

REPORT OF THE CHAIR OF THE TRANSPORT AND HIGHWAYS COMMITTEE

HIGHWAYS AND FLEET MANAGEMENT JOINT VENTURE COMPANY

Purpose of the Report

1. To seek approval for the establishment of a joint venture company with CORMAC for the delivery of integrated highway services for Nottinghamshire.

Information and Advice

The Current Position

2. Highways are a vital part of the infrastructure of any area and a universally used service for residents and businesses in the County. The sustainability of the current service is challenged by the current financial position of the Authority, and as a result alternative service delivery models have been considered to secure a long term sustainable service.
3. The service has experienced very significant revenue budgetary reductions, over the last few years, whilst at the same time dealing with increased demand and a growing asset base. Many of the services provided in respect of Highways are statutory and whilst short term reductions in service can and have been made, these are not sustainable in the long term and the current model of provision will become unviable unless steps are taken to address the situation.
4. Further savings to the value of £1.1m are predicated against the Highways budget. Without both commercial input and adopting more flexible operating practices it will not be possible to improve productivity and sustain the current range, depth and quality of Highways services. This situation is compounded by the increasing buoyancy of the construction market which has already attracted skilled staff away from the local authority sector. Adopting a commercial approach, securing external business and enhancing productivity has become paramount for the future viability and sustainability of the service.
5. An options appraisal was undertaken in 2014 to identify the most appropriate model to deliver a sustainable Highways service. The options appraisal was based on 3 key assumptions:
 - That the Authority would retain a high degree of control over any new service provision.
 - That any new service provision would deliver a balance of value for money and service quality.

- That any new service would be commercially viable and have the capability to market and sell design and delivery services into the market to ensure its sustainability.
6. The options appraisal concluded that a public joint venture company with an existing provider – such as CORMAC, was the best model to satisfy the above criteria.
 7. The Authority has taken external legal advice from Bevan Brittan LLP to ensure the best model and the proposed governance and contractual structure are compliant with the legal framework within which the Authority operates. Much of this work is still ongoing and legal issues are still to be finalised including the terms of governance arrangements; ensuring the group structure satisfies the new Procurement Regulations; terms of the proposed service regime are enforceable through robust contracts and that the services specifications and payment regimes meet the Authority's requirements.

The Proposed Partner

8. CORMAC was established in 2012 as a wholly owned company by Cornwall Council. Since that time, it has grown considerably, increasing its turnover by an additional £35m per annum, staff numbers have increased by 16% and benefits returned to Cornwall Council to the tune of £20m over 3 years through productivity improvement rebates and from profit on external work. CORMAC operates through two companies: CORMAC Solutions Ltd – which is a Teckal company and CORMAC Contracting Ltd which is a trading company. Both these companies provide a range of services to Cornwall Council. If the decision is taken to establish a joint venture with CORMAC, Cornwall Council would establish a holding company, provisionally known as CORSERV. CORMAC Solutions Ltd and the new joint venture company would be subsidiary companies of CORSERV. A case study on CORMAC is included within the DfT's Highways Maintenance Efficiency Programme and this is listed as one of the background papers.

The New Arrangement

9. The new joint venture company would be a "Teckal Company" which means it is controlled by a Local Authority or authorities and can trade outside that local Authority(s) by up to 20% of its turnover and this has been introduced into law by the Public Contracts Regulations 2015. If services were to be undertaken by such a company there should be no requirement to undertake a competitive procurement process. Instead, the proposed arrangements (especially the arrangements between the new company and CORSERV) would need to satisfy the new procurement regulations.
10. It is proposed that the new joint venture company would provide the current Highways and Fleet Maintenance and Fleet Management services for the Authority. This is with the exception of: flood risk management, transport planning, strategic programme development, definitive map, town and village green functions and assurance processes in relation to traffic regulation orders, parking enforcement, traffic and asset management and highways development control. Energy procurement and highway policy and strategy enquiries would also remain with the Authority. It would be the intention to include the responsibility for managing the Lafarge Tarmac contract in the scope of services to be performed by the new company and at some stage the Civil Parking Enforcement Unit.

11. If the proposals are approved, it is intended that the newly formed company would commence trading from April 2016. The Authority would enter into a 10 year contract with the new company with a possible extension for a further 5 years thereafter.
12. Should the Authority wish to cease the arrangement, the contract would provide that it can be reviewed after 3 years and ended after 5 years on a no-fault arrangement. However, in the event of major performance failure, the contract can be terminated at any time. The contract would contain detailed definitions as to what constitutes major performance failure. If the contract continues beyond 5 years, two years notice would be required to end the arrangement. There would be costs associated with any decision to exit the contract.
13. The principle of this arrangement is that the Authority would lay out what it wants the company to deliver and what resources it can afford to provide – ie outcomes and budget allocation. It would be up to the new company to determine the best way to deliver this – ie the operational practices and procedures, and the how. As now, annually the authority would determine the budget to be allocated for Highways and Fleet, this having been worked up through the negotiation between the County Council and the new company. The company would use budget allocation along with their forecasts of commercial growth to form their business plan for the following year and this would be subject to unanimous sign off by the board. As is the case with Cornwall Council, if the Authority needs to further reduce budgets or change priorities this can be done and the new company would advise on the implications and determine the best approach to deliver the revised service.
14. Staff currently employed by the Authority in Highways services would transfer to the new company under TUPE provisions, i.e. on their existing terms and conditions, including, where relevant, the living wage. It is intended that the company would also have admitted body status to the Nottinghamshire Local Government Pension Scheme (LGPS), and as such, staff transferring to the new company could remain in the scheme. More detail on HR issues is included at Appendix 1.
15. In the longer term the CORMAC Group proposal is to provide the support services to the new company through the holding company CORSERV. This is still subject to further negotiation and compliance with the new procurement rules. On a temporary basis, but for a minimum of 12 months, the intention is for payroll and other HR operational functions and ICT services to be provided by the in-house teams at Nottinghamshire. There may be some staff from other support services who would also TUPE transfer to the new organisation. These staff have yet to be identified, however, it is estimated there would be a minimum of two full time equivalent posts.
16. Public contact to Highway services would remain via the Customer Service Centre, as per the current arrangements, and complaints would also be received by the County Council and dealt with through joint processes. Highways information such as winter maintenance routes, traffic management notifications etc would continue to be sourced through the County Council website and through County Council social media outlets.
17. It is intended that the Authority will retain a contract and performance management team to would oversee and manage the contractual arrangements and the residual functions. Resources would be retained by the Authority to fund this function.

18. Vehicles, plant and machinery, and other assets used to deliver the highways services would remain in the ownership of Nottinghamshire County Council (NCC) and leased to the Company for the remainder of its useful life, however, replacement of assets would be the responsibility of the CORMAC Group.
19. The new company would operate from the existing highways and fleet management bases and where necessary the buildings would be sub-let to the new company who would be responsible for utility charges and other direct service charges for the first 2 years of the contract.

Ancillary Matters

20. CORSERV would make a charge to the new company for support services and a proportionate charge for use of their existing systems and management support as detailed in the table below. Final costs would be negotiated as part of the contract arrangements but indicative costs have been accounted for when calculating the benefits of the proposed arrangements and would be serviced within the overall annual budget allocation.

| Estimated Charges payable to CORSERV | £000 p.a. | |
|--------------------------------------|-----------|-------------|
| Governance Fee | 50 | |
| Use of financial system | 66 | for 4 years |
| Support Services costs | 700 | year one |

21. The Council will be smaller as a result of transferring staff to the new company. Consequently overhead costs will be spread across the smaller remaining Council. This will result in an increase in unit costs when compared with other authorities until further changes can be made in the medium to longer term.
22. The position with regard to pension liabilities has been considered by a pension actuary. The Council would take responsibility for the historical pension deficit relating to the transferring staff, and the company scheme would commence on a fully funded basis. The company would assume responsibility for any future deficit. There is an annual pension contribution shortfall of circa £175k due to these adjustments. There is the option to obtain a bond to the value of £7.5m to protect the pension position. However, this would be an expensive proposition and an alternative arrangement to agree a joint guarantee between Cornwall Council and NCC would offer similar protection and is being developed. This should avoid the need to fund working capital but would be a potential liability for the Authority should the liability materialise.
23. Each party is meeting its own legal costs. Funds are also available within the Transformation fund for mobilisation estimated to be in the order of £0.6m.
24. There would be some post reductions to meet the savings that are predicated in the Medium Term Financial Strategy (MTFS) as part of the set-up of the Company. Whilst it is hoped that compulsory redundancies can be avoided, any redundancy costs related to former NCC staff up to October 2017 would be the responsibility of the County Council. However, a cap would be agreed with CORSERV to ensure any such costs are affordable and manageable.

25. The County Council would continue to handle insurance claims arising on the highway for the first 12 months of the contract, except where the claim is as a result of a clear failure by the company. Thereafter it is proposed that the new company will take responsibility for such claims (without the Authority delegating its statutory responsibility).

Governance

26. In December 2014, a Member Reference Group was established to consider and oversee the work in relation to the establishment of a Joint Venture Company. It is proposed that this Member Reference Group continues and meets regularly to monitor and oversee the ongoing establishment of the new company. In addition, Corporate Leadership Team (CLT) would undertake regular reviews in accordance with current practice for all Redefining Your Council (RYC) programmes of work.

27. Once the company is established it would be governed by its board of Directors. In order to avoid potential conflicts of interest it is proposed that the Authority's representation on the Board is through Officers not elected members. The Board for the new company would consist of four statutory and voting directors: two non-executive directors from CORSERV and two non-executive directors from the County Council. The proposal is that the County Council non-executive directors would be the Chief Executive and the Section 151 officer. It is also proposed that the new Company's Managing Director and Operations Director would be on the Board. These appointments will be made jointly by CORSERV and the County Council's NEDs. A range of reserved matters would be established in the contract on which unanimity would be required. Appendix 1 provides more detail on this.

28. As detailed above, Cornwall Council would establish CORSERV as a new wholly owned intermediate holding company when authority to establish the new company has been agreed by both Councils. On 12 May Cornwall Council Cabinet will consider a report recommending the establishment of the JV. When CORSERV is established it is proposed that the Chief Executive of the County Council sits on the Board of CORSERV as well as the Board of the new Company.

29. Elected members would receive regular reports, via the Transport and Highways Committee in relation to contract performance of the new company. The County Council will continue to set Highways policy and strategy, will determine priorities and will approve the Highways Capital Programme.

The Benefits

30. The primary benefit from the establishment of these new arrangements would be the long term sustainability of a quality highways service. This would predominantly be achieved by increasing the commerciality of the service. This would include greater cost control and transparency, driving efficiency and productivity benefits, operating in a more agile and flexible way and all linked to access to and use of a well-established and successful commercial bid team. Current estimates of efficiency and productivity benefits rise to circa £3m after 2-3 years. A breakdown of the figures is enclosed at Appendix 2.

31. The company is predicted to increase its external earnings year-on-year up to the maximum permissible, under the Teckal legislation, of up to 20% of its turnover (circa £10M). The forecasted assumption is that the new company would achieve £5m of external income by Year 2. 50% of profits accrued would be returned to the County Council. In addition the company would be committed to share the benefit of further efficiency and productivity improvements through a rebate with the County Council, as CORMAC has done with Cornwall Council.
32. External income would also help to maintain and develop the skill base and sustainability of the overall service, as around 40% of cost is related to staff. This is how CORMAC has successfully grown their business and employment over the past 3 years. With business growth CORMAC have also been able to invest in the development of apprentices (50) and graduate trainees.
33. The delivery of the savings already included as part of the MTFs (£1.1m between 2016-2018), would be the responsibility of the new company and the budget allocation for the new company would reflect these savings. This would be delivered through changes to operational practice and productivity improvements. The savings required by the end of 2015/16 will be made by the current highways division.
34. For this Joint Venture to be successful and viable it is important that all parties derive benefit from the arrangement. For the County Council this would be the sustainability of a quality service and access to commercial knowledge and expertise, for CORMAC it is the ability to grow their enterprise and more cost effectively share capability and resource, for Cornwall Council it is a share of the overall profit derived from the Group.

Other Options Considered

35. The Authority could decide to retain the current in house delivery model but for the reasons set out in the report this is not sustainable in the long term without severe cuts to service provision which would have an operational and reputational impact and may mean that the Authority is unable to fulfil its statutory duty in relation to Highways provision.

Reason/s for Recommendation/s

36. To provide a sustainable way of meeting the financial challenges facing the Highways and Fleet management services while retaining a good level of service.

Statutory and Policy Implications

This report has been compiled after consideration of implications in respect of crime and disorder, finance, human resources, human rights, the NHS Constitution (Public Health only), the public sector equality duty, safeguarding of children and vulnerable adults, service users, sustainability and the environment and ways of working and where such implications are material they are described below. Appropriate consultation has been undertaken and advice sought on these issues as required.

Financial Implications

These are described in the body of the report and at Appendix 2.

Human Resources Implications

Approximately 690 staff would transfer to the new company under TUPE regulations. The transfer will take place in line with legislative requirements and will draw on existing good practice and experience of setting up other arms-length organisations and TUPE transfers of staff.

A number of briefing sessions have taken place with affected staff involving senior managers from the Council and Cormac and HR representatives and a set of frequently asked questions made available to respond to general staff enquiries. Ongoing dialogue with staff and support will continue to be provided in the period up to transfer; with staff having access to the usual range of support mechanisms.

The recognised trades unions have been involved in the staff briefings and meetings have also taken place between NCC, Cormac and trades union colleagues. Trades union representatives from Nottinghamshire have also had separate meetings with trades union representatives from Cornwall; facilitated by the Council.

Public Sector Equality Duty implications

An equality impact assessment has been undertaken and is available as background paper to this report.

Implications for Service Users

As described within the report access by the general public to highways would remain via the CSC, as at present. The new service delivery model would ensure high quality highways services throughout Nottinghamshire for the foreseeable future.

Implications for Sustainability and the Environment

It is not expected that there would be any adverse implications as the Council will retain responsibility for Policy

RECOMMENDATION/S

It is recommended that Policy Committee:

- 1) Agrees to the establishment of a joint venture company for the delivery of Highways and Fleet management services, with CORMAC group.
- 2) Agrees that the target date for the new company to become operational would be 1 April 2016.
- 3) Agrees that the contractual arrangements with CORMAC group, including the establishment of CORSERV as a holding company, will be in line with the arrangements proposed within the report.
- 4) Agrees the Governance arrangements, including the board membership, as set out in the report.
- 5) Delegates to the Chief Executive, in consultation with the Group leaders and relevant officers, the responsibility for finalising the contractual arrangements.

- 6) Agrees that progress reports regarding the arrangements will be brought to Policy Committee as part of the general reporting arrangements agreed as part of Redefining your Council

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For any enquiries about this report please contact:

Constitutional Comments (SSR 08/05/2015)

37. The decisions set out in this report fall within the scope of decisions which may be approved by Policy Committee.

Financial Comments (TMR 08/05/2015)

38. The main financial implications arising from the creation of a Joint Venture Company with CORMAC to deliver Highways services are set out in the report and the appendices. It should be noted that there is significant uncertainty in both costs and benefits, and a number of risks, including around continuing insurance arrangements, which may have unknown but significant financial implications. Some of these may not become apparent until after the contract has begun – others will become clearer during due diligence work. However it should also be appreciated that there would also be significant risks associated with alternative options.

Appendices:

- 1) Information on Governance and HR.
- 2) Costs and Benefits table.
- 3) CORMAC - Working with You brochure

Background Papers and Published Documents

Except for previously published documents, which will be available elsewhere, the documents listed here will be available for inspection in accordance with Section 100D of the Local Government Act 1972.

- DfT's Highways Maintenance Efficiency Programme – Procurement Route Choices for Highway Maintenance Services - 2 August 2014

Electoral Division(s) and Member(s) Affected

- All