by auditors identified all mutually-agreed severance cases in the study period. Data was then collected on the employment path of each exiting chief executive following departure. This was drawn from auditors and from public information sources.

The research identified cases where departing chief executives in mutually-agreed severance cases had taken full-time, permanent employment in executive roles in public bodies of all types within a 12-month period of their exit. Data was taken from auditors and publicly available information sources.

The research included appointments at director level as well as to chief executive posts. For DC chief executives, an appointment at director level in an STCC was considered to be on a par with the previous role.

### **Calculating changing rates in severances over time**

Data for non-resignation chief executive exits was collected for STCCs going back to 2000, and reported in the Commission's report *Tougher at the Top* (Ref 6). This data can be compared with similar data collected in the current research – this includes all exits in the study period including mutually-agreed severances, but excluding resignations.

## **Appendix 4: Responsibilities of the chief executive**

The following sections are extracted from the JNC's conditions of service handbook for chief executives (Ref 1).

The chief executive has responsibility for:

- 'leading the management team or equivalent, in particular in securing a corporate approach;
- securing the provision of advice on the forward planning of objectives and services;
- ensuring the efficient and effective implementation of the council's programmes and policies across all services and the effective deployment of the authority's resources to those ends;
- advising the council, its executive and its committees on all matters of general policy and all other matters upon which his or her advice is necessary, with the right of attendance at all committees of the council and all subcommittees and working parties;
- advising the leader or elected mayor of the council, or where appropriate the party group leaders, on any matter relevant to the council's functions;
- representing and negotiating on behalf of the council on external bodies and networks; and
- advising or making suitable arrangements for advising the Lord Mayor, Mayor or Chair of the council on all matters within the duties of that office'.

## Appendix 5: Severances included in the report

Seventy five severance payments, excluding early retirement requests, were paid to council chief executives in the study period. However, many do not fall within the remit of this research. In particular, the following cases are not relevant (see Figure 12):

- Thirty three severance cases were due to redundancies linked to the 2009 local government reorganisation (LGR) process.<sup>i</sup>
- Four severances resulted from redundancies due to councils introducing shared chief executive arrangements with either Primary Care Trusts (PCTs) or other councils. In these cases the chief executive post was abolished in the relevant council.
- One severance was due to ill-health. Ill-health was mentioned in two other cases, but other factors were involved and the contracts were terminated by mutual agreement rather than for ill-health.

This leaves a further 37 cases where the contract has been terminated early, other than due to early retirement requests from the chief executive. These remaining cases are ‘mutually-agreed’ severances that fall within the remit of the research.

<sup>i</sup> Councils involved in LGR have been excluded from all the analysis in this research altogether. This means the base number of councils used in the analysis is 143 STCCs and 201 DCs.

Figure 13: **Reasons for contract terminations in severance payment cases in the study period**

Thirty-seven of the 75 severances paid in the study period are relevant to the research.

Contract termination	Number	Included in the research
<b>Redundancy – due to 2009 local government reorganisation</b>	33	x
<b>Redundancy – shared CE</b>	4	x
<b>Ill-health</b>	1	x
<b>Mutual agreement cases</b>	37	✓
<b>Total</b>	<b>75</b>	

(Source: Auditor data)

The research has been careful to exclude mutually-agreed severance packages arising from requests by chief executives for early retirement. Early retirements have been distinguished from the target group of mutually-agreed severance payments on two grounds:

- Discretionary lump sums cannot be awarded in cases of genuine early retirement requested by the chief executive. Consequently, as these sums cannot be paid in early retirement cases, any mutually-agreed settlement package including these payments is relevant to the research.
- In cases where discretionary lump sums have not been paid, auditors have provided evidence on the background to the severance payment. The research only includes cases where there is clear evidence that the payment is based on factors other than a request for early retirement from the chief executive.

Consequently, the mutually-agreed severance payments discussed in this report exclude any packages negotiated in cases of genuine, voluntary early retirement resulting from requests from chief executives.

## Appendix 6: LGA Group's proposals for reform of the DIP procedures

As part of the consultation for this report John Ransford, Chief Executive of the LGA Group, wrote to the Audit Commission with the following comments and proposals regarding the DIP procedures:

- 'The appointment process for a Designated Independent Person can be an obstacle because the DIP has to be agreed by the parties, which effectively gives a veto over a proposed appointment. We would propose that the regulations be amended so that the JNC for Chief Executives of Local Authorities (in respect of chief executives) and the JNC for Chief Officers of Local Authorities (in respect of monitoring officers and section 151 officers) are jointly responsible for maintaining a list of DIPs. The list would comprise suitable people retained and appointed by the JNCs, suitability being based on knowledge, skills, experience and, of course, independence.
- A further obstacle is the fees paid to DIPs. There is no fixed rate currently, so fees are a matter for negotiation between the council (which is responsible for paying) and the DIP. If the chief executive proposes an expensive DIP the council can find that the only alternative is not to agree that person and thus prolong the process further. We would therefore propose that the JNCs should agree and periodically review the daily rate for that work, based on appropriate comparators.
- In some cases there is evidence that the appointment of a DIP may have been premature. This is not because councils have acted hastily or unreasonably, but because they have concluded that there may be a case to answer and have appointed a DIP when the remedy may better lie in mediation between the parties. We therefore believe that the DIP should be given the power to adjourn proceedings to allow mediation to take place'.

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