Establishing a local authority controlled company

Business case and implementation plan

South Hams District Council and West Devon Borough Council

23 June 2016

Private and confidential

Ms Sophie Hosking
Executive Director,
Service Delivery and Commercial Development
South Hams District Council
Follaton House, Plymouth Road, Totnes

23 June 2016

F014SHWD Management Consultancy Services (South Hams and West Devon)

Dear Sophie,

Business Case

Please find enclosed our Report setting out our Business Case and Implementation Plan content, outlining our findings in respect of the potential establishment of a Local Authority Controlled Company (LACC) for the delivery of existing services back into South Hams District and West Devon Borough Councils. This has been developed in accordance with the scope of our engagement, dated 29 March 2016, including concentrating on a comparison between the two key options under consideration:

- "As is" – The continuation of the current arrangements of in-house service delivery with some outsourced services (e.g. Leisure Centres and the West Devon waste collection, grounds maintenance and street cleansing service);
- "Transferring all Council services to a LACC" – where the LACC is jointly owned by South Hams District and West Devon Borough Councils. This does not include transferring the Elections Team, Democratic Services or the Strategy & Commissioning function to the proposed LACC.

In undertaking this engagement we have considered various sources of information, including: our internal network; existing information provided by the Councils and publicly available information. We have not validated the information provided to us by your or by third parties. We have also made assumptions (highlighted as appropriate) where information could not be sourced or provided.

This Report has been developed for the sole consideration of South Hams District and West Devon Borough Councils (the Councils) and, if this were to become the Business Case, it should be adopted by the Councils, with appropriate reference to PwC input. This document should not be provided to any other parties as our duty of care with regard to our engagement is to the Councils and to no other party.

Except for an overall legal review, the provision of legal advice was not included as part of our scope of work for this engagement. We recommend the Councils seek legal advice with regard to the items discussed and considered in this report should they wish to proceed to the next phase.

PricewaterhouseCoopers LLP, 2 Glass Wharf, Bristol, BS2 0FR
T: +44 (0) 0117 955 7779, F: +44 (0) 0117 309 2005, www.pwc.co.uk

We have enjoyed working with you on this engagement and I will be pleased to answer any further questions you may have.

Yours sincerely,

Paul Brewer
Partner
paul.k.brewer@uk.pwc.com
T: +44 (0) 131 260 4263

Important Note

This Report has been prepared by PricewaterhouseCoopers LLP ("PwC") for South Hams District and West Devon County Councils ("Councils"), under the terms of the Council's engagement letter with PwC dated 29 March 2016 (the effective date) (the "Engagement") and its contents are strictly confidential.

This Report contains information obtained or derived from a variety of sources as indicated within the report. PwC has not sought to establish the reliability of those sources or verified the information so provided. Accordingly no representation or warranty of any kind (whether express or implied) is given by PwC to any person (except to the Councils under the relevant terms of the Engagement) as to the accuracy or completeness of the report. Moreover the report is not intended to form the basis of any investment decisions and does not absolve any third party from conducting its own due diligence in order to verify its contents. For the avoidance of doubt this Engagement is not an assurance engagement and PwC is not providing assurance nor are the services being performed in accordance with the International Standard on Assurance Engagements 3000 (ISAE 3000).

PwC accepts no duty of care to any person (except to the Councils under the relevant terms of the Engagement) for the preparation of this Report. Accordingly, regardless of the form of action, whether in contract, tort or otherwise, and to the extent permitted by applicable law, PwC accepts no liability of any kind and disclaims all responsibility for the consequences of any person (other than the Councils on the above basis) acting or refraining to act in reliance on the briefing or for any decisions made or not made which are based upon such report.

In the event that, pursuant to a request which the Councils receive under the Freedom of Information Act 2000 or the Environmental Information Regulations 2004 (as the same may be amended or re-enacted from time to time) or any subordinate legislation made there under (collectively, the "Legislation"), the Councils are required to disclose any information contained in this report, it will notify PwC promptly and will consult with PwC prior to disclosing such report. The Councils agrees to pay due regard to any representations which PwC may make in connection with such disclosure and to apply any relevant exemptions which may exist under the Legislation to such report. If, following consultation with PwC, the Councils discloses this report or any part thereof, it shall ensure that any disclaimer which PwC has included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.

Table of Contents

1. Executive Summary

1.1. Introduction

This Report has been developed to meet South Hams District Council and West Devon Borough Council Project specification requirements, comply with the Local Government (Best Value Authorities) (Power to Trade) (England) Order 2009 (SI 2009/2393) and also the Treasury's Greenbook business case guidance.

1.2. Strategic Case

The strategic case demonstrates that the Councils' LACC proposal addresses a strategic need:

- Local government is set to face a funding gap of £9.5 bn by 2020. With limited scope for further efficiencies, this can only put at risk valued public services;
- PwC's review identified that the spectre of financial failure across the sector looms large, with nine out of ten Chief Executives believing that some local authorities will get into serious financial difficulties in the next five years;
- The collective budget gap from 2017/18 to 2020/21 for South Hams District Council and West Devon Borough Council is anticipated to be in excess of £2 million; and
- Local authorities see a way ahead through joint working and many are already working closely together and with other local partners to reform delivery and funding of local services by managing demand and agreeing joint objectives.

1.3. Economic Case

The economic case demonstrates that the LACC proposal can offer value for money:

- There is market potential that the current operating model is not able to capitalise on in an effort to offset the projected future funding gap;
- There are a range of potential contracts coming available in the medium term, giving time to develop commercial and tendering skills;
- The options assessment did not consider increasing charges or reducing services, but did consider a range of options for delivery of services through the current operating model;
- The 'As Is' approach does not provide opportunity to generate additional external profit to offset the cost of service provision;
- There are potential management efficiencies to be made as a result of the LACC providing delivery of waste management across both Councils and options to integrate waste services in West Devon should be incorporated into any potential LACC.
- A Multi-Criteria Assessment (MCA) was utilised to qualitatively assess the options of 'As Is' v 'LACC'. The LACC limited by shares scored highest. This option involves a combination including:
    - In-house provision of member services and communications to be retained by the Councils and managed by Strategy and Commissioning;
    - Continue with outsourced contracts for leisure services etc. These are to be retained by the Councils and managed by Strategy and Commissioning; and
    - The LACC will deliver Customer First, Commercial Services (including waste services) and Support Services to the Councils initially. Once T18 transition has been embedded within the LACC and it has been demonstrated that contracts have been bid for and won, there are opportunities to offer services to additional third parties.

1.4. Commercial Case

The commercial case demonstrates that the LACC proposal is commercially viable:

- The Councils are able to establish a LACC within a company structure limited by shares that appropriately allocates roles, responsibilities, voting and returns to the Councils;

- The commercial transition phase will need to focus on contract governance, including the novation of existing contracts, as the majority of the current operational structure, as established as part of the T18 Programme will remain as is;
- Shareholders agreement in the LACC should provide for different shares that enable equal voting and returns based on utilisation of services and assets, as well as terms for share sale, exit and share buyer controls;
- Governance and management reporting and responsibility will change but the operating model is unlikely to require additional change;
- Key areas include:
  - Corporation Tax: There is potential to obtain exemptions from HMRC for trading with the Councils, meaning that tax implications are only attributable to revenue generated external to the Councils;
  - VAT: It is envisaged that all services attract VAT and although the LACC does not have as favourable VAT exemptions as the Councils, it is unlikely irrecoverable VAT would have any adverse impacts on the Councils;
  - Employee tax: Employee taxes are likely to remain the same, although potential for 0.5% apprenticeship levy from April 2017, if the pay bill of a public (e.g. Council) or private body (e.g. LACC) exceeds £3m each year;
  - Pensions: The LGPS fund is likely to require some form of guarantee from the Councils with regard to their existing pension liabilities; however, this should not increase the cash requirement within the LACC; and
  - Accounting: The LACC will require audited financial statements to be developed, which will be an additional cost as each of the Councils will still need to maintain their own financial records.

1.5. Financial Case

The financial case demonstrates that the LACC proposal is affordable:

- There will be set up costs of c£400k relating to the establishment of a LACC;
- There will be additional on-going costs of c£60k per annum relating to the running of a LACC;
- There are opportunities to generate ongoing third party profits (c£<< figures removed – commercially confidential>> a year) from April 2020. Additionally, there are potential savings in the cost of West Devon waste management by providing the service within the LACC (c£<< figures removed – commercially confidential>> a year). This additional saving only applies to West Devon and accounts for the shorter payback period than South Hams (see Appendix 6.6); and
- The net result could be an unindexed c£<< figures removed – commercially confidential>> a year (c£<< figures removed – commercially confidential>> for South Hams District Council and c£<< figures removed – commercially confidential>> for West Devon Borough Council), contributing to a payback of the set up and ongoing costs by 2022 for South Hams District Council and 2020 for West Devon Borough Council (see section 6.4).

1.6. Management Case

The management case demonstrates that the LACC proposal and target date of 1 April 2017 is achievable (notwithstanding the decision to be made in respect of the West Devon waste service):

- The LACC provides:
  - a level of flexibility to respond to future market conditions;
  - is deliverable and appropriately allocates and shares risks across the Councils;
  - has greater risk from set up costs; and
  - presents greater opportunities to generate revenue in the future to offset the project funding gap
- An implementation plan includes:
  - Seeking legal advice on establishment;
  - Developing calculations for pensions; and
  - Application to HMRC for Corporation Tax exemption.

1.7. Summary

Our assessment concluded that:

- There are clear strategic imperatives that support the development of innovative solutions to the projected future funding gap;
- The remaining 'As Is' option is unlikely to be a sustainable long term solution with the additional risk of not taking action potentially constraining the Councils to increasing taxes or reducing services;
- The Councils have established an effective operating model, through T18, delivering all services end to end through Customer First, Commercial Services and Support Services with a clear steer and monitoring interface provided by Strategy and Commissioning and functional allocation of responsibilities for services delivery;
- This is an appropriate platform from which to continue the development of a LACC;
- There are potential market opportunities available to the Councils within their local regions, primarily with adjacent Local Authorities and other Public Sector entities, but also some private sector opportunities;
- The establishment of a LACC:
  - Enables the Councils to build upon the structural changes made as part of the T18 Programme;
  - Will incur setup costs of c£400k that should be paid back by April 2020; and
  - Presents opportunity to generate additional revenues not available under the 'As Is' option if the identified risks are managed appropriately.

We recommend that the Councils:

- Seek confirmation / guidance from HMRC regarding an exemption from paying Corporation Tax on profits related to income derived from services provided to the Councils. This should be undertaken prior to incurring further significant cost as it is fundamental to the assumptions within this report;
- Seek confirmation / guidance from LGPS on how the current pension deficit should be treated;
- Obtain legal advice and support to deliver the proposed corporate and associated share structure of the LACC to ensure that it meets both the governance and spend requirements;
- Obtain legal advice in relation to the Councils' vires to trade the identified services, and ensure LACC constitution has the flexibility required for future change in scope if envisaged as part of the LACC strategy;
- Obtain legal advice to confirm that the business plan conforms with State Aid requirements and public procurement regulations;
- Obtain legal support and advice in relation to Pensions, TUPE and employment matters; and
- Subject to confirmation of the above bullet points that the Councils proceed with establishing the LACC.

2. Introduction

2.1. Context

South Hams District Council and West Devon Borough Council ("the Councils" or "they") have been shared service partners since 2007. As two of the very first Councils to share a Chief Executive, the Councils have been bold in challenging the traditional local government model and have always been at the forefront of radical change and innovation. Shared services (through sharing staff) has now yielded over £7.7 million in savings across the two Councils since 2007, with each Council generating ongoing savings of over £700,000 every year.

The Councils engaged PwC ("we"), under the terms of the engagement letter dated 29 March 2016, to work with them to develop a business case and implementation plan to determine whether or not to proceed with the setting up of a Teckal[1] compliant Local Authority Controlled Company (LACC). They have previously commissioned work that compared the options of 'As is' against an 'LACC' and have also considered and discounted a number of other options.

The Councils are seeking to make a decision by mid-2016, in time to respond to the forthcoming conclusion of the West Devon waste contract with FCC in March 2017. For completeness, this Business Case has considered:

- The previous assessment undertaken by Grant Thornton, including:
  - Options appraisal for a Local Authority Controlled Company;
  - Options appraisal for waste services in West Devon.
- The current context including political drivers and policy directions, including Devolution;
- The market potential for services provided by the Councils; and
- And we have worked with the Councils to assess a broader number of options.

2.2. Collaboration

The Councils signed a Collaboration Agreement in March 2015. There are some key principles from this agreement that have influenced the assessment and development of this report. The key principles include:

- Each Council has an equal standing, regardless of size or financial contribution;
- The Councils retain their independence as separate local authorities with separately elected members;
- Each Council retains the right to set its own priorities, service levels and outcomes; and
- Achieving net financial savings, including the generation of income, where it is within the power of the Councils.

2.3. Objectives of our engagement

The objectives of the Business Case are to identify and test the strategic fit of options to take forward. In undertaking this engagement we have sought to:

- Confirm the drivers and need for change as identified by the Councils;
- Clearly define the potential scope of services to be provided by the new entity (including the future of West Devon waste services);
- Provide an analysis of potential business growth, market share, income generation and trading opportunities;
- Identify and assess the technical options available, in particular, whether a LACC is flexible, sustainable and represents value for money;
- Identify the commercial and tax implications of the preferred option;
- Identify and assess the set-up costs, ongoing costs and revenue implications of the preferred option;
- Identify the change management requirements and implementation plan for the preferred option; and

---

[1] Note references to Teckal compliant companies for this Business Case and Implementation Plan, includes the controlled persons conditions and exemptions in Regulation 12 of the Public Contract Regulations 2015

- Recommend an option for the future provision of Council services based on the above information.

2.4. Our approach to this engagement

This engagement is comprised of two phases including:

1. Business Case and Implementation Plan:

To meet the requirements of this phase we adopted the Treasury 5 Case Modelling approach (Appendix 2.1). The primary purpose of Phase 1 was to provide sufficient detail to enable a decision and provide a recommendation on proceeding to Phase 2. Additionally, we also gave consideration to the key tasks to be undertaken in Phase 2.

2. Implementation and establishment:

If Phase 1 results in an approved Business Case for a LACC, Phase 2 is to include:

- Change management: Change readiness and impact assessments and transition strategy;
- TUPE and payroll requirements, calculations and process commencement;
- Pension administration: Calculations on new body contributions, deficit allocations and advice on new body;
- Financial support and advice: Accounting treatments, commercial pricing, VAT registration, taxation, Key Performance Indicator development, insurances and financial policies;
- ICT systems and Resources: ICT strategy and service agreements, ICT governance and engagement with Civica;
- Financial and operational controls and assurance framework: Key financial controls, responsibilities, accountabilities, processes, risk framework and assurance arrangements including risk governance;
- Recruitment: (where required) job descriptions, skills and benchmarking;
- Project Management and implementation: Developing management plan and delivery team and managing risks, issues, changes; and
- Legal advice: Development of the articles of association, service delivery and other contracts including shareholder agreements, pensions, leases/licences etc.

2.5. Constraints

This Report has been developed over a 7 week period and is based on a number of assumptions, which are identified throughout, where relevant. In undertaking this assessment we have not considered other options to address future deficits, such as increasing council charges or other levies, nor have we considered service redesign or service reductions.

We have not been asked to validate the outputs of the T18 Programme and it is assumed that the majority of the available efficiencies have been, or are being realised. The T18 Programme has already delivered significant savings through the redesign process and it is assumed that the current delivery model is not separable; therefore, no further redesign is being considered as part of this engagement, other than the insourcing of the current West Devon waste and cleansing services into the LACC.

We have not undertaken an assessment of the current skills and capacity of the proposed management team, or their ability to deliver a successful LACC. Accordingly, there may be additional skills required that are not available currently and we would recommend a skills and capacity analysis is conducted as part of any subsequent mobilisation period, so that any additional requirements can be identified and addressed in a timely fashion.

We have not considered the potential implications of the outcome of the referendum on European Union membership.

2.6. Dependencies

A number of dependencies were considered in developing this report, including:

- The West Devon waste services contract with FCC is due to expire in March 2017. In discussion with the Councils, we have considered the high level implications of four options. These are at Appendix 2.2; however, throughout the report we have assumed that the intention is to transfer in the waste and street cleansing services at some point, should the LACC be formed;

- <<This information has been removed due to commercial sensitivities>>
- The Councils are currently in re-procurement for a leisure services contract which is likely to be a long term contract (25 years). This would be retained by the Councils and managed by Strategy and Commissioning.

3. Strategic Case

3.1. Introduction

The Strategic Case seeks to demonstrate that there is a need for a new approach to service delivery across the Councils, that the objectives are clear and that there is a clear case for change. The purpose of this section is to:

- Identify the strategic drivers and policy alignment of the initiative;
- Demonstrate the case for change for a new service delivery framework; and
- Consider the consequences of inaction and the risk of not proceeding.

3.2. Strategic Context

The Local Government Association paper, English Devolution Local Solutions For A Successful Nation (2015) identified that the Government has set out a long-term agenda for economic and social reform. Through its proposals for devolution in England, the Government has already recognised the principle that national prosperity can be enhanced by vibrant local democracy, as councils work with residents and businesses in their communities to provide the services people need and expect. The paper outlines that by working together, central and local government can deliver £11bn in savings through radical reform.

The Local Government Association paper, Under Pressure: How councils are planning for future cuts (2015) identifies:

- Councils are currently half way through a scheduled 40% cut in funding from central government. Having delivered £10bn of savings in the three years from 2011/12, local authorities have to find the same savings again in the next two years. As a result of these cuts, councils in many areas will not have enough money to meet all their statutory responsibilities;
- The Local Government Association paper, Our Future Funding Outlook model predicts that, due to protected services, the amount of money available to deliver some of the most popular local services will shrink by up to 66% by the end of the decade. This is likely to result in asignificant reductions in the help that councils can provide to local businesses; and
- Councils across England are preparing strategies to help mitigate these pressures. Local circumstance dictates what options are available for quick cost savings or income generation and the nature of the decisions that need to be made to achieve a sustainable financial position.

The paper also identified 2016 as a year when many councils will have to make very difficult choices about which services to prioritise. Some services have already been reduced and may need to be cut altogether. In order to avoid cuts to services, authorities are increasingly looking for ways to restructure service delivery to ensure that services remain fit for purpose in the context of smaller budgets.

PwC undertake an annual survey of 100 Chief Executives and Leaders of local authorities and the 2015 'Local State We're In' asked about the challenges facing local government and their responses to them. It found that councils have been successful in managing the significant cuts to date, but that local authorities are now facing challenges on all fronts. Financial pressures continue while demand and public expectations grow with the way ahead being challenging, but full of opportunity that the sector has the confidence to tackle and face.

PwC's research into local government identified:

- Only one in ten council Chief Executives are confident their council can protect frontline services in the face of continued austerity over the next five years;
- The spectre of financial failure across the sector looms large, with nine out of ten Chief Executives believing that some local authorities will get into serious financial difficulties in the next five years; and
- 80% of our respondents believe that some local authorities will fail to be able to afford to deliver the essential services residents require in the next five years.

Importantly, Chief Executives and Leaders have recognised the need to do things differently and the realisation that councils cannot operate in isolation, partnership working has also risen up the agenda.

> *"It is clear, speaking with Council Leaders and their Chief Executives, that Councils are now considering more radical options – from rethinking relationships with customers and communities and better use of digital technologies, to deeper collaboration with partners. The business model of the public sector is changing rapidly as decision makers are considering what is the role of the public sector within a local area.*
>
> *Local authorities have largely responded well to the budget gap of the last four years. They are now anticipating having to do the same again, with less and less certainty of how to achieve this. We have no doubt that the future business model for public services will change significantly in the next four years - and those leading the sector in localities will be the ones who will deliver this new model – changes won't all necessarily be centrally driven."*

Chris Buttress
PwC partner and local government leader comments

The Future Funding Outlook for councils 2019/2020 (Interim 2015 Update) identified that:

- Councils are continuing to balance their budgets and fulfil their statutory obligations as well as delivering a range of services to promote growth and community cohesion, in spite of continued funding cuts and expenditure pressures; and
- The challenge cannot be solved by back-office efficiencies alone.

An analysis of projected income and expenditure trends of Local Authority funding shows that the overall funding gap starts at just over £3bn in 2015/16 and reaches over £10bn by 2018/19, before shrinking to **£9.5bn** by 2019/20. This equates to a **reduction of approximately 20% in real terms**, see Appendix 3.1.

Local authorities also receive funding from the Non-Domestic Rates they collect from within their area. Before April 2013, all business rate income collected formed a single, national pot, which was then distributed by the Government to councils in the form of formula grant. The Local Government Finance Act (2012) gave Local Authorities the power to keep half of the business rates in their area, the other half being used by Central Government to provide additional grant funding.

The Business Rate Retention: the story continues (March 2015) states that the primary challenges are the level of financial risk that councils face due to appeals and the dependence on a small number of large businesses for a significant proportion of their business rate income. It also identified that mechanisms which were designed to encourage local authorities to grow their economies (e.g. reliefs and discounts) are a counterproductive feature of the new system.

In summarising the national context, there are significant policy drivers of Central Government funding that will continue to influence the way local authorities deliver services and value for money.

PwC view:

- ***The problem is clear that local authorities are facing increasing funding pressures.***
- ***Local authorities will need to consider and change the way they deliver services, not just individually, but collectively.***

3.3. The Case for Change

3.3.1. Building on a history of driving change

The Councils have a successful track record of reducing costs through shared services, whilst improving service delivery and commenced a joint Transformation Programme 2018 (T18) in December 2013, to deliver a new service delivery model (Appendix 3.6) They continue to face significant reductions in Central Government funding and the T18 Programme will continue to develop their financial resilience and reduce the risk of having to make annual budget reductions that would inevitably impact upon front line services.

South Hams and West Devon Councils are pioneering a new model for local government which could be applied to other local authorities, irrespective of the scale, acting as a catalyst for extending shared services without undermining each participating Councils' democratic independence.

They are now providing their services in an entirely new way and have become more flexible and customer focused using the latest technology. Services have been redesigned around customers and communities and, as a consequence, all departmental silos removed. This involved the re-engineering of over 500 business processes and the sharing all of corporate services and information technology systems. The first phase of the programme went live in September 2014, with the main phase of the programme delivered in 2015.

At its heart, the transformation programme is one of cultural change. This radical transformation has been the most significant change in the way that the Councils work for more than 40 years. The Councils' non-manual workforce is now approximately 30% smaller, with all staff roles adapted to be flexible and responsive to the needs of the customer. Officers from different areas of the Councils now work within the communities to improve the service for the customer and reduce the need for office accommodation.

The principle of the new model is a cross functional organisation with matrix management, which can be flexible, respond to the needs of the customer, deliver good quality services, and, ultimately, generate its own income. The model is now split into two distinct parts; the Strategy and Commissioning side, which sets policy and contains the governance structure and then the Service Delivery and Commercial Services side, which delivers the services. The Councils have reduced the work force by 30%, and the T18 Programme has achieved joint savings of £4.7m to date, thanks to these major changes.

West Devon Borough Council and South Hams District Council were recognised on a national stage in March 2015, receiving the Gold Award for 'Delivering through Efficiency' and the Silver Award for 'Council of the Year' at the Improvement and Efficiency Social Enterprise Awards (iESE). The awards celebrate Councils who are developing new ways of working and transforming public service delivery to improve services and reduce costs.

PwC view:

- ***The Councils have made significant progress in responding to the funding constraints and they have determined that further work is required to identify additional opportunities to maintain service provision whilst delivering value for money.***

3.3.2. The future

The Councils have been bold in challenging the traditional local government model and have always been at the forefront of radical change and innovation. Shared services (through sharing staff) and consolidated services through the T18 Programme has now yielded over £7.7m in savings across the two Councils, since 2007.

Current Council budget projections (including a £5 council tax increase from 2016/17); however, identify a collective cumulative budget gap of over £2m from 2017/18 to 2020/21.

	2016/17 £	2017/18 £	2018/19 £	2019/20 £	2020/21 £
SHDC annual budget (surplus) / gap	(£767,995) – one-off	155,155	541,170	135,247	178,263
Cumulative SHDC budget gap over the four years from 2017/18 to 2020/21					£1,009,835
WDBC annual budget (surplus) / gap	(669,292) – one-off	506,617	571,781	17,823	(27,547)
Cumulative WDBC budget gap over the four years from 2017/18 to 2020/21					£1,068,674

3.3.3. Risk of not taking action

The risks to the Councils of not planning to address the projected future funding gap and taking further action could result in:

- Reductions in staff and/or services. At its extreme, this could result in ceasing to provide certain services and potential financial failure of the Councils;

- Not capitalising on the opportunities presented by other Local Authorities who have not planned for the future; and
- Not protecting local services if future changes to governance structures consolidates the number of Local Authorities in the South West Region.

A more detailed risk analysis is contained within Section 7 (Management Case).

PwC view:

- ***T18 Programme benefits are not enough to meet the projected funding gap and further action is required.***
- ***This Report is considering an option that could potentially offset some of the projected funding gap and position the Councils for a future where it could provide service to other local authorities that are looking for additional efficiencies and savings.***

3.4. Strategic Case Summary

The strategic case demonstrates that the Councils' LACC proposal addresses a strategic need:

- Local government is set to face a funding gap of £9.5 bn by 2020. With limited scope for further efficiencies, this can only put at risk valued public services;
- PwC's review identified that the spectre of financial failure across the sector looms large, with nine out of ten Chief Executives believing that some local authorities will get into serious financial difficulties in the next five years;
- The collective budget gap from 2017/18 to 2020/21 for South Hams District Council and West Devon Borough Council is anticipated to be in excess of £2 million; and
- Local authorities see a way ahead through joint working and many are already working closely together and with other local partners to reform delivery and funding of local services by managing demand and agreeing joint objectives.

PwC view:

- ***The future funding model for Local Authorities is uncertain.***
- ***Through the T18 Programme, the Councils have made significant savings; however these savings are not sufficient to address the future funding gap.***
- ***Consideration of a Local Authority Controlled Company is an innovative way of being proactive, rather than reactive.***

4. Economic Case

4.1. Introduction

The Economic Case seeks to explore the benefits of options available to the Councils in addressing the need for change. The purpose of this section is to:

- Outline the objectives of the LACC;
- Outline the market context and market potential for local authority services;
- Provide an overview of the current delivery model;
- Demonstrate the options and that they have been considered appropriately;
- Determine the option that presents the best value for money, i.e. the preferred option for delivering services and potential to generate revenue; and
- Identify the scope and elements of the new framework for service delivery.

4.1.1. Objectives

The following objectives for the new entity were developed in conjunction with the Councils, including:

1. Provide the comprehensive range of services required by the Councils and the community across the region in a sustainable manner;
2. Deliver the services required in an efficient and effective way, including reduced duplication;
3. Build on and further support the benefits already achieved through the T18 Programme;
4. Deliver service performance levels expected by the community;
5. Provide greater value for money for residents;
6. Allocate resources in a manner that addresses future funding constraints;
7. Be flexible and able to respond to the Council' changing needs and governance structures over time; and
8. Bring a commercial focus that generates revenues, profits and dividends to shareholders.

These objectives formed part of the options identification and assessment process.

4.2. Market Size

Identifying the market size and penetration potential for the range of services provided by the Councils presented a number difficulties, the key ones being with regard to scope, timing and locational influences. We established a high level assessment to try and quantify the market size for services provided by the Councils by considering other local authorities and their budget spend on services. This was then broken down further to focus on key services that could potentially be provided by the Councils.

Our research identified that the combined Local Authorities in the South West have an annual budget spend of approximately £4.6b, of which approximately **£780m** is the potential market for services currently provided by the Councils, Appendix 4.1. We also identified a range of contracts with a potential value **>£38m** within the South West area that are anticipated to be released to market within the next **4 years**, Appendix 4.1. Even if the Councils can claim a quarter of a percent of this market that equates to approximately £2m additional revenue.

PwC view:

- ***There is a significant spend by local authorities across the South West region.***
- ***The current spend is spread across a broad range of services and demonstrates that there is opportunity within the region for services currently provided by the Councils to be provided to other public bodies.***

4.2.1. Responding to the Market

In considering the potential for a LACC our approach involved:

- Reviewing existing LACCs to identify key characteristics;
- Considering potential regional Local Authority partners;
- Consider other public sector opportunities such as NHS, education/schools and other government agencies such as parks and environment; and
- Assessing potential private sector services.

LACCs

We undertook a desktop review of approximately 20 established LACCs and found:

- LACCs were generally established to realise efficiencies through a restructuring and to bring a commercial focus;
- These are primarily comprised of commercial services with opportunity to generate revenue including:
  - Waste management (including recycling and environmental services);
  - Health and Care;
  - Building, facility management and maintenance; and
  - Energy services.
- Entities were established to predominantly provide services locally; and
- Governance is important in providing clarity on roles and responsibilities of members and/or company directors.

Profiles are available at Appendix 4.1.

Regional considerations

We next considered the regional market opportunities with other Local Authorities. We understand that previous discussions with Torridge District Council were unsuccessful as they did not wish to participate in the T18 programme and shared services. We also understand that an existing relationship exists with Teignbridge District Council who provide specialised procurement, building control and training services to the Councils on a part time basis.

The proximity of other Local Authorities presents multiple opportunities either for the provision of services, or to form partnerships or joint ventures in order to leverage local operations. In the short term it is likely that operations will be focused locally, but longer term opportunities may be presented further afield e.g., Somerset and Wiltshire. An example of this happening successfully is Norse Group, established by Norfolk County Council who have established joint operations nationally.

A table summarising the key features across the South West is at Appendix 4.3.

It is of note that the majority of Local Authorities appear to outsource waste services. This is an opportunity for the LACC to develop third party revenues from other Local Authorities.

Other Public Sector Entities

In addition to Local Authorities, we considered potential for other public sector customers and their requirements for services that the LACC could potentially provide.

With an ageing population, forecast to increase in the future, the provision of health services in the South West region has the potential to expand. There are a large number of privately owned and operated hospitals and health facilities across Cornwall and Devon, with Nuffield Health and Ramsay two of the major providers. Consideration would need to be given to the service offering available to these entities, once a credible track record had been developed through the provision of similar services into other public facilities. There may also be opportunity to leverage waste and cleaning services in expanding into clinical waste treatment, as an example.

Also, in spite of the recent setbacks, the Government is continuing to drive increased autonomy in the education sector through increasing the number of academy schools. Schoolsnet outlines that across Cornwall and Devon there are approximately 730 preparatory, primary and secondary schools.

In addition to health and education, other government bodies include:

- The Department for Communities and Local Government;
- The Department for Business, Innovation and Skills;
- The Department for Environment, Food and Rural Affairs;
- The Food Standards Agency;
- The Department of National Parks, Sport and Racing;
- National Trust, English Heritage or other charitable organisations;
- Environment Agency; and
- Areas of Outstanding Natural Beauty.

These organisations have varying degrees of operation within the region and could present opportunity to provide a range of services.

Private Sector

We assumed that external opportunities in the region are likely to be limited in the near term. There could; however, be medium term opportunities, but market penetration will require commercial pricing and tendering capabilities, which may not currently be available within the Councils. These capabilities will be significant in the Councils ability to generate additional revenues.

A desktop review identified that there are existing suppliers of a range of the services to be provided by the LACC. The Councils would need to consider their unique selling proposition when engaging with the private sector to enhance their brand and improve their ability to compete established private sector suppliers.

In the short term it is considered that the Councils should focus on functions and areas that are more familiar, for example, other local authorities and/or other public sector entities within the Councils geographic area.

PwC view:

We observe the key differences between these examples and the Councils being:

- ***The Councils have already established a commercial operating model through the T18 Programme and, therefore, have an advanced starting point.***
- ***The Councils services have been restructured and efficiencies have been or are being realised meaning operational impacts are likely to be less complex than in other examples of a LACC.***
- ***We did not find examples of LACCs being established to provide majority/all services back to Councils.***
- ***The Councils case management operating model has clearly defined services thereby reducing the potential for duplication.***
- ***There is an opportunity to bid for and win contracts in sectors where the Councils currently provide services across the region.***

4.3. Current Model

The current operating model was created as a result of the T18 programme. This involved the redesign of all services within the Councils across:

- Customer First
- Commercial Services
- Support Services
- Other functions.

Appendix 4.4 shows the split of the services and headcount across the different areas. Under the proposed LACC structure, Customer First, Commercial Services and Support Services would transfer to the LACC, with Strategy and Commissioning retained by the Councils.

The Councils advised significant work has been expended on establishing the current operating model through the T18 Programme. Any further restructure of the model may cause substantial disruption and is not guaranteed to realise any material additional efficiencies. We have not considered restructuring the operating model in detail as part of this engagement; however our assessment does not preclude the Councils from identifying opportunities to improve the operating model in the future.

The key features of the current operating model established through the T18 Programme are:

- The Councils share management and resources and deliver majority of services in-house;
- West Devon waste is contracted whilst South Hams waste services are in-house;
- Leisure services management is currently being procured and likely to be a long term contract of 25 years; and
- Current levers available to the Councils to drive change and realise efficiencies include; contracting for delivery of services (i.e. Leisure and West Devon waste), better asset utilisation and investment to generate income or cost management for efficiencies and productivity improvements.

While the Councils do generate some revenues through leasing out existing office space and charging for services within their existing structure, no additional profit generating revenue is generated from providing existing services to other parties. Where services are provided currently it reflects cost recovery at best. The majority of their revenue; therefore, comes from council taxes, business rates and government grants.

4.3.1. Building Control Partnership

The Councils are also members of the Devon Building Control (DBC) through a partnership arrangement across Teignbridge, South Hams, West Devon and Dartmoor National Park. The DBC Partnership is made up of two councillors from South Hams District Council, two councillors from West Devon Borough Council and two councillors from Teignbridge District Council. The Partnership is administered by Teignbridge District Council and meetings are held bi-annually at Teignbridge District Council offices, Forde House, Newton Abbot.

DBC provides a flexible building control service to businesses and householders for the design, approval and construction of buildings. DBC includes a professional team of chartered surveyors, fire and building engineers and provide clients with clear expert guidance on a range of construction projects. Although we have not investigated DBC's financial and operating practices or engaged with their customers to determine current profitability or market position; this demonstrates the Councils ability to be innovative and generate revenues from external sources through providing services valued by the market. The market analysis identified building control functions equate to approximately £1.7m per annum across the South West. DBC provides services to the market and may form the foundations of a pricing model that the LACC could leverage in future when tendering competitively in the open market.

In establishing a LACC, the Council could retain involvement in the DBC Partnership and manage it through Strategy and Commissioning; however, there are likely to be benefits of incorporating DBC functions within the LACC as the entity has an established brand and market revenue position that the LACC may be able to leverage or learn from throughout the transition phase.

PwC view:

- ***Consideration needs to be given to Teignbridge involvement and hosting of DBC. The Councils have already established a commercial operating model through the T18 Programme.***
- ***The Council have a range of options available and establishment of a LACC presents opportunity to negotiate with Teignbridge regarding their ongoing involvement and consideration of transitioning DBC to a subsidiary entity of the LACC.***
- ***Councils' services have been restructured and efficiencies have been or are being realised meaning operational impacts are likely to be less complex than in other examples.***

The current operating model provides the Councils with the platform to bid for opportunities presented by the market. Further changes in the operating model would not be sufficient to offset the projected future funding gap on its own, resulting in further consideration of options to address this.

4.4. Options Assessment

The Councils have already undertaken significant work in considering various options for service and required our analysis to compare the 'As Is' v 'LACC with all services transferred'. Our approach in assessing the options, as directed, included:

- Identifying the objectives in conjunction with the Councils;
- Reviewing the previous work undertaken provided by the Councils, including:
  - Operating company options;
  - Options for West Devon Waste and cleansing services.
- Undertaking a high level options assessment;
- Identifying and agreeing the assessment criteria with the Councils, including weightings;
- Assessing the options against a broad base of criteria; and
- Identifying shortlisted options to be considered further for quantitative impacts.

This section summarises the outcomes of the assessment, with the detailed results provided in Appendix 4.5.

4.4.1. Multi Criteria Assessment

A Multi-Criteria Assessment (MCA) was utilised to qualitatively assess the options. The assessment included scoring and ranking the options on both a weighted and unweighted basis to determine the relative impacts of each option.

The MCA of the options identified that the combined model, where the Councils retain Strategy and Commissioning, management of long term contracts (i.e. Leisure) and establish a LACC for Customer First, Commercial Services and Support Services, scored the highest on both unweighted and weighted scores, when compared to the 'As Is' model.

The table below is a graphical illustration of the results for each of the Strategic Categories. The detailed weighted and unweighted scores are at Appendix 4.5.

Key

○	Very high	◔	High	◑	Medium	◕	Low	●	Very low

Strategic Category	Strategic Fit	Social benefits and impacts	Governance	Commercial	Financial	Implementation and Delivery
Weighting	5%	10%	10%	25%	25%	25%
Base Case- 'As Is' with Customer First, Commercial Services, Support Service, contracted services for Waste in West Devon, Leisure	◔	◔	◔	◑	◑	◔
A Combined model (a combination of insource for Strategy and Commissioning, outsource for leisure, and LACC for Customer First, Commercial Services, Support Services)	◔	◑	◔	◔	◔	◔

4.4.2. SWOT Analysis

An analysis of the Strengths, Weakness, Opportunities and Threats (SWOT) was undertaken. The table below summarises these.

Shortlisted Option	Strengths	Weaknesses	Opportunities	Threats
'As Is' Base Case- 'As Is' with Customer First, Commercial Services, Support Service, contracted services for Waste in West Devon, Leisure.	• Understood delivery model. • All services directly controlled by the Councils. • Tax efficient operation through current legislation.	• Does not address projected funding gap. • Not fully commercial operations. • No major opportunity to generate additional revenues.	• Devolution with combined authorities where the District and Borough Councils join with larger Authorities.	• Impacts of Devolution with dilution of services or reduced control within a combined authority. • External funding reductions. • Business rates unknowns. • Potential to pay other Local Authorities.
A Combined model (a combination of insource for Strategy and Commissioning, outsource for leisure, and LACC for Customer First, Commercial Services, Support Services).	• Commercial focus which builds on the T18 Programme and could realise further efficiencies and costs savings. • Additional levers (i.e. pricing mechanism). • The Councils retain control through ownership. • Performance based mechanisms • Ability to innovate and potential to expand service offering (i.e. expand waste to include clinical).	• There is no precedent of other Local Authorities establishing a LACC for a similar operating model. • Arm's length control for the Councils. • Exit strategy required to ensure statutory service provision. • Potential increased tax burden. • Unlikely to generate additional external revenue for a number of years.	• Take on additional partners. • Generate additional revenues. • Apply for HMRC Corporation Tax exemption if trading solely with the Councils. • Better understanding and unit cost analysis.	• Central Government policy changes. • Policy or control changes within the Councils. • Staff and union action. • Future market conditions hard to predict.

The opportunities are further explained in 4.4.4 below.

4.4.3. Anticipated Benefits

The assessment highlighted a number of anticipated benefits from Option 6, including:

- Supports the Councils' visions and objectives of service delivery and obtaining value for money;
- The ability to operate commercially with mechanisms to respond to change and include new partners;
- Teckal procurement exemptions;
- Improved staff mix for the long term that delivers services locally;
- Opportunities to realise additional efficiencies through consolidated waste services across the Councils;
- Potential to generate additional revenues following transitional phase and skills development.

These benefits are further considered in the Management case.

4.4.4. Opportunities

There are a number of opportunities presented by considering establishing a LACC to provide services to the Councils, including:

- To help inform government policy on local service provision in the uncertainty of what Devolution will mean for Local Authorities;
- The ability to be innovative and establish operations that can capitalise on Local Authorities that are reactive, rather than proactive in addressing the projected future funding gap;
- To bring a commercial focus which builds on the T18 Programme that could realise further efficiencies and costs savings of parts that have not yet been fully scrutinised (i.e. grounds/building maintenance);
- Provides the Councils additional levers to address projected funding gap (i.e. pricing mechanism, efficiencies, economies of scale);
- To provide further clarity to the Councils through ownership and management agreements;
- Implementation of performance based mechanisms and culture in service delivery;
- The potential to expand service offering to the market in future (i.e. expand waste to include trade/commercial/recycling/clinical);
- To take on additional partners or establish joint arrangements with other Local Authorities;
- Generate additional revenues from other Local Authorities or Government agencies to offset costs of service delivery;
- Develop a better understanding of cost and implementation of relevant controls;
- Opportunities to realise additional efficiencies through the building control partnership and consolidated waste and street cleansing services across the Councils;
- Potential to generate additional revenues following transitional phase and skills development, including:

  - ‘know how’ i.e. the selling of experience and knowledge gained from the T18 transformation programme and the establishment of a LACC;
  - Support services (provision of administration services e.g. payroll);
  - Field services (e.g. provision of waste and building control services)

4.5. Options for West Devon waste services

FCC Environmental are currently contracted to West Devon Borough Council to provide waste collection, recyclable and street cleansing services for a period of 7 years, with an expiry date of 31 March 2017. As part of this contract, FCC utilise depots currently owned or leased on a long term basis by West Devon.

We have been instructed to assess the viability of establishing a LACC and consider the implications of incorporating these waste services (including street cleansing) into the LACC after the expiry date. We were briefed to look at the timeframe for incorporating the West Devon Waste and Cleansing contract into the LACC in terms of feasibility and cost, as well as exploring the alternative options for the delivery of the service. We considered efficiencies which might be gained through delivery of joint services through the LACC, whilst recognising the current individual service configuration.

We were informed by the Councils that without the establishment of a LACC, waste services in West Devon would continue to be outsourced and retendered. Although our engagement did not include any in depth analysis and/or service redesign, we have considered the previous work undertaken by Grant Thornton (GT), which identified a number of opportunities, and our assessment has focussed on maximising the benefits associated with incorporating these services into the LACC.

PwC view:

- ***The inclusion of waste and street cleansing services currently outsourced by West Devon Borough Council into a combined LACC will align service offerings across the Councils.***
- ***The inclusion of these services appears to represent an opportunity to generate some additional efficiencies, primarily through management, as waste collection would remain as is in meeting the needs and expectations of the West Devon community.***
- ***The inclusion of these services in the LACC improves the balance of services provided to the Councils by the LACC whereas the continuation of outsourced arrangements would significantly distort the value of services purchased by West Devon Borough Council from the LACC.***
- ***Financially the inclusion of waste and street cleansing services improves the payback period.***
- ***The assumption of no additional revenue for the LACC generated from third parties presents an opportunity to appropriately plan and not rush the process of incorporating within the LACC.***
- ***The establishment of a LACC is not dependent on inclusion of waste and street cleansing services in West Devon.***

Our assessment of waste and street cleansing services in West Devon found:

- That inclusion of these services into the LACC improves the overall offering of the LACC
- That inclusion of these services better represents West Devon Borough Council interest in the LACC as a proportion of the potential service fee
- The transition phase of the LACC does not need to be driven by these services as management mechanisms are available to respond to West Devon Borough Councils decision on its preferred option.

Additional detail can be found in the West Devon Waste Options paper available at Appendix 2.2.

4.6. Economic Case Summary

The economic case demonstrates that the LACC proposal can offer value for money:

- There is market potential that the current operating model is not able to capitalise on in an effort to offset the projected future funding gap;
- There are a range of potential contracts coming available in the medium term, giving time to develop commercial and tendering skills;
- The options assessment did not consider increasing charges or reducing services, but did consider a range of options for delivery of services through the current operating model;
- The 'As Is' approach does not provide opportunity to generate additional external profit to offset the cost of service provision;
- There are potential management efficiencies to be made as a result of the LACC providing delivery of waste management across both Councils and options to integrate waste services in West Devon should be incorporated into any potential LACC.
- A Multi-Criteria Assessment (MCA) was utilised to qualitatively assess the options of 'As Is' v 'LACC'. The LACC limited by shares scored highest. This option involves a combination including:

    - In-house provision of member services and communications to be retained by the Councils and managed by Strategy and Commissioning;
    - Continue with outsourced contracts for leisure services etc. These are to be retained by the Councils and managed by Strategy and Commissioning; and
    - The LACC will deliver Customer First, Commercial Services (including waste services) and Support Services to the Councils initially. Once T18 transition has been embedded within the LACC and it has been demonstrated that contracts have been bid for and won, there are opportunities to offer services to additional third parties.

PwC view:

- ***The 'As Is' option will not address the future funding gap without future intervention. If the LACC is not established then alternative strategies would be required.***

- ***There are likely to be efficiencies in bringing together the managed delivery of existing waste services.***
- ***The Local Authority Controlled Company using the current operating model presents opportunity to respond to a changing market and generate additional revenues to offset the projected funding gap.***

5. Commercial Case

5.1. Introduction

The Commercial Case seeks to demonstrate that the formation of a LACC is commercially viable with clear governance arrangements, appropriate financial and funding structures, can be implemented and operational responsibilities assigned appropriately. The purpose of this section is to:

- Determine the operational requirements of the preferred model;
- Determine the commercial structure/model including the key elements;
- Identify the charging mechanisms and commercial principles that are required to ensure value for money for delivery; and
- Identify accounting and tax impacts and interfaces.

This section also acknowledges that the Councils have previously received advice regarding a LACC option and also specific advice regarding the provision of waste services.

Additionally, we have sought to test the commercial requirements and identify if there are significant roadblocks that would preclude the Councils from further considering setting up a LACC.

5.2. Operational Requirements

The commercial considerations in this case are quite different to either establishing a new company or expanding services of a Local Authority. The key considerations for the commercial requirements include:

- The different levels of participation of the Councils:
  - Service use;
  - Asset use;
  - Financial return;
  - Voting rights.
- The flexibility to change and include new partners;
- The level of control;
- Teckal requirements;
- Pensions and TUPE;
- Tax implications.

5.3. Commercial Structure

The Councils are considering establishing a LACC which it controls and contracts with to provide and receive services. The LACC would be owned and controlled by the Councils and would need to comply with the Teckal control tests or now, and more significantly, Regulation 12 of the Public Contract Regulations 2015 (Public Contracts between entities within the public sector), making it possible to trade with external parties and provide flexibility for procurement. These are:

- The company should behave and be controlled as a department of the local authority;
- The major part of the Company's business must be with the local authority owner(s), so that public procurement exemptions can be accessed; and
- The conditions in relation to direct private capital participation in the LACC are met.

In practice, the Teckal trading exemption applies where in excess of 80% of the LACC's income comes from those who exercise control over the LACC Board.

Conceptually a LACC can offer:

- New opportunities and potentially greater reward compared to the current model;

- The potential to offset costs through generating additional revenue in response to a changing market; and
- The opportunity to build upon the culture developed as part of the T18 Programme to develop a more commercial operating model.

The establishment includes a different risk profile to the one the Councils are currently exposed to. As outlined above, the key focus is the ability to operate commercially and provide a value proposition in a competitive market.

The general trading power under Section 4 of the Localism Act 2011 requires the Councils to trade using a company structure:

- Company limited by shares;
- Company limited by guarantee;
- Industrial and Provident Society;
- An unlimited company; and
- Community Interest Company (for trading under section 4 of the LA 2011).

The company structure adopted by the Councils will depend to an extent on the services to be provided. Whatever level of trading activity is contemplated by a local authority, the activity can only be carried out by a company within the meaning of the Local Government and Housing Act 1989 (the "1989 Act"). Companies under the control of local authorities and subject to their influence are governed by the provisions in Part V of the 1989 Act. Part V of the 1989 Act is scheduled for repeal in its entirety by section 216 of the Local Government and Public Involvement in Health Act 2007 (the "2007 Act"). Section 212 of the 2007 Act introduces "local authority entities" in place of companies controlled by or under the influence of authorities, although an order under this section has yet to be made by the Secretary of State or Welsh Ministers.

Once the type of company structure has been decided, company formation can take place. Company formation is usually a straight forward process. For example, to set up a private company limited by shares a *Form IN01* needs completion and, with the company's memorandum of association and incorporation fee, filed with the Registrar of Companies. *Form IN01* sets out:

- the company's proposed name;
- type of company and members' liability (e.g. private company limited by shares);
- company's registered office address;
- proposed articles of association (if the model articles have been amended);
- details of first directors and secretary (if any);
- statement of capital and initial shareholding; and
- statement of compliance.

An option for the Council is the purchase of an off-the-shelf company, which would never have traded before yet is pre-registered with the Registrar of Companies and would be ready for immediate use.

PwC view:

- ***The current model is not able to take advantage of procurement and profit generating opportunities which would be available to a LACC.***
- ***The risks associated with operating a commercial entity are manageable and acceptable when considered against the potential benefits.***
- ***A LACC is able to operate commercially and, in satisfying the relevant 'tests', is able to generate additional revenue and provide services to the Councils.***

5.3.1. Ownership

Generally companies have one class of share, traditionally known as ordinary shares. The use of different share classes is increasing for a variety of reasons including, to vary the dividends paid to different shareholders or create non-voting shares. There are no real restrictions on the type or number of shares a company can have and in addition to ordinary shares, common share types are:

- preference shares which reflects the different contributions of the owners and the dividends they receive;
- non-voting shares which reflect the owners input or involvement, but not directly in the decision making;
- A and B shares to reflect or assign different voting rights between the owners; and
- shares with extra voting rights to reflect different shareholding and decision making requirements.

For the Councils it will be important to create a share structure that enables them to appropriately separate items such as control, voting and dividends to the extent that they are unlikely to be equal on all counts. Existing LACCs have been established in various forms within single councils or in partnership with others; although joint ownership presents some challenges, it does not preclude or restrict the establishment of a LACC.

PwC view:

- ***The Councils are seeking to establish the LACC under the same principles as their 2015 Collaboration Agreement. This would represent equal voting rights on matters that impact both of the Councils, therefore A Shares equate to 50/50 for each Council.***
- ***With regard to financial returns, we would propose they be based on the current budget contributions of each of the Councils. This is based on each Council receiving appropriate consideration for their asset contribution through the lease to the LACC and service utilisation for each Council is reflected in their respective service agreements with the LACC.***

5.3.2. Control and Voting

The Councils must retain control of the LACC to meet the requirements of the Teckal case and/or conditions for legal persons under Regulation 12 of the Public Contracts Regulations 2015. All parties need to be clear where voting, control and returns sit within the structure and the shareholders agreement provides the opportunity to clarify this.

The LACC will also require a Board of Directors (and potentially a Joint Ownership Committee) with clearly defined roles and responsibilities. This is to ensure that their purpose is clear and that it is successful in providing services to both the Councils and, potentially, other parties in the future. Membership of the Board (and Committee) requires further consideration as there are decision that need to be made before establishing a LACC, including:

- Whether there should be an Independent Chairperson and whether the scope of this as a part-time or full-time position;
- Whether a new Managing Director is required to achieve long term success of the LACC model and whether, for example the Executive Director, Service Delivery and Commercial Development could fulfil that role in the interim period where the focus is on service delivery back to the Councils;
- The selection of appropriate directors who understand their role and responsibilities and where applicable, are capable of separating LACC and Council roles; and
- The Councils could be represented by, for example the Executive Director, Strategy and Commissioning. There may be a further requirement for elected members to be suitably identified to fulfil roles on the Board (and/or Committee).

Board membership will be defined in the Shareholders Agreement. The Shareholders Agreement also needs to consider other key elements relating to each councils involvement, including:

- Risk to the shareholder;
- Agreement on voting rights and share structure that relates to usage of services and assets provided to the LACC;
- Contribution (i.e. assets) and utilization of the services provided to ensure that each Council receives appropriate return from the assets contributed; and
- Reserved matters, including the potential for additional shareholders joining in the future.

We would recommend each of the Councils seek independent legal advice with regard to Shareholders Agreement and any articles of association or other supporting agreements that may be required so that future opportunities are not precluded.

PwC view:

- ***The Owners would have equal voting rights attributable to their shareholding in the LACC.***
- ***As there will be areas that impact each Council differently, Reserved Matters could be established within the Shareholder Agreements to facilitate effective decision making and voting where impacts are not equally attributable to each of the Shareholders.***

5.3.3. Governance

Establishing a LACC requires the development of a new commercial operating model that maintains the integrity of the T18 programme, but provides the governance required for an incorporated body, as shown in Appendix 5.1. The key differences to the current operating model include:

- Shareholder agreements, to govern ownership rights in a corporate structure, including the preservation of essential services that could potentially be loss making over the longer term, going against commercial priorities of a LACC;
- Management agreements between the LACC and the Councils and other interfacing contracts;
- Senior leadership is likely to be shared between the Councils (i.e. Executive Director, Strategy and Commissioning) and the LACC (i.e. Executive Director, Service Delivery and Commercial Development, Commercial):
  - Strategy and Commissioning will be responsible for strategy and policy direction, member services and contract management (including LACC and others such as leisure);
  - LACC will be responsible for providing services currently provided within Commercial Services, Customer First and Support Services back to the Councils.
- Change mechanisms and levers including pricing and cost controls will be jointly managed within the contract management team;
- LACC management will be responsible for external opportunities, pricing and business development;
- Strategy and Commissioning will be responsible for setting lease, ICT asset and asset management strategies in line with LACC and Councils requirements;
- Benefits realisation processes should be incorporated into the governance structure to maintain a focus on achieving the outcomes.

These items are further explained in this section.

PwC view:

- ***The proposed operating model maintains the integrity of the operating model established by the T18 Programme and the changes will be with regard to ownership and governance arrangements.***

5.3.4. Decision Making

Delegated authorities and decision making responsibilities will be clearly defined in both the proposed structure and the relevant shareholder agreements. Decision making needs to cover the Councils', contracts and the LACC and we would recommend a decision making framework be developed during the implementation phase to facilitate this clarity.

The framework should include, but not be limited to:

- Policy Decisions:
  - Policy development could be by LACC or by Councils requiring different engagement and approvals
  - For Councils: approval by Executive and Hub and then by Councils
  - For LACC: LACC Board approval, shareholder committee and then by Councils
- Strategy Decisions:

  - Strategy development could be by LACC or by Councils requiring different engagement and approvals
  - For Councils: approval by Executive and Hub
  - For LACC: LACC Board approval, Executive and Hub

- Partnership Decisions:

  - Partnership proposals could be by LACC or by Councils requiring different engagement and approvals
  - For both: approval by Executive and Hub, LACC Board and then by the Councils

- Management Decisions:

  - Management decisions for LACC by LACC management
  - Reporting on management decisions to Executive and Hub

- Tactical Decisions:

  - Day to day decisions by respective party with consideration of interfaces

A key lesson to be learnt from our research is that decision making ability and lines of accountability need to be clearly understood as, under this model, the Councils could be exposed to greater risks if decisions are made without understanding broader implications created by the new structure. Alternatively, a structured approach to decision making will provide transparency for members and the community.

PwC view:

- ***Decision making will be similar to the current model where joint decisions and individual decisions are made by the Councils.***
- ***With a LACC, mechanisms for decision making will be formalised within the Shareholders Agreement and service contracts with the LACC.***

5.3.5. Management

The LACC model will require a suitable management structure. Changes already made as part of the T18 Programme are reflective of an appropriate management structure for this model and a number of resources within the Senior Leadership Team (SLT) have experience of both the public sector, as well as LACCs. Although there are no examples of LACCs currently delivering the scope of services proposed, the approach reduces duplication across the Councils and leverages the benefits and efficiencies already realised by the T18 Programme.

The approved management structure will need to work within the new governance model and decision making framework. In the interest of cost control, it would be advisable to create 'dual hatted' posts, where possible, with the current management teams being split between the LACC and the Councils. For example; the Executive Director, Strategy and Commissioning could represent Councils and members interest, whilst the Executive Director, Service Delivery and Commercial Development could represent the LACC on the Councils. It is assumed that the nominated Section 151 Officer remains with the Councils.

Key roles and responsibilities include:

Role	Responsibilities
Executive Director, Strategy and Commissioning	Reports to the elected members of the Councils and is responsible for managing the contracts with service providers (i.e. Leisure services) and the LACC
Managing Director LACC / Executive Director, Service Delivery and Commercial Development	Reports to the LACC board and is responsible for the operations and performance of the LACC and for the interfaces between the LACC and the Councils
Finance Director LACC / Deputy 151 officer (potentially)	Reports to the LACC Board and is responsible for the financial performance and governance of the LACC
Director, Customer First	Reports to the Executive Director, Commercial and is responsible for service delivery of Customer First functions
Director, Commercial Services	Reports to the Executive Director, Commercial and is responsible for service delivery of Commercial Services, including consolidated waste functions
Director, Support Services	Reports to the Executive Director, Commercial and is responsible for service delivery of Support Services, including ICT to the LACC and the Councils

However the Councils decide to establish the new LACC board, these decisions will be made either under section 111 of the LGA 1972 (on the basis that having a Council appointee on the board is "conducive or incidental to, or calculated to facilitate" the discharge of the Council's functions, or section 1 of the LA 2011 (general power of competence) based on this participation being likely to produce an economic, social or environmental benefit to the area. See paragraphs titled *Personal liability for directors* and *Conflicts of interest* for more information on director considerations.

Personal liability of directors

Given that directors may incur personal liability, for matters such as breach of duty, wrongful trading, fraudulent trading, breach of a disqualification order, and that some or all of the directors of the LACC will be council members or employees, it is good practice for the LACC to take out insurance in relation to their liabilities as a director.

It is good practice for a local authority to issue guidance to their nominated directors on the responsibilities and liabilities of being a director of a company. Any such guidance should cover the following matters:

- Directors' duties to act in the best interests of the company;
- The provision and use of information;
- Duty to employees;
- Fiduciary duty to creditors.

Although a local authority may be able to indemnify members and officers against this personal risk, any such indemnity will generally only cover actions taken honestly and in good faith.

Conflicts of interest

Members of the Councils who are appointed directors of the LACC have a fiduciary duty to the LACC, not to their respective Council. They have the powers and duties of company directors while they are appointed directors, and as directors, they are answerable to the membership of the LACC in accordance with the company's articles of association. However any member elected as a director is still bound by relevant local authority codes of conduct[2], in so far as these codes do not conflict with their legal obligations under company law.

It is important that the members and officers are aware of potential conflicts of interest when carrying out their roles for their authorities, or when acting as directors of trading companies.

[2] Under section 27 of the Localism Act 2011, a local authority in England is now required to adopt a voluntary code dealing with the conduct that is expected of its members and co-opted members. The voluntary code of conduct must include appropriate provisions for registering and disclosing pecuniary interests and interests other than pecuniary interests (see section 28) of the Localism Act 2011.

PwC view:

- ***There is unlikely to be any management changes initially and maintaining the Executive Director positions is likely to provide continuity through the transition phase.***
- ***Consideration will need to be given to the skills required of a Managing Director for the LACC to deliver the anticipated benefits.***
- ***There may be some governance issues in respect of items required to ensure transparency and assurance for the FD / S151 role. This can be clarified during the implementation phase.***
- ***There may be potential to create a Sales Director role in the future to manage and build external relationships.***

5.3.6. Location

The location of the LACC will need to be considered by the Councils. Operationally there are no major influences for a preferred location. The current operating model across the Councils is representation of a joint working relationship that has resulted in benefits through restructured and sharing of services through the T18 Programme. The LACC will utilise existing assets leased to the LACC on appropriate market rent/lease terms.

PwC view:

- ***The establishment of the LACC and registered office should not impact the operating model or perceptions of the level of control within the LACC.***

5.4. Charging Mechanisms

Pursuant to *Section 1* of the *Local Authorities (Goods and Services) Act 1970* (the "LAG&S Act 1970") the Councils can provide to any other "public body", including local authorities:

- Goods or materials (and the power to purchase and store any goods or materials that in the public body's opinion they may require for the purposes);
- Any administrative, professional or technical services;
- Use of any vehicle, plant or apparatus belonging to the authority (and the services of any person employed in connection with the vehicle or other property in question);
- Works of maintenance in connection with land or buildings for which the recipient public body is responsible (but not the construction of buildings).

The various bodies that can benefit are listed in orders made under the LAG&S Act 1970. These include other local authorities, certain NHS organisations, schools and academies.

A local authority is not limited in the amounts it can charge the public bodies to which the LAG&S Act 1970 applies and may trade for profit (R v Yorkshire Purchasing Organisation ex p British Educational Suppliers' Association (1997) 95 LGR 727).

In respect of the discretionary provision of goods or services to bodies which fall outside the LAG&S Act 1970, the Councils are limited to covering its costs. Unless there is a specific power enabling the authority to charge more than the costs of supply, in general, if the local authority trades with a view to making a profit with any organisation which is not a public body under the LAG&S Act 1970, it may only do so through a company.

To trade commercially, the Councils must rely on either specific or general trading powers. Under specific powers, a local authority may charge in excess of the cost of supply (e.g. Section 38 of the Local Government (Miscellaneous Provisions) Act 1976 for provision for computer based services) without a trading vehicle in place. In the absence of a specific power to trade, the Councils may only trade under a general trading power (e.g. Section 4 of the Localism Act 2011), in conjunction with a power to carry out the activity in question, through a company.

Therefore, prior to trading a range of services through the newly formed LACC, the Council will require legal advice to ensure it has the power to trade each of the proposed services.

The Councils will need to consider charging mechanism and the pricing of services (both internally and externally). To achieve this, it will be important to understand the relevant costs and how they are attributed or apportioned across the service levels. This understanding of costs will enable commercialisation of individual services that have the potential to generate revenue from external parties.

This activity should be undertaken once the business case has been approved and as part of the detailed implementation phase.

Consideration will also need to be given to the current skills and capacity of council staff and where responsibility for this would sit within the organisational structure. If not readily available, they may need to be recruited for at the appropriate time.

Pricing for tenders or work will also need to consider relevant competition legislation as well as local impacts. For example, do the Councils wish to take on additional work at the expense of local contractors. These may be considerations for the future as it is not envisaged that the LACC will be seeking to provide services externally in the initial phases, although opportunities for new business may arise during this time.

PwC view:

- ***Through establishing a LACC the Councils will be able to develop a better understanding of their cost base which will enable appropriate cost allocation across each service over time. This will in-turn inform the relevant charges to cover the costs attributable to each service provided by the Councils.***
- ***Charging mechanisms will be important in the LACC's ability to not only win but also deliver services to external parties cost effectively.***

5.5. Accounting

In the United Kingdom local authorities are required to prepare statutory financial statements in line with the Code of Practice on Local Authority Accounting in the United Kingdom (the Code). This is based on International Financial Reporting Standards (IFRS). The Companies Act 2006 allows companies to prepare their accounts in accordance with either the International Financial Reporting Standards (IFRS) or the Companies Acts and UK Generally Accepted Accounting Practices (UKGAAP). The Financial Reporting Council (FRC) has issued new accounting standards (FRS 100-102) which will apply to the LACC.

PwC view:

- ***The establishment of a LACC will require audited financial statements to be developed, which will be an additional cost over the current model.***
- ***The Councils will also need to continue to maintain their independent financial statements to account for the treatment of assets for use by the LACC.***

5.6. Tax

The establishment of a LACC means that it will be liable for various tax commitments. Currently the Councils structure and benefits are tax efficient and this section seeks to build upon previous advice and identify the key requirements and obligations.

5.6.1. Corporation Tax

Local authorities are exempt from Corporation Tax on all trading surpluses. LACCs are non-exempt bodies and are generally subject to Corporation Tax on all trading profits. The current rate of Corporation Tax is 20% (reducing to 18% by 2020). Transferring profitable activities from the Councils to the LACC will; therefore, result in a tax cost which would not otherwise occur.

The table below sets out the projected corporation tax liabilities on trading with third parties, assuming no external revenue until FY20. The same tax rates will be applied to profits from trading with the Councils if those activities are also deemed to be taxable.

£'000s	2019/20	2020/21	2021/22	2022/23	2023/24
Combined Councils' Profit before tax (see Financial Case)	137.0	281.0	432.0	590.0	605.0
Corporation Tax rate*	18%	18%	18%	18%	18%
Corporation Tax	24.7	50.6	77.8	106.2	108.9

*assumes no change in rates from 2020

To reduce the effect of Corporation Tax in the LACC on the otherwise exempt local authority trading activities the following options could be considered:

1. Reduce LACC income/increase LACC expenditure - Any transactions between the Councils and their LACC would be subject to the transfer pricing rules. Depending on the nature and direction of the transactions, the application of an appropriate transfer price may reduce the level of profits in the LACC;

2. If required, the LA makes justifiable management charges for central services - Management charges from the Councils to the LACC will have the effect of reducing profit in the LACC. As with option 1 any management charges should be at arms' length and will be subject to transfer pricing rules;

3. Make use of group losses - If the Councils have/form any other LACCs then profits/losses could be group relieved to reduce the overall level of profits within the group. Any residual profits would be subject to Corporation Tax in the usual way;

4. Make Qualifying Charitable Donations (QCDs) - QCDs are an allowable deduction from taxable profits. The LACC could make QCDs equal to the taxable profits each year to charities already established/to be established by the Councils to further a charitable purpose such as the arts or sport within each of the areas. This would have the effect of reducing profits by the amount of the QCD made. An estimate of the profits would need to be made before the end of each accounting period and the QCD physically paid in order for a deduction to be claimed. It should be noted that QCDs cannot be made to the authority directly and must be a physical payment between the LACC and the charity/charities and be from distributable reserves.

   This would however add a further level of complexity and administration should a charity or charities need to be established; and

5. Obtain HMRC clearance that the only taxable trading in the LACC is with third parties. This could be achieved through a non-statutory agreement with HMRC that any trading between the LACC and its members is not a taxable activity (because it is mutual trading or possibly as an Arms' Length Management Organisation (ALMO)). Extracts from HMRC's guidance with more detail on Mutual Trading and ALMOs can be found at Appendix 5.4.

We are aware that in exceptional cases LACCs have been accepted as non-trading by HMRC. Any such agreement is based upon the specific fact pattern and does not guarantee that HMRC would accept such an argument in this instance. Should HMRC agree the position then only profits made from transactions with third parties would be subject to Corporation Tax.

We would advise making an application to HMRC for an exemption. The primary task of the implementation phase and the acceptance of the LACC's exempt status should be an initial Quality Hold Point (QHP).

In addition to the corporation tax cost there would be additional annual tax compliance filing obligations on the new company. We estimate these additional annual costs in relation to corporation tax compliance would be:

- Preparation and submission of an annual Corporation Tax Return (CT600) £3,000-£5,000 *
- iXBRL tagged accounts (required for tax return filing) £500

*depending on the level of activity in the LACC.

A LACC may benefit from tax reliefs such as capital allowances. Further reliefs may also be available but these will rely on a holding company structure (reliefs could include group relief/consortium relief and capital gains tax relief).

PwC view:

- ***The establishment of a LACC will expose the Councils to Corporation Tax liability.***
- ***There are a number of ways in which this liability can be mitigated. Our recommendation is to apply for an exemption from HMRC.***
- ***For the LACC to be viable, it is imperative to engage with HMRC regarding an exemption from paying Corporation Tax on profits related to income derived from services provided to the Councils.***
- ***While this is not guaranteed, based on recent precedent, the impact of Corporation Tax may only be attributable to income derived from additional revenue generated from external sources.***
- ***We would recommend making this a QHP of the implementation phase. There is unlikely to be any additional tax implications whilst only trading with the Councils.***

5.6.2. Transfer Pricing

UK tax legislation requires large enterprises/groups to recognise all transactions between group companies (subject to exceeding the Medium Enterprise conditions as set out in the table below) on an arms' length basis or to adjust the results of such activities for UK taxation purposes.

	Maximum number of staff	And less than one of the following limits: Annual turnover**	Balance sheet asset total**
Small Enterprise	50	€10m/£7.6m	€10m/£7.6m
Medium Enterprise	250	€50m/£38.1m	€43m/£32.8m

**assuming exchange rate of £1/€1.31

The arms' length principle is that transactions between connected parties should be treated for tax purposes by reference to the amount of profit that would have arisen if the same transactions had been executed by unconnected parties. Any transactions not at arms' length should be accounted for in the LACCs self-assessment tax return.

Consideration should also be given to the application of Diverted Profits Tax to any transactions which move taxable profit from the LACC to the tax exempt local authorities.

A detailed commentary on Transfer Pricing and the Diverted Profits Tax can be found at Appendix 5.4.

5.6.3. VAT

In this section, we have considered the potential VAT impact of transferring activities to the LACC and have undertaken our analysis based upon our understanding of the activities undertaken by the two authorities. In some instances, it has not been possible to provide a definitive position at this stage as further information will be required regarding the nature of the activities; however, to the extent it is possible we have sought to provide an indication as to the VAT position that could be achieved to inform your decision making process.

Overview

Local authorities benefit from a special legal regime provided for by s.33 of the VAT Act 1994. The effect of this is that they are able to recover VAT incurred on their non-business activities. In addition to this, they enjoy favourable treatment in respect of costs incurred in relation to their exempt supplies, in that they can recover all of the VAT incurred in relation to these (i.e. the exempt input tax), provided that the total value does not exceed 5% of the total input tax.

Normal businesses that do not fall to be treated as s.33 bodies are generally not able to recover VAT incurred in relation to non-business or exempt activities. The LACC will fall into this category and, as such, care will need to be taken in respect of the transfer of activities to the LACC to offset the risk of creating an irrecoverable VAT cost where one did not exist previously. For the LACC, the irrecoverable VAT costs will include any related to assets that are transferred to the LACC and operated by that entity but which are not income generating as this could be a non-business activity in the hands of the LACC.

The Councils will be able to recover any VAT charged to them by the LACC in line with their current position; however, the outsourcing of activities will lead to an increase in VAT being incurred by the Councils due to the VAT liability on previously non-VAT items (such as labour). Whilst there will be an increase in exempt input tax, there should be a proportionally larger increase in the 5% ceiling in overall £ terms.

Analysis of Activities and Comments

It appears from our analysis that most of the activities that will fall to be undertaken will be taxable activities for VAT purposes and as such, entitle the LACC to VAT recovery.

Of the activities that will be transferred by the Councils to the LACC, the ones that potentially qualify for exemption and could lead to an irrecoverable VAT cost for the LACC are as follows:

- Interests over land (residential accommodation/commercial lets (where no option to tax in place);
- Provision of sporting/leisure facilities (subject to certain conditions);
- Burial and cremation services;
- Vocational Training (where centrally funded).

Exemption is available in other areas; however, they would not appear to be relevant here.

Assets retained by the Councils

In terms of the above, with the exception of vocational training, if the Councils do not transfer the assets in question (i.e. properties/community parks/cemeteries etc.) and retain the right to derive any income, which is our understanding of the intention at this point, then it is likely that the supply by the LACC to the Councils will be a taxable supply of management services only. As such, there will be no restriction to VAT recovery in the LACC and the Councils' VAT position will remain broadly unchanged apart from the increase in VAT incurred as outlined above.

Assets transferred to the LACC

Should the physical assets be transferred to the LACC along with the right to collect and retain any income from their operation, the position will be different and the parties would need to factor in the potential for an irrecoverable VAT cost.

We have calculated that this cost would amount to approximately **£1.3m pa** based on the current level of expenditure Appendix 5.5. Please note that in reality this amount is likely to be overstated as it makes the following assumptions:

- All property rental income to be exempt. It is likely that the LACC will opt to tax any commercial properties, meaning that VAT incurred will be fully recoverable; and
- Leaving aside whether or not leisure centre activities have already been outsourced, if these facilities were to be outsourced to the LACC (which owned and operated the assets), further consideration would need to be given to whether the LACC could qualify to be an eligible body for the purposes of the sporting exemption. If not, the significant proportion of expenditure would relate to taxable activities and be recoverable.

There would also be a restriction on residual VAT recovery, which is more difficult to quantify at this stage but is not likely to be significant given the preponderance of taxable activity.

Other considerations

As noted above, if the assets are retained by the Councils, the VAT impact should be minimal, with the LACC able to recover most if not all of the VAT it incurs (the only exception possibly being VAT incurred in relation to exempt vocational training) and the Councils' VAT position remaining broadly unchanged, apart from the increase in input tax relating to all of its business (taxable and exempt) and non-business activities. The Councils' entitlement to recover that input tax will be in line with the current position.

In our experience local authorities are usually on monthly VAT returns. It is likely that the LACC's output tax will exceed its input tax and, as such, it would be recommended that the LACC requests quarterly VAT. It is of course possible that the level of net VAT due to HMRC will mean that the LACC will be subject to the Payment on Accounts Scheme.

Subject to any other commercial issues, consideration should be given to the timing of payments/invoicing. For example the LACC might consider raising invoices for its services at the start of its VAT period so that it is able to receive payment from the Councils before the end of the period, thus ensuring it has sufficient funds to make payment to HMRC. If this invoice is raised near the end of the monthly VAT period for the Councils, it might be possible for them to receive the input tax from HMRC before making payment to the LACC thus mitigating the impact on their cash-flow position.

PwC view:

- ***The LACC will be responsible for VAT and mechanisms are available to reduce potential impacts on cash flow, such as monthly versus quarterly invoicing.***
- ***The Councils retain their favourable VAT treatments.***
- ***VAT is unlikely to have a negative impact on the Councils as long as the assets remain within the Councils.***

Employee

From an employment taxes perspective there is likely to be little change to the obligations currently incurred by the Councils. There is a proposed Apprenticeship Levy, due to come into force on 6 April 2017. This means that any employer with a payroll (broadly, the amount of wages and salary paid to employees subject to Class 1 NIC) exceeding £3m will have to pay a charge of 0.5% on the balance. The combination of the Councils workforce coming together into what will be a larger one, could give rise to this extra cost. This has been considered within the financial appraisal and is deemed to have minimal impact. Additional consideration needs to be given if the proposed model is one of some services in house/some outsourced, and if an employee has two or more jobs with separate contracts of employment for each. History shows that HMRC have challenged payments that have not been aggregated in these sorts of circumstances. We understand that this is unlikely to occur in this instance and have assumed that employees will have one defined employment contract.

5.6.4. Pensions and TUPE

It is envisaged that the Councils will transfer approximately 400-450 employees to the LACC to in turn provide the services back to the Councils. This may amount to a transfer under TUPE obligations, or it may be subject to directions under section 101 of the LGA 2003. Whether or not there is a TUPE transfer will depend on the facts of the case.

Where a relevant authority is contracting-out a service, section 101 of the LGA 2003 requires that authority to deal with matters relating to the employment of staff who will be transferred or brought back at the end of the contract in accordance with the directions issued by the Secretary of State and have regard to guidance. (In Wales, directions are issued by the National Assembly, and in Scotland, the Scottish ministers.)

Where existing local authority employees are transferred to the new business, which is separate from the local authority, the expectation would be that the employees' existing terms and conditions are protected under TUPE or section 101 of the LGA 2003, unless there are exceptional circumstances.

Section 102 of the LGA 2003 provides that directions under section 101 require local authorities to secure pension benefits for transferred employees which are the same as or broadly comparable to or better than those enjoyed before the transfer. This requirement also applies if there is a subsequent contract transferring those employees to another contractor.

The Councils are committed to meeting their obligations for existing staff in maintaining their terms, conditions and pensions and understand that a change to a LACC will not change their legislative obligations. In addition to meeting their current obligations, a LACC presents greater flexibility of staffing compared to the current model and may present opportunities to incentivise staff through profit sharing or bonus schemes.

A large TUPE transfer of the Councils staff into the LACC will impact on the Councils' current participation in the LGPS. Given that the Councils are "Best Value" local authorities, then under the Best Value (Pensions) Direction 2007, the staff will have an ongoing right to LGPS benefits. This is generally provided by the new employer participating in the LGPS and although the Direction does not explicitly require a past service liability transfer, one is normally implemented.

<<This paragraph has been removed due to commercial sensitivities>>

- Staff remaining with the Councils: 25 in total, 14 at South Hams District Council and 11 at West Devon Borough Council with the staff continuing to participate in their sections of the Devon LGPS Fund (the Fund).
  - Cash: the Councils will continue to pay future service contributions in respect of staff remaining and in respect of a possibly changed funding deficit amount after the transfer. The amount will depend on the terms agreed and could be smaller in £ terms or smaller i.e. worse in funding level % terms. The Councils are due to be notified of a new deficit amount towards the end of 2016 anyway once the results of the triennial valuation due at 31 March 2016 are available. There is no expectation of immediate cash input being required into the Fund unless the LACC establishment triggers redundancies amongst staff over age 55 (who can claim immediate unreduced redundancy pensions), which this is assumed to not be the case;
  - Accounting: There would be a settlement gain or loss in the Income and Expenditure of the relevant financial year's accounts as the transfer terms will not match the accounting basis. Year-end pension assets and liabilities would be reduced post transfer.

- LGPS members transferring to the LACC: approximately 400, 325 at South Hams District Council and 75 at West Devon Borough Council with the staff transfer into a new section of the Fund for which the LACC would be responsible. Legal advice would be needed on the route to participate: the LACC may be accepted as a "Part 2" employer without the need for an admission agreement or via becoming an admission body with such an agreement. One admission agreement may be required for each contract awarded to LACC at inception, increasing the administration although a single actuarial valuation by the Fund actuary covering multiple admissions may be agreed to reduce this.

- Cash: The LACC would pay future service contributions in respect of its staff (if any and will depend on terms agreed). A common approach to transfer terms would be to receive sufficient assets from the Councils so that those retain the same % funding level after the transfer and the initial % funding level of the LACC section is the average of the Councils' sections funding levels. Under this approach the quantum of the Councils' deficits would be reduced. Another approach is commonly called a "fully funded" transfer so that assets are transferred in line with liabilities to create nil deficit initially for LACC (with no change to the quantum of the Councils' deficits and a lower % funding level). There is no expectation of initial cash inputs to the Fund by the LACC.
- Accounting: Unless the Councils agree to underwrite the LACC's exposure to pension risk via its LGPS participation, the LACC will need to follow full defined benefit accounting which can be volatile i.e. fluctuate year on year in both P&L and balance sheet e.g. due to movements in prescribed bond yields used to assess liabilities. In its opening balance sheet there could be an accounting deficit since the transfer terms (even if "fully funded" as above) will not match accounting assumptions;
- Security requirements: The Fund will assess whether the failure of the LACC poses a risk to the Fund e.g. should the LACC section have an unpaid deficit and consideration of if the LACC collapses. The Fund could either require LACC to pay for a bond or indemnity or require that it obtains a guarantee from a combination of the Councils. The commercial pricing of a bond or indemnity, whose amount would likely be substantial, may render it impractically expensive although taxpayer support to provide a guarantee might also be unacceptable.

Note: a large number of factors will affect the contribution assessments by the Fund actuary of the Councils' and LACC's sections of the Fund at successive triennial valuation. These include the financial and demographic experience (e.g. pay awards, number of ill health retirements). If the LACC does not admit new hires into the LGPS, such that the average age of the membership increases, then its average contribution rate as a percentage of pay will increase though paid on a reducing payroll.

- Non-LGPS members transferring to the LACC: 10 currently (West Devon waste services remain outsourced)

  - Cash: Under the legislation we would expect Council staff who have opted out of the LGPS to retain LGPS eligibility after employment is transferred to the LACC. Subject to legal advice, statutory auto enrolment duties would also mean that these staff would need to be assessed and potentially enrolled into the LACC section of the LGPS Fund on their first day (and re-enrolled every 3 years). If these staff do not immediately opt out then this requirement could increase the LACC's immediate pension costs relative to the Councils' pension costs.

- <<This paragraph has been removed due to commercial sensitivities>>

For new hires of the LACC (subject to legal advice), the LACC would not be obliged to provide LGPS pension provision to new hires (i.e. not compulsorily transferred) even if they work on Council services. Lower cost defined contribution provision accompanied by risk benefits e.g. life assurance and PHI insurance might be provided instead. Using defined contribution provision would give greater certainty of employer pension costs (subject to take up rates) and less pension risk exposure with simple cash accounting applying. Tiered pension provision could create HR and recruitment issues.

A LACC builds on the culture developed as part of the T18 Programme and provides flexibility through staff demographic changes as people leave and new people join the transition is likely to be gradual. The T18 Programme has already delivered the majority of the benefits of staffing changes and this is not a major drive and is not likely to present material benefits in the short to medium term. Establishment of a LACC presents the Councils an opportunity to establish an alternative pension provision for new hires to the LACC which could present some long term savings.

The Councils have requested the latest actuarial reports from the Fund and these are anticipated to be received to inform detailed calculations during the implementation phase.

While it is difficult to predict future pension contribution requirements as a result of fluctuations in the calculations over time, our appraisal has assumed that the existing contributions made by the Councils continue to provide a baseline for the future. Going forwards, there may be an opportunity to fund a portion of the Councils' historic pension liabilities via any profits generated by the LACC; however, alternative mechanisms should also be incorporated to provide flexibility in accounting for fluctuations. A potential impact may arise where fluctuations are higher than anticipated and the LACC is subsequently required to make contributions to the Fund in excess of those forecast. If this situations arises, the LACC and the Councils may need to seek specific accounting advice; however, overall, the Councils would be responsible for accounting for the required pension contributions and address any fluctuations, whether the LACC is established or not. The Councils have requested the latest actuarial reports from the Fund and these are anticipated to be received to inform detailed calculations during the implementation phase. This information will provide a basis for identifying the cashflow requirements and contracts between the Councils and the LACC so that future pension contribution requirements are met.

PwC view:

- ***Council staff transferred to the LACC will need to be re-enrolled into the Fund at the relevant commencement date.***
- ***The Councils will likely be required to provide guarantees to the Fund regarding pension liability for current staff, reducing the establishment impacts of the LACC;***
- ***Seek confirmation / guidance from LGPS on how the current pension deficit should be treated.***

5.6.5. State Aid

Establishing a LACC may have State Aid implications if state resources are used to provide assistance that gives an economic advantage over others. Pricing, selling, ownership, leasing, rebates, grants etc to or from the LACC will need further detailed consideration to determine if they could be classed as State Aid. Legal advice is anticipated to be sought in the next phase of development.

5.7. Contracting with the LACC

Transition to the preferred option requires additional contracting compared to the current model. This section summarises the key considerations to be considered in development, establishment and transition, including:

- Contract management;
- Contract Change;
- Contract term;
- Individual elements;
- EU procurement rules.

5.7.1. Contract Management

Contract management will be critical to the success of the preferred option and this in turn will rely upon the skill and capacity of the management team. As demonstrated by extensive reviews of PFI contracts, the performance of individual contract managers can significantly influence the outcomes over the term of the contract and requires further consideration.

A LACC presents additional complexities and arrangements between the Councils and the LACC management resulting in differences between service expectations and actual service delivery. A contract management manual should be developed to guide the parties through the complex situations as they arise.

5.7.2. Contract Change

It is inevitable within a political environment that there will be continued change and, as demonstrated by recent events, they could be significant in terms of the political standpoint of the leadership. Contract management is the mechanism that enables the contract to be changed or adapted to respond to the changing needs of both parties. It is particularly important where the owner is also the customer and the directors of the LACC will need to understand their individual roles in resolving what could be significant competing priorities. These mechanisms should be embedded in governance, contract management and decision making frameworks.

5.7.3. Contract Term

Establishment of a LACC to provide services to the Councils is likely to require a long term contract that enables the parties to understand performance and to provide certainty of service provision and funding over that term. Consideration has been given to the impacts of assets and funding. As the LACC will lease assets from the Councils it is important that each of the Councils agree on services being provided and assets being contributed.

Leasing agreements between the Councils and the LACC should be considered on appropriate commercial terms which may differ between assets classes, for example:

- Commercial offices 3-5 years;
- Maintenance or depots 5-7 years;
- Commercial, industrial or specialist vehicles 5-10 years.

Further consideration should be given to the contract term and defined in the Shareholder Agreements.

5.7.4. Individual but collective

The Councils will have a Shareholders' Agreement with regard to their interests in the LACC and there will also be individual contracts for the services that the LACC will provide to the Councils respectively. There will also be contracts with the LACC for assets or leases to be provided within the structure to represent the asset utilisation of the LACC in delivering its services and performing its obligations under the contracts.

5.7.5. EU Procurement Rules

It should be noted that the EU procurement rules may apply in any of the following situations:

- Either one or both of the Councils provides services, supplies or staff to the trading company;
- Either one or both of the Councils buys services, supplies or staff from the trading company;
- The LACC itself buys the services;
- The provision of services to another public body[3].

5.8. Commercial Case Summary

The commercial case demonstrates that the LACC proposal is commercially viable:

- The Councils are able to establish a LACC within a company structure limited by shares that appropriately allocates roles, responsibilities, voting and returns to the Councils;
- The commercial transition phase will need to focus on contract governance, including the novation of existing contracts, as the majority of the current operational structure, as established as part of the T18 Programme will remain as is;
- Shareholders agreement in the LACC should provide for different shares that enable equal voting and returns based on utilization of services and assets, as well as terms for share sale, exit and share buyer controls;
- Governance and management reporting and responsibility will change but the operating model is unlikely to require additional change;
- Key areas include:
  - Corporation Tax: There is potential to obtain exemptions from HMRC for trading with the Councils, meaning that tax implications are only attributable to revenue generated external to the Councils;
  - VAT: It is envisaged that all services attract VAT and although the LACC does not have as favourable VAT exemptions as the Councils, it is unlikely irrecoverable VAT would have any adverse impacts on the Councils;
  - Employee tax: Employee taxes are likely to remain the same, although potential for 0.5% apprenticeship levy from April 2017, if the pay bill of a public (e.g. Council) or private body (e.g. LACC) exceeds £3m each year;

[3] The LACC's customers, where they are public bodies, will, in most cases, have to carry out a procurement process before buying LACC services, however, this will depend on the nature, value and type of arrangement: The Council owners of the LACC can purchase directly from it without advertising the contract if it falls within the Teckal exception or conditions under Regulation 12 of the Public Contract Regulations 2015.

- Pensions: The LGPS fund is likely to require some form of guarantee from the Councils with regard to their existing pension liabilities; however, this should not increase the cash requirement within the LACC; and

- Accounting: The LACC will require audited financial statements to be developed, which will be an additional cost as each of the Councils will still need to maintain their own financial records.

PwC view:

- ***There are established examples of commercial structures for ownership, governance and management of the LACC's functions of Customer First, Commercial Services and Support Services.***
- ***Strategy and Commissioning would be responsible for contract management of the LACC's performance.***
- ***The commercial arrangements are likely to have minimal impact on the existing operational and service delivery model, the changes are primarily reporting, governance and ownership.***

6. Financial Case

6.1. Introduction

This section focuses on the financial benefits of the new model. This section also considers affordability and funding requirements. The purpose of this section is to:

- Summarise the outcomes of the financial appraisal;
- Summarise scenarios, the differences in results and the reasons for them;
- Consider cashflow and affordability requirements.

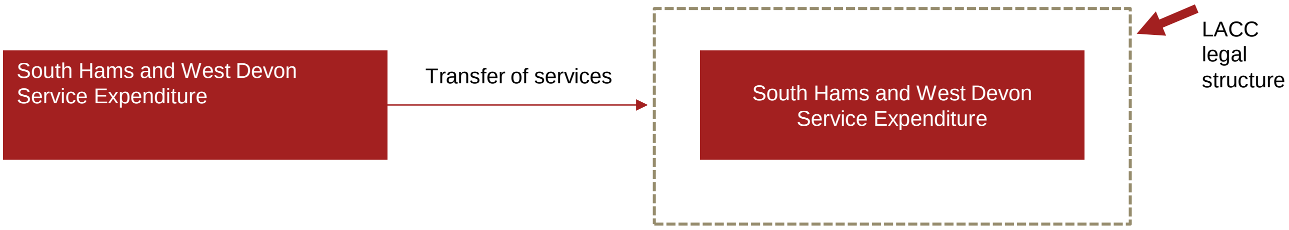
6.1.1. Financial Appraisal Overview

The financial appraisal compares the 7 year forecasted expenditure under the current delivery of the Councils services with the forecasted expenditure of various scenarios under the preferred Option 6 in order to highlight the possible financial impact of adopting a new delivery structure.

6.2. Expenditure with a LACC

The proposition is to transfer all of the Councils' services to a LACC (except for certain Strategy and Commissioning activities). The Councils will fund the LACC for the cost of delivering the transferred services in the LACC whilst continuing to fund Strategy and Commissioning within the Councils. The split of funding between the Councils is assumed to be on the same level of spend relating to each Council. This is discussed further in Appendix 6.1.

The change in legal structure to deliver these services should not change the fundamental costs of delivering these services; however, the LACC will incur both one off set up and annual on-going costs in addition to the service delivery costs. Other than these additional costs, the expenditure profile of the LACC should mirror that of the base case position i.e. the current Councils' expenditure (refer to detailed financials in Appendix 6.2).



Reference to the term expenditure in the Financial Case is the annual cost irrespective of when the cash payment is made. For instance, Employers National Insurance on employee costs (i.e. expenditure) for the month of March would not get paid (i.e. cashflow) until April. Note that this is a timing difference between expensing in the income or profit and loss statement and the subsequent payment through the cashflow statement.

The base case assumption is that the Councils would fund the expenditure of the LACC in advance. This would, however, result in an increase in the short term cashflow funding requirement of the Councils, as currently non-employee related costs are paid for by the Councils on 30 day terms.

This additional funding requirement could be avoided if cashflow arrangements between the Councils and the LACC were put in place. For instance, the cashflow funding of the LACC could be delayed until the LACC is required to make payment, which should mirror payment terms of the existing Councils. See Appendix 6.3 for further detail. As a result, our analysis is based on the expenditure profile, as the only changes resulting from transferring services to the LACC relate to non-cashflow specific items.

Any financial assistance provided by each Council to the LACC, whether in cash or in kind, should be for a limited period with an expectation of returns at a later date.

Providing such assistance should be formalised by an agreement entered into for a commercial purpose between each Council and the LACC. Before entering into an agreement, each Council should be satisfied that what is proposed is not ultra vires. Each Council has the power to do anything reasonably incidental to its express powers. The trading power under section 95(1) of the LGA 2003 is an express power. If a local authority decides therefore that the most appropriate vehicle for trading is a company, it would be able to establish a company under its subsidiary powers.

Until Part V of the 1989 Act is repealed, any company established to carry out a trading activity in which a local authority has an interest is subject to the rules about controlled[4], influenced[5], regulated and minority interest companies in Part V of the 1989 Act and the Local Authorities (Companies) Order 1995 (1995 Order).

If a company is "controlled" it will be regulated, and if it is an "influenced" company it may well be regulated. Regulated companies are treated as if they are the local authority and are therefore subject to financial and propriety controls (see section 5.3.5).

The main consequences of the company being controlled or regulated are set out in the 1995 Order and include the following proprietary controls:

- Any financial support for the LACC, or possible liability for the Councils associated with the company, will have to be included in any assessment of the authority's finances under the prudential framework for capital investment by local government;
- All relevant documents must state that the company is controlled or influenced by a local authority;
- The relevant local authority must be named;
- There are limits on the allowances payable to directors of such companies;
- Regulated companies are bound by the restrictions on publication of information imposed by section 2 of the Local Government Act 1986. This means that they are prohibited from publishing party political material;
- Directors of regulated companies must be removed if they become disqualified for membership of a local authority;
- A controlled company must obtain the National Audit Office’s consent to the appointment of its auditor;
- Requirements are imposed relating to the provision of information to the local authority's auditor and members and of financial information to the authority;
- Controlled companies that are not arms' length companies must allow for public inspection of the minutes of any general meeting for four years after the meeting, unless disclosure would be in breach of any statutory requirement or obligation owed to any individual;
- As with any private limited company, at the end of its financial year, full statutory annual accounts must be prepared and filed with the Registrar of Companies. Corporation tax due for that period must be paid to HM Revenue and Customs (“HMRC”) or nil tax return notified. Also, a completed Company Tax Return to HRMC must be filed;[6] and
- Business rates and VAT rules apply to a local authority private limited company.

[4] Section 68 of the 1989 Act defines controlled companies. If any one of the following conditions is met, the company will be controlled:

  - The company is a "subsidiary"4 of the local authority by virtue of section 1159 of the Companies Act 2006.
  - The company is not a subsidiary, but the local authority has the power to control a majority of the votes at a general meeting of the company.
  - The company is not a subsidiary, but the local authority has the power to appoint or remove a majority of the directors of the company.

[5] A company is subject to the influence of a local authority if all of the following conditions are met:

- It is not a controlled company;
- There is a business relationship between the company and the authority;
- There is a "personnel association" between the company and the authority. A personnel association exists when:
  - at least 20% of the total voting rights at a general meeting are held by persons associated with the authority; or
  - at least 20% of the directors are persons associated with the authority; or
  - at least 20% of the total voting rights at a directors' meeting are held by persons so associated.

A person is at any time "associated" with an authority if they are at that time a member or officer of the authority, or both an employee and a director, manager, secretary or similar officer of the company under the authority's control, or if they have been a member of the authority within the preceding four years.
A company has a "business relationship" with a local authority if one or more of the following apply:

- Within 12 months up to and including the day on which the question arises, more than half of the company's turnover is made up of payments from the authority or from a company under the control of the authority;
- More than 50% of the company's turnover is derived from exploiting assets in which the local authority or company under the control of the authority has an interest;
- The total of the following exceeds 50% of the net assets of the company:
  - grants made either by the authority (being expenditure for capital purposes) or by a company under the control of the authority; and
  - the nominal value of shares in the company which are owned by the authority or by a company under its control;
- The total of grants, shares and loans or other advances made or guaranteed by the authority or by a company under its control exceeds 50% of the fixed and current assets of the company;
- The company at that time occupies land by virtue of an interest obtained from the authority or a company under its control at less than best consideration reasonably obtainable; and/or

The company intends at that time to enter into or complete a transaction and when that is done there will be a business relationship under any of the above.

[6] There is more detailed accounts and tax return information for private limited companies at https://www.gov.uk/prepare-file-annual-accounts-for-limited-company/print

Refer to Appendix 6.6 for assumptions used in the Financial Case.

6.2.1. Additional Costs

The formation of a LACC will result in the following additional costs:

1. One-off set up costs
2. On-going costs.

The impact of these costs are considered further below and at Appendix 6.4 and 6.4.1.

Set up cost expenditure

The formation of a LACC will include the following estimated one-off set up cost expenditure:

Table A

£'000	South Hams	West Devon	Combined	Notes
Legal advice and support	50.00	50.00	100.00	Including assistance drafting shareholder agreements, articles, contract review, novation etc.
Finance support and advice	75.00	75.00	150.00	Including detailed budgeting of LACC, operational planning for transition to LACC, VAT registration, CT establishment, accounting principles, Co. registration, leases, pricing models, commercial governance, finance system interfaces and controls, LACC reporting tools and templates, commercial and financial risk advice.
Pension administration	10.00	10.00	20.00	Including pension calculations, engagement with fund, establishment and registration assistance.
Implementation and change management	37.50	37.50	75.00	For project management, change management, risk management (possible need for external advisors), Director training, Governance establishment (roles and responsibilities), communications and stakeholder engagement, potential resources or advisors for transition i.e. West Devon waste.
Contingency	15.00	15.00	30.00	For unforeseen transition items.
IT system and resource	12.50	12.50	25.00	Civica and other system integration requirements including based, financial, communications, customer systems, web-based applications etc.
Total set up costs	200.00	200.00	400.00	

Note that these set up costs do not include the cost of preparing this Business Case, as this is a sunk cost that is not dependent on the decision to be made. Further detail on these costs is provided in Appendix 6.4.2.

On-going cost expenditure

The formation of a LACC would include the following estimated annual on-going cost expenditure (borne by the LACC). We have assumed that these costs would be required from April 2017.

Table B

£'000	South Hams	West Devon	Combined	Notes
Corporation tax	2.50	2.50	5.00	Annual cost as advised by PwC team for corporation tax compliance
Other Finance	2.50	2.50	5.00	Statutory accounts and other including pensions
Audit	10.00	10.00	20.00	Estimated cost subject to firm used
Chairperson	2.50	2.50	5.00	10 meetings a year at £500 a meeting
Business Development	5.00	5.00	10.00	This could be deferred until private revenue is generated but for prudency is considered to be required from the establishment of the LACC
Legal	2.50	2.50	5.00	Estimate of costs for preparing LACC specific contracts
Contingency	2.50	2.50	5.00	To account for any other costs related to running of a LACC
Civica	2.50	2.50	5.00	Ongoing maintenance
Total on-going costs	30.00	30.00	60.00	

Appendix 6.4.3 shows the detailed profile of these annual on-going costs over the next 7 years. We have assumed that these costs would be funded equally by the Councils, as discussed further in Appendix 6.1.

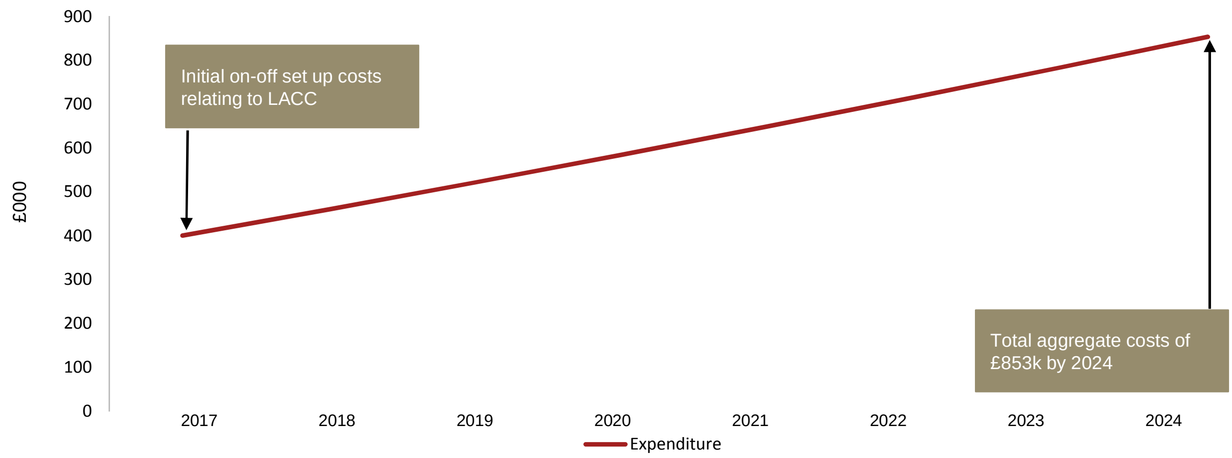
Cumulative impact of additional costs

The impact of the cumulative additional costs on the Councils expenditure profile is shown in Table C and more detail provided in Appendix 6.4.4. The ongoing LACC cost is inflated by 2.5% from 2018/19.

Table C

Cumulative Change in expenditure due to additional costs (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
South Hams	200	200	200	200	200	200	200	200
West Devon	200	200	200	200	200	200	200	200
LACC	-	60	122	185	249	315	383	453
Combined	**400**	**460**	**522**	**585**	**649**	**715**	**783**	**853**

Aggregate additional expenditure before opportunities



6.3. Opportunities

The transfer of the Councils' services into the LACC structure provides opportunities for reducing the funding requirement of the individual Councils, resulting in the ability to reverse the impact of the additional c£853k of cumulative costs, as shown in the graph above. See Appendix 6.5.

6.3.1. Financial implications of West Devon waste services

Our base case analysis above has been on the basis that waste management of West Devon remains outsourced. The outsourced cost profile has been provided by Grant Thornton report – Options for Waste Services Delivery – January 2016. There is; however, potential for the Council to provide this service within the LACC ('LACC provided' or 'LACC provision' or 'in-house') , which we understand from Council management would only be considered if a LACC were formed, thereby generating savings in respect of the existing contractor's applied mark-up. There is also future scope to generate efficiencies from shared management, although this has not been factored in our analysis.

The different options are detailed in Appendix 6.5.1 and 6.5.1.1, however, the choice of LACC provided option does not impact on the decision over establishing a LACC. We have assumed a delay of 6 months to establish a LACC provided operation, which is considered to be the most likely option. There is also the possibility of adopting a managed service option, whereby the existing contractor manages the waste management assets purchased by West Devon Council. Asset acquisition profiles are shown in Appendix 6.5.1.2.

Table D <<This table has been removed due to commercial confidentiality>>

Table E

Difference in expenditure	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	Cumulative Total
Outsourced annual cost	Figures removed – commercial in confidence								
Option 4 - managed service									
Difference in expenditure									
Aggregate difference	40	325	576	1,090	1,627	2,190	2,778	3,392	

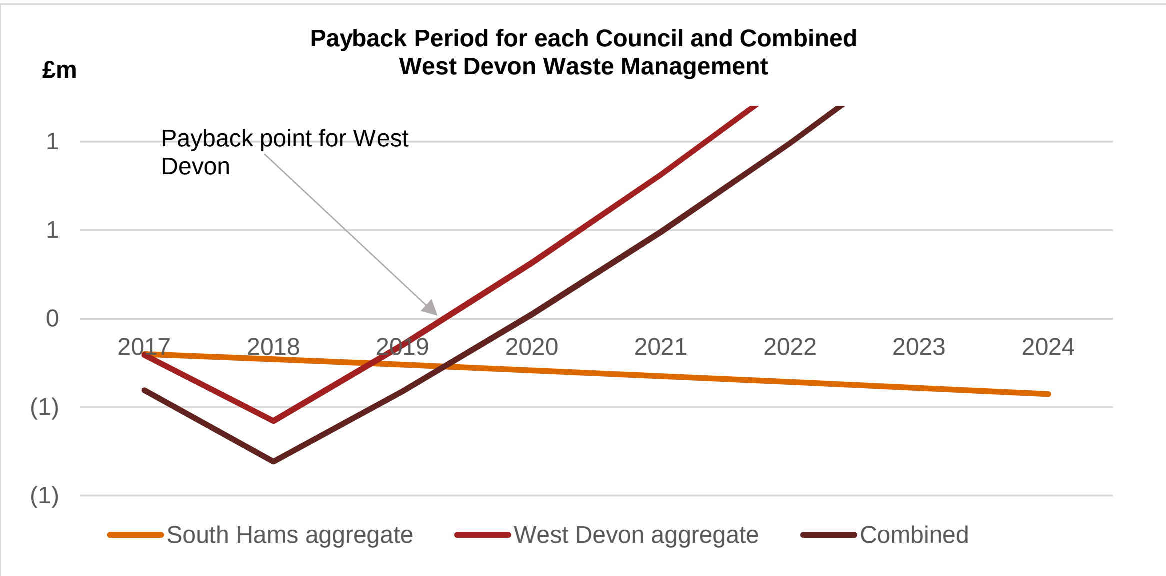
In 2016/17, both the outsourced option and the LACC provided service would require re-tender or set-up costs (assumed to be c£50k). In addition, the LACC provided option would require an extension cost to the current outsourced contract of an assumed £5k resulting in the difference shown in Table D.

Adoption of the LACC provided service halfway through 2017/18 would require the Councils to continue to pay the outsourced rate over the first 6 months of the year (annual cost of £<< figures removed – commercially confidential>> for 6 months), but with an additional £<<confidential>> per month (£<<figures removed – commercially confidential>> . The remaining 6 months of the year would be at the new LACC provided cost (inclusive of asset costs). We understand from Councils' management that the on-going annual LACC provided cost would be c£<<confidential>> before adjusting for inflation (£<<confidential>> of operating costs and c£<<confidential>> of assets finance costs). This would mean that the cost for the final 6 months of 2017/18 would be £<<confidential>>. Total costs for 2017/18 under the LACC provided 6 month delay option would be c£<<confidential>> as shown in Table D (£<<confidential>>).

<<Paragraph removed due to commercial sensitivity>>

In 2018/19, the annual outsourced cost is assumed to be £<<confidential>>. The cost of the LACC provided option is £<<confidential>>. This creates a reduction in the funding requirement from the adoption of the LACC provided option of c£<<confidential>> as shown in Table D above. From 2019 the annual difference between the cost of the two options increases. The increase is the result of the effects of 2.5% indexation on different cost bases and no indexation required on £<<confidential>> of asset repayments included in the LACC provided cost profile. By 2024 Table D shows aggregate benefits of adopting a LACC provided option of £<<confidential>>.

These savings are assumed by the Councils' managements to only be available to West Devon Council (see Appendix 6.5.1.5) and as a result the following shows the impact a LACC provided West Devon Waste Management service on the Payback of both Councils:



This shows that Payback period for West Devon is achieved by 2020, whereas South Hams would not achieve payback from this option alone (i.e. assumed payback to be achieved from the generation of private profits). The Combined Council achieves payback by 2020.

We have not assumed any additional efficiencies or cost saving opportunities due to the extensive transformation process already undertaken by the Councils. We understand, for example, that there is scope to improve the grounds and estate maintenance service as a result of forming the LACC, although we have not been provided with a quantum of these savings.

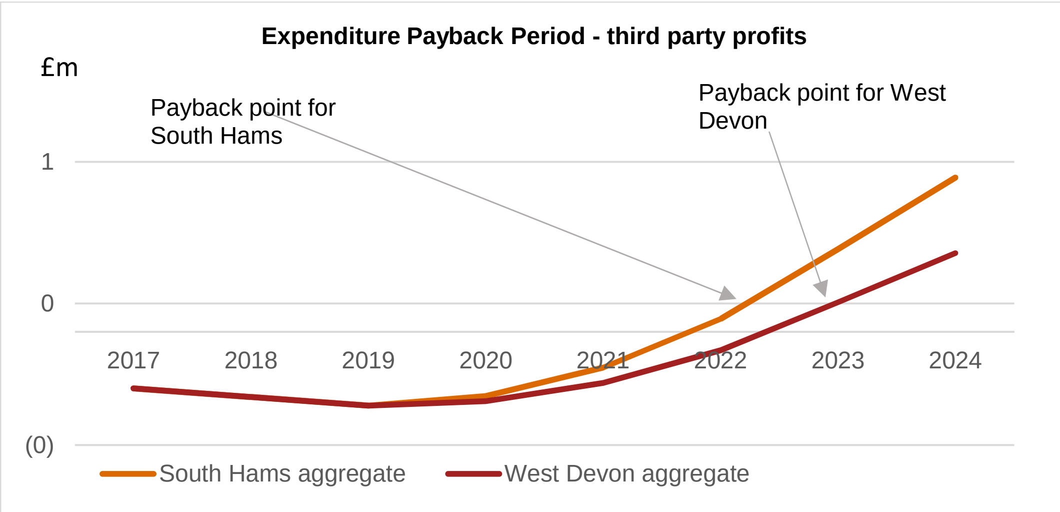
6.3.2. Third Party Income – Potential profits from a LACC

We have assumed that third party revenue could be generated by the Councils from April 2020, and as discussed above is required for South Hams to generate a Payback. As detailed in Appendix 6.5.2, we have assumed a scenario of revenue of 5% of current activity levels and a marginal cost of << figures removed – commercially confidential>>. We have assumed that there is surplus capacity within the Councils' capital assets and administrative functions to support revenue generation of 5% of current activity levels and that the additional cost requirement is << figures removed – commercially confidential>> of the third party revenue. There is the possibility to achieve revenue levels of up to 20% under Teckal Exemptions, although at this level there may be additional capital asset and overhead costs that would increase the marginal cost of this third party revenue.

Table F <<Table redacted due to commercial sensitivities>>

Table G <<Table redacted due to commercial sensitivities>>

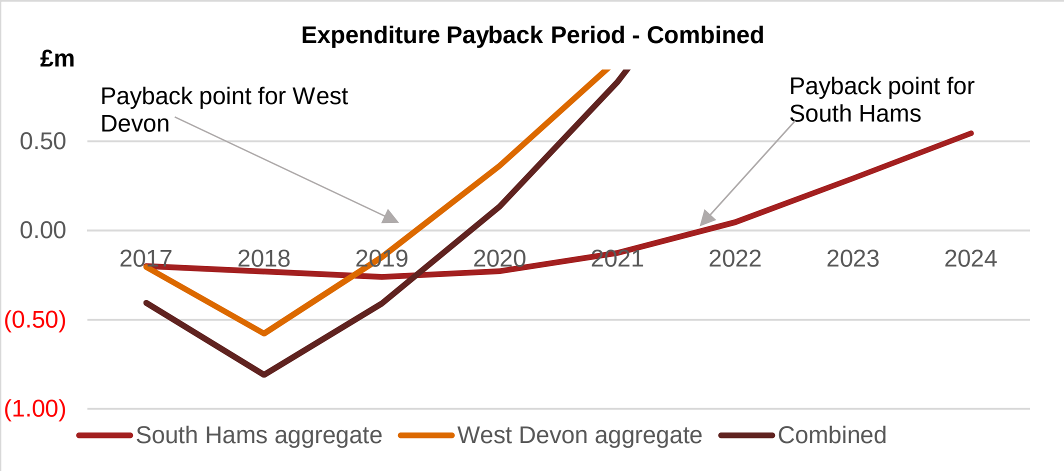
We have not assumed any profits from sale of 'know-how' to other Councils, however there is potential for significant returns in excess of those assumed here.



Payback from third party profits alone is achieved by 2022 for South Hams and 2023 for West Devon. Profits from third parties are assumed to be split between the Councils in the same proportion as calculated for the funding of the LACC, although the exact details of this would be determined between the Councils during the implementation phase, to ensure both are in agreement. See Appendix 6.1.

6.4. Payback Period

Accumulated payback (including a LACC provided West Devon Waste Management service) is shown below, with further detail in Appendix 6.5.3. Payback for West Devon is achieved by 2020 (using the data and assumptions provided), whereas South Hams District Council still achieves payback by 2022.


Expenditure Payback Period - Combined
£m
Payback point for West Devon
Payback point for South Hams
0.50
0.00
(0.50)
(1.00)
2017
2018
2019
2020
2021
2022
2023
2024
South Hams aggregate
West Devon aggregate
Combined

Maximum funding requirement

1. £400k set up costs (combined)
2. £60k ongoing cost (combined)
3. £<< figures removed – commercially confidential>> West Devon Waste Management cost relating to extension of contract (could be avoided by adopting a managed service option). Note that this funding requirement is only relevant to West Devon as the impact of the changes in cost profile of a LACC provided West Devon Waste Management service are not borne by South Hams under the assumptions

Table H <<Table removed due to commercial sensitivities>>

The exact timing may vary, however, as long as the anticipated on-going benefits exceed the on-going costs, then payback of the set up costs will be achieved, irrespective of quantum in the medium to long-term, with an increase in funding requirement only over the short-term.

Table I <<Table removed due to commercial sensitivities>>

6.5. Financial Case Summary

The financial case demonstrates that the LACC proposal is affordable:

- There will be set up costs of c£400k relating to the establishment of a LACC;
- There will be additional on-going costs of c£60k per annum relating to the running of a LACC;
- There are opportunities to generate ongoing third party profits (c<< figures removed – commercially confidential>>) from April 2020. Additionally, there are potential savings in the cost of West Devon waste management by providing the service within the LACC (c£<< figures removed – commercially confidential>> a year). This additional saving only applies to West Devon and accounts for the shorter payback period than South Hams (see Appendix 6.6); and
- The net result could be an unindexed c£<< figures removed – commercially confidential>> a year (c£<< figures removed – commercially confidential>> for South Hams District Council and c£<< figures removed – commercially confidential>> for West Devon Borough Council), contributing to a payback of the set up and ongoing costs by 2022 for South Hams District Council and 2020 for West Devon Borough Council (see section 6.4).

7. Management Case

7.1. Introduction

The Management Case seeks to demonstrate that the benefits of change are achievable with clearly identified transition and delivery requirements. The purpose of this section is to:

- Provide an overview of deliverability of the preferred option;
- Outline key elements of the Implementation Plan for the preferred option;
- Identify key stakeholders involvement;
- Summarise the risks and benefits.

7.2. Deliverability

The key features required to successfully deliver a LACC are likely to be:

- A strong commitment from the elected members and the leadership team;
- Clear objectives of the organisation against the expectations of members, community and staff;
- A governance structure that appropriately designates roles and responsibilities and conflict resolution procedures;
- Ensuring the LACC, its operations and decisions are fully transparent;
- A partnership approach to avoid the 'us and them' scenario, with the current Collaboration Agreement forming the foundations of this;
- Financial understanding of the costs of providing services and in particular any additional costs associated with revenue generating opportunities;
- Contract management will be key to managing the interfaces between elected members and potential changes in priorities resulting from available funding or political persuasion;
- Early consideration of 'what if' scenarios to ensure the strategies are in place to deal with eventualities, such as emergency situations or natural disasters.

7.2.1. Delivery Considerations

When considering the changes in the sector in the recent past it is hard to predict the future. In establishing a LACC the Councils have a number of considerations, including:

- The ability to develop internal commercial skills to expand reach into potential markets;
- The ability to source external skills if required to supplement internal capability with regard to tendering;
- Potential to adapt the commercial structure if revenues increase to levels that exceed Teckal exemptions;
- Opportunities to take on other owners (i.e. other Local Authorities) with restructured shareholdings to expand the overall value of the 20% to maintain Teckal exemptions.

There are a broad range of factors affecting the final delivery model; including the timing of West Devon waste services, market characteristics over the short to medium term, services offered and skills required. As there are a number of different permutations, we have not considered all of these in detail; however, the establishment of a LACC does not necessarily restrict expansion and is flexible enough to respond to the on-going market conditions and drivers of the Councils.

In a broader context, the Councils still retain the right to increase taxes or reduce services within the structure.

7.2.2. Transparency

The Councils have to ensure that any trading company they respectively establish is not used as a device for inhibiting legitimate public access to information about local government and local government services.

The overview and scrutiny committee of each Council must be able to exercise their powers in relation to the discharge of local authority functions under the relevant legislation. Under Schedule 12 of the 1972 Act, matters relating to the trading company may be exempt from disclosure to the public where a local authority (or a committee or an executive) meet to consider the affairs of the trading company.

Although Part 1 of Schedule 12A refers to information relating to the financial or business affairs of any particular person (including the authority holding that information) as being exempt, that is qualified by paragraph 8 of Part 2 of Schedule 12A, which states that information is not exempt information if it is required to be registered under, for example, the Companies Act 1985, the Friendly Societies Act 1974 and the Friendly Societies Act 1992 (as updated).

Even if the exemptions in Schedule 12A can be said to apply, a local authority may in the interests of transparency and accountability wish to consider whether it would be in the public interest for discussions to take place in an open meeting forum, or whether the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

PwC view:

- ***The Councils have brought a commercial focus to service delivery through the T18 Programme and a LACC structure could enable the Councils to respond to future market opportunities to generate additional revenue to offset the projected funding gap.***

7.3. Transition and Implementation

The Business Case has identified a preferred option that includes establishment of a LACC to deliver services back to the Councils. This section summarises the key tasks, timing and considerations that will need to be addressed during the transition and implementation phase. The activities to be progressed as a priority include:

- Project management capability assessment and detailed transition and implementation planning;
- Application to HMRC for exemption from Corporation Tax for revenue generated from trading with the Councils;
- Company establishment including registration and relevant articles, shareholder agreements, lease and service contracts with the LACC;
- The TUPE process including calculations of pension liabilities;
- Skills assessment and development to enable commercial response to market opportunities, i.e. tendering.

A more detailed Implementation Plan is at Appendix 7.5.

7.4. Stakeholder Engagement

In progressing with the preferred option a strong focus on stakeholder engagement will be required. Key stakeholders include:

- Elected Members of each of the Councils;
- Internal Staff including administrative, operational (i.e. grounds, maintenance, South Hams Waste) and Frontline staff;
- Waste services across the Councils;
- Other Local Authorities across the South-West;
- Other stakeholders including the Department for Communities and Local Government and neighbouring Councils.

Different engagement strategies will be required for each of these groups and should be defined during the transition planning.

7.5. Risk Management

The Business Case has identified potential risks, pricing and cost impacts which can be mitigated. The Councils have demonstrated that through a shared approach they are able to treat and share risks. The Councils are focused on contingency planning and believe that the establishment of a LACC with shared ownership and consolidated governance and management is an efficient way of managing and mitigating potential risks throughout delivery and operations. There are tactical controls available to the Councils to mitigate risks and contingency, including:

- Long term contracts that transfer risk;
- Cost controls across multiple sites, including staffing;
- Pricing mechanisms that provide flexibility in responding to the market opportunities to generate revenues.

In addition to these mechanisms, there are specific treatments for both process and commercial risks presented by the transition to the preferred option.

7.5.1. Key Risks

A risk assessment of the options was undertaken which identified a number of key commercial risks including:

No	Risk	Treatment
1.	The risk of not being able to meet Member requirements, causing complexity/disputes in the contract	Consideration should be given to roles and responsibilities when transferring services into the LACC
2.	The risk of creating a dual workforce with different employment terms and conditions	The Councils have a legal obligation for transferring employees and mechanisms are available to manage over the longer term.
3.	The risk of complex financial arrangements between entities leading to confusion regarding cross subsidisation	Clear accounting principles to be developed but a consolidated set of accounts could be positive for the Councils.
4.	The risk of perceived differences between ownership, control, returns and rewards	Appropriate structures of share ownership (i.e. A and B shares) can be developed to accommodate and separate voting rights from financial returns.
5.	The risk that skills are not developed to enable successful tendering resulting in anticipated external revenues not being realised	The development of a staged development plan and targeting potential clients provides a realistic platform for expected revenue potential that underpins the costs.
6.	The risk that other Councils set up similar ventures creating more competition	Sales strategy developed at the appropriate time
7.	The risk that this sets a precedent for all LAs that Central Government does not agree with and adverse action is taken or policies implemented	Communications program and engagement with Central Government
8.	The risk services are not provided to the quality and within the budget anticipated	Contractual arrangements include performance measures to provide greater transparency and budget control. Owners still ultimately responsible.
9.	The risk of going over the Teckal thresholds	Options and thresholds considered into decision making framework Positive position to be in and have demonstrated successful ability to further transition to company without need for Teckal exemptions
10.	The risk of the Councils being able to successfully operate a LACC/commercial trading arm in an uncertain funding environment	Consideration of developing skills internally or recruiting externally for key roles will enable transition and long term development.

7.6. Performance Management and Benefits Realisation

Benefits management identifies the performance measures the key executive roles will have responsibility for within the LACC. The preferred option is likely to deliver a number of benefits and they will be measured by and the responsibility of key executives, including:

Benefit	*Measures*	*Responsibility*
Supports the Councils visions and objectives of service delivery and obtaining value for money	Comparative cost of service delivery, pre and post change.	Executive Director, Strategy and Commissioning
The ability to operate commercially with mechanisms to respond to change and include new partners	Expansion and additional of new partners	Executive Director, Strategy and Commissioning
Teckal procurement exemptions	Service transition and engagement with other public bodies	Executive Director, Commercial and Service Delivery
Improved staff mix for the long term that delivers services locally	Staff demographic changes	Director, Customer First
Opportunities to realise additional efficiencies through consolidated waste services across the Councils	Waste services cost per household	Executive Director, Strategy and Commissioning
Potential to generate additional revenues following transitional phase and skills development	Percentage of revenue generated externally (long term)	Executive Director, Commercial and Service Delivery

7.7. Exit Strategy

There are numerous examples of LACCs being established and operating successfully. There are also examples of LACCs being established and then reintegrated back into the Local Authority. An exit strategy is a planned approach to changing the model of service delivery in the event that it is no longer viable to continue to operate a LACC. This could occur for various reasons and, while it is not possible to plan for these individually, there should be sufficient planning in place to facilitate such changes without significantly impacting upon service delivery.

The Councils could consider thresholds of where either additional investment is required or when step in rights should be exercised. There may also be alternate structural options that could be considered, for example external contracting. This type of plan is a form of mitigating potential political risks associated with failure or difficulties of a LACC. There are a range of options available in the event that a LACC is not viable, these include:

- Re-scope the LACC contract: Throughout the contract there will be opportunity to determine the Councils funding against its service agreement with the LACC, and in the event that funding is not available for the service levels, agreement may be reached to reduce or cut services;
- Transition back to the Councils: In the event of failure of the LACC there may be services that could be transferred back to the Councils, although this will need to be considered in the context of the operating model at the time;
- Outsource: In the event of failure of the LACC there may be services that could be outsourced.

As outlined earlier, other Local Authorities have established LACCs for certain commercial services which have continued to work and expand. Outsourcing of services has proven successful in maintaining service delivery, such as waste services in West Devon. There have been examples where services have been outsourced and brought back in house after not realising the savings anticipated.

In the event of failure the Councils will be responsible for any transitional or retender costs associated with the changes. In the implementation phase an exit strategy will be developed that considers:

- Continued provision of statutory services;
- Assets, contracts and lease transfers or novation;
- Treatment of supplementary services;

- Loss making operations and timeframes for decision making.

7.8. Management Case Summary

The management case demonstrates that the LACC proposal and target date of 1 April 2017 is achievable (notwithstanding the decision to be made in respect of the West Devon waste service):

- The LACC provides:
  - a level of flexibility to respond to future market conditions;
  - is deliverable and appropriately allocates and shares risks across the Councils;
  - has greater risk from set up costs;
  - presents greater opportunities to generate revenue in the future to offset the project funding gap.
- An implementation plan includes:
  - Seeking legal advice on establishment;
  - Developing calculations for pensions;
  - Application to HMRC for Corporation Tax exemption.

PwC view:

- ***The LACC model is deliverable and an implementation plan has identified the key requirements to be progressed as a priority.***

8. Conclusions and Recommendations

8.1. Summary

The objectives of this Business Case were to assist in the creation of a detailed business case and implementation plan. In particular, the business plan should concentrate on a comparison between the two key options under consideration:

- **"As is"** – The continuation of the current arrangements of in-house service delivery with some outsourced services (e.g. Leisure Centres and the West Devon waste collection, grounds maintenance and street cleansing service); or
- **"Transferring all Council services to a LACC"** – where the LACC is jointly owned by South Hams District and West Devon Borough Councils.

This was to be done against a requirement to preserve service delivery standards, without imposing an additional Council Tax burden on the local population.

In undertaking this engagement we have sought to:

- Confirm the drivers and need for change as identified by the Councils;
- Clearly define the scope of services to be provided by the new entity;
- Provide an analysis of potential business growth, market share, income generation and trading opportunities;
- Identify and assess the technical options available, in particular, whether a Local Authority Controlled Company is flexible, sustainable and represents value for money;
- Identify the commercial implications of the preferred option;
- Identify and assess the cost and revenue implications of the preferred option;
- Identify the change management requirements and implementation plan for the preferred option;
- Recommend an option for the provision of Council services that is flexible, sustainable and represents value for money.

8.2. Conclusions

Our assessment concluded that:

- There are clear strategic imperatives that support the development of innovative solutions to the projected future funding gap;
- The remaining 'As Is' option is unlikely to be a sustainable long term solution with the additional risk of not taking action potentially constraining the Councils to increasing taxes or reducing services;
- The Councils have established an effective operating model, through T18, delivering all services end to end through Customer First, Commercial Services and Support Services with a clear steer and monitoring interface provided by Strategy and Commissioning and functional allocation of responsibilities for services delivery;
- This is an appropriate platform from which to continue the development of a LACC;
- There are potential market opportunities available to the Councils within their local regions, primarily with adjacent Local Authorities and other Public Sector entities, but also some private sector opportunities;
- The establishment of a LACC:
  - Enables the Councils to build upon the structural changes made as part of the T18 Programme;
  - Will incur setup costs of c£400k that should be paid back by April 2020; and
  - ;
  - Presents opportunity to generate additional revenues not available under the 'As Is' option if the identified risks are managed appropriately.

8.3. Recommendations

We recommend that the Councils:

- Seek confirmation / guidance from HMRC regarding an exemption from paying Corporation Tax on profits related to income derived from services provided to the Councils. This should be undertaken prior to incurring further significant cost as it is fundamental to the assumptions within this report;
- Seek confirmation / guidance from LGPS on how the current pension deficit should be treated;
- Obtain legal advice and support to deliver the proposed corporate and associated share structure of the LACC to ensure that it meets both the governance and spend requirements;
- Obtain legal advice in relation to the Councils' vires to trade the identified services, and ensure LACC constitution has the flexibility required for future change in scope if envisaged as part of the LACC strategy;
- Obtain legal advice to confirm that the business plan conforms with State Aid requirements and public procurement regulations;
- Obtain legal support and advice in relation to Pensions, TUPE and employment matters;
- Subject to confirmation of the above bullet points that the Councils proceed with establishing the LACC.

Business Case Appendices

1. **General Appendix:**
    1.1. Glossary of key terms
    1.2. General assumptions
2. **Introduction:**
    2.1. 5 Case overview diagram
    2.2. West Devon waste options
3. **Strategic Case:**
    3.1. Strategic context
    3.2. PwC Understanding of Local Government
    3.3. Future funding for local authorities
    3.4. Business Rates Uncertainty
    3.5. Regional Context
    3.6. Current Operating Model
4. **Economic Case:**
    4.1. Market overview
    4.2. Potential contracts within the SW area (0 – 4 years)
    4.3. Responding to the Market
    4.4. Business Needs and Service Requirements
    4.5. Options Assessment
    4.6. Options assessment
    4.7. MCA table
5. **Commercial Case:**
    5.1. Operational Requirements
    5.2. Commercial Structure
    5.3. Governance
    5.4. Corporation Tax
        5.4.1. Mutual trading and ALMOs
        5.4.2. Transfer pricing and diverted profits tax
    5.5. VAT
6. **Financial Case:**
    6.1. Funding split
    6.2. Current net expenditure
    6.3. Cashflow implications of establishing a LACC
    6.4. Costs and other implications of establishing a LACC
    6.5. Opportunities as a result of establishing a LACC
    6.6. Assumptions

7. Management Case:

7.1. Transition

7.2. Key Considerations

7.3. Change Management

7.4. Stakeholder Engagement

7.5. Implementation Plan

7.6. Risk Matrix

7.7. Post Implementation Review

7.8. Future Considerations

1. General Appendix

1.1. Glossary of key terms

Glossary of key terms	
2016/17	Financial year 1 April 2016 to 31 March 2017
2017/18	Financial year 1 April 2017 to 31 March 2018
2018/19	Financial year 1 April 2018 to 31 March 2019
2019/20	Financial year 1 April 2019 to 31 March 2020
2020/21	Financial year 1 April 2020 to 31 March 2021
2021/22	Financial year 1 April 2021 to 31 March 2022
2022/23	Financial year 1 April 2022 to 31 March 2023
2023/24	Financial year 1 April 2023 to 31 March 2024
A or B Shares	Different class of ordinary or preference share
ALMO	Arm's length management organisations
Arm's length transaction	Transaction at fair market value
Business rates	Rates charged on business related properties
Capital allowances	Tax related deduction relating to the purchase of capital assets
Capital gains	Profit from the sale of an asset or investment
Cashflows	The payment of relevant expenditure
Commercial Services	Councils' operating model as part of T18 programme
Council 'As Is'	The position of the Council if the option to form a LACC is not chosen
Council under a LACC/services in a LACC	The position of the Council if the option to form a LACC is chosen
Customer First	Councils' operating model as part of T18 programme
Employers NI	The employers contributions on their employees earnings and benefits
Expenditure	The costs matched to the year incurred and reported in the P&L
FCC	FCC Environment (UK) Limited
FD	Finance Director
Field services	Councils' operating model as part of T18 programme
Finance Lease	Acquisition of assets under finance/borrowings. Assets recognised on Balance Sheet
Financial and accounting period	The period between which the financial statements are prepared. In the case of the Council they report 1 April to 31 March
FY20	Financial Year 1 April 2019 to 31 March 2020
Group/consortium relief	Tax reliefs available to groups or consortia of companies
HMRC	Her Majesty's Revenue & Customs
HR	Human Resources
ICT	Information and Communications Technology
Income	Councils' revenues

Glossary of key terms	
Indexed/indexation	Monetary amounts inflated using assumed compounded annual inflation of 2.5%
Joint Venture company	Company established by 2 or more parties to pool resources for the purpose of accomplishing a specific task
Know how	Knowledge and experience gained from the establishment of a LACC
LA	Local Authority
LGPS	Local Government Pension Scheme
Mark up	Amount added to the cost price of goods or services to cover overheads and profits
Multi-criteria analysis	Decision-making tool used to evaluate problems when one is faced with a number of different alternatives and expectations.
Net Expenditure	Councils' expenditure less income
Nominal prices	Prices or values are not adjusted for inflation
P&L	Profit and Loss account
Payback	Time lag before benefits of forming the LACC outweigh the costs
Payment on Accounts Scheme	Companies with a VAT liability of over £2.3m are required to make interim payments during a VAT quarter
PHI Insurance	Permanent health insurance
Preference Shares	A share which entitles the holder to a fixed dividend, whose payment takes priority over that of ordinary share dividends.
Profits	Earnings from the delivery of services
Real prices	Prices or values are adjusted for inflation
Reserved Matters	Shareholders of particular classes may be granted veto rights in respect of specific reserved matters
Revenue/turnover	Sale of goods and services
S151 role	Responsible Financial Officer
Schoolsnet	Web based Schools guide
South Hams	South Hams District Council
State Aid	Any advantage granted by public authorities through state resources on a selective basis to any organisations that could potentially distort competition and trade in the European Union (EU
Strategy and Commissioning	Councils' operating model as part of T18 programme
Sunk cost	A cost that has been incurred and cannot be recovered
Support Services	Councils' operating model as part of T18 programme
T18 programme	Transformation Programme 2018
Teckal exemption	Permission for a Public Authority, in specified circumstances, to procure direct from an external company in which it has control.
Third parties	Other entities or individuals other than the LACC or the Councils
Treasury 5 Case Modelling approach	Guidance from the Treasury Greenbook business guidance
Treasury Greenbook business guidance	HM Treasury guidance for public sector bodies on how to appraise proposals before committing funds to a policy, programme or project
TUPE	Transfer of Undertakings (Protection of Employment) Regulations 2006
Unindexed	Monetary amounts have not been inflated using the assumed compounded 2.5%

Glossary of key terms	
Use of brackets	This represents a subtraction or a funding requirement
VAT	Value Added Tax
West Devon	West Devon Borough Council

1.2. General assumptions

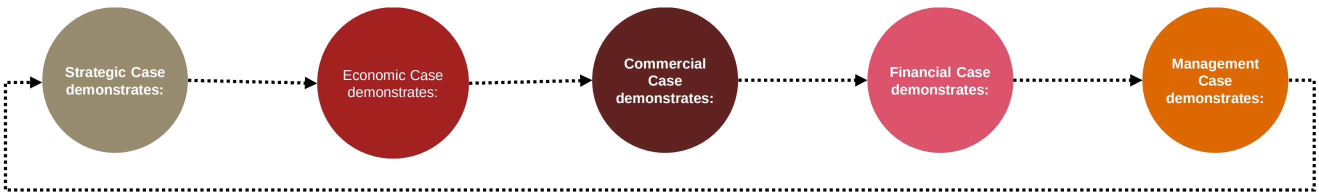
	'As Is' Current operating model, assuming West Devon Waste retendered as outsourced	LACC LACC including delivery of waste services across SH&WD
South Hams District Council		
Staff costs retained	346 combined	14
Staff costs transferred	n/a	332
Assets	Retained by the Council	Retained by the Council and leased to the LACC
Asset utilisation	Retained	Transferred
Current Leases - assets	Retained	Retained
Current Lease revenue	Retained	Retained
Pensions liability retained	Retained	Retained and guarantee provided to fund for current liability.
VAT claimable	All	All
Corporate Tax payable	n/a	Likely only payable on profits generated from activity outside of the Councils.
Payments to LACC	n/a	Payment based on current service levels offset by lease payable by the LACC
Waste services	Retained	Transferred to the LACC
Waste revenue	Retained	Transferred to the LACC
Current revenue- i.e. harbours, car parks, locational	Retained	Retained by the Council
Other revenue- i.e. BCP	To be agreed	To be agreed
Dividends from LACC	n/a	Payable to the Council

West Devon Borough Council		
Staff costs retained	<<this information has been removed due to commercial sensitivities>>	11
Staff costs transferred	n/a	<<this information has been removed due to commercial sensitivities>>
Assets	Retained	Retained by the Council and leased to the LACC
Asset utilisation	Retained	Transferred
Current Leases - assets	Retained	Retained

	'As Is' *Current operating model, assuming West Devon Waste retendered as outsourced*	*LACC* *LACC including delivery of waste services across SH&WD*
Current Lease revenue	Retained	Retained
Pensions liability retained	Retained	Retained and guarantee provided to fund for current liability.
VAT claimable	All	All
Corporate Tax payable	n/a	Likely only payable on profits generated from activity outside of the Councils.
Payments to LACC	n/a	Payment based on current service levels offset by lease payable by the LACC
Waste services	Outsourced	Transferred to the LACC
Waste revenue	Outsourced to FCC for recyclables and included in contract price.	Transferred to the LACC
Current revenue- i.e. car parks, commercial units, locational	Retained	Retained by the Council
Other revenue- i.e. BCP	To be agreed	To be agreed
Dividends from LACC	n/a	Payable to the Council

2. Introduction Appendix

2.1. Treasury Green Book 5 Case Modelling Approach



Strategic Case demonstrates:
- Consider the strategic drivers of government impacting on Local Authorities ability to deliver services
- Review strategic context and identify if there is a need for change

Economic Case demonstrates:
- Identify a number of options that suitably address the needs of the Councils
- Consider the risks and assess the options across a comprehensive range of criteria
- Identify a preferred option that meets the strategic drivers and need

Commercial Case demonstrates:
- Identify the commercial issues relevant to the preferred option
- Consider if there are any show stoppers that would preclude the Council from taking action
- Consider if the Councils are capable of controlling the commercial issues and risks

Financial Case demonstrates:
- Review the previous financial appraisals undertaken by the Councils and align key assumptions
- Identify the potential financial scenarios and their respective benefits
- Identify if the financial implications of the preferred option

Management Case demonstrates:
- Identify the management requirements
- Identify the key risks and what is required to manage them appropriately
- Identify governance and responsibility for key management functions
- Outline an implementation plan that incorporates key transition requirements

2.2. West Devon Waste Options

Overview

FCC are currently contracted to West Devon Borough Council to provide waste collection, recycling collection and street cleansing services for a period of 7 years, with an expiry date of 31 March 2017. As part of this contract, FCC utilise depots currently owned or leased on a long term basis by West Devon.

We have been instructed to assess the viability of establishing a LACC and consider the implications of incorporating these waste services (including street cleansing) into the LACC after the expiry date. We were briefed to look at the timeframe for incorporating the West Devon Waste and Cleansing contract into the LACC in terms of feasibility and cost, as well as exploring the alternative options for the delivery of the service. We considered efficiencies which might be gained through delivery of joint services through the LACC, whilst recognising the current individual service configuration.

We were informed by West Devon Borough Council that without the establishment of a LACC, waste services in West Devon would continue to be outsourced and retendered. Although our engagement did not include any in depth analysis and/or service redesign, we have considered the previous work undertaken by Grant Thornton (GT), which identified a number of opportunities, and our assessment has focussed on maximising the benefits associated with incorporating these services into the LACC.

This section summarises the findings of our analysis and should be read in conjunction with the financial appendix, where the financial implications have been considered.

Background

The contract included three Lots i.e. Waste and Recycling; Street Cleansing; and the Cleansing and Maintenance of Public Conveniences. In 2009, FCC tendered for and were successful across the three Lots as their tender price included a discount for multiple award. Additionally, FCC were also successful in an option of managing (i.e. treatment including selling) of the dry recyclables collected.

We were **NOT** asked to look at providing a combined service delivery model for waste collection, this would be a completely separate piece of work to be undertaken by the Councils.

South Hams reviewed their service format in 2012/13 and West Devon are doing this currently through the work of their waste group.

Following reports to both Councils there was no appetite for a pan Devon waste solution but there was an agreement to continue to work together to align materials collected, procure jointly where appropriate and to look to work together in clusters in the future. The real block to achieving cluster working at present is the absence of a platform/or mechanism to deliver services in clusters.

Our approach

With regard to the outsourced waste and street cleansing services in West Devon we sought to keep the considerations separate from the concept of the Councils establishing a LACC. This proved to be complicated as a number of elements are intertwined. To make the distinction we:

- Considered the implications of the available options for inclusion within the LACC against the 5 cases in the business case;
- The financial implications of the options on the LACC;
- Considered the Devon wide assessment of waste services and the GT report into options for waste service delivery.

In conjunction with the Councils we identified a number of options that we have considered.

This has been informed by the Councils and other advisors including White Young Green who have worked with West Devon Borough Council on the waste contract and have a detailed understanding of the costs and implications of the current FCC contract and market conditions.

Options

In consultation with the Councils a number of options were identified and their relative impacts on each of the Council and the LACC considered. This section summarises the options and there relative impacts from a cost perspective and potential impacts on each entity.

Option 1: Included in LACC from commencement (April 2017)

Cost impact: Set up costs could be shared with the overall LACC establishment.

Impacts:

West Devon Borough Council	*South Hams District Council*	*LACC*
Impacts on timing of ordering assets required and resourcing to meet time requirements.	Opportunity to generate efficiencies through economies of scale through combined management.	• Opportunities to redesign service to timeframe i.e. garden-waste. Potential efficiencies to be realised from year 2/3. • Flexibility to introduce service changes i.e. chargeable garden waste at a point determined by the Members.

Option 2: Extend current contract with FCC for [6/12] months

<< Section removed – commercially confidential>>

Option 3: Continue to outsource current services and re-tender

<<Section removed – commercially confidential >>

Option 4: Managed service contract utilising new assets procured by West Devon Borough Council

<<Section removed in respect of possible contract negotiations>>

Considerations for establishment of a LACC

We considered the implications of including the services currently provided by FCC in the LACC in line with the 5 case business case adopted for consideration of a LACC as a whole. This section summarises the key findings for each of the five cases.

Strategic Case

The Business Case identified that recent Central Government policy decisions are significantly impacting the local authority funding model and that local authorities will need to be innovative if they are to be able to continue to provide services that meet their community's' needs.

There is a need for action to be taken as the current contract with FCC is due to expire on 31 March 2017. Previous work undertaken by GT identified that a range of options were available and that, even with retention of the different collection models across the Councils, there are likely to be efficiencies in management and a reduction in cost as a result of not having to pay the contractor's profit margin. These are further explained in the financial case.

PwC view:

- ***Strategically, the inclusion of waste and street cleansing services into a combined LACC aligns the service offerings across the Councils.***

Economic Case

The market analysis undertaken identified that a large portion of local authority budget spend across the South-West is on waste and street cleansing services and that a number of local authorities across the region already outsource these services.

The options appraisal assumed that the LACC would provide waste and street cleansing services across both Council areas for comparative purposes against the As Is model; however, consideration was also given to the timing of consolidating these services into the LACC.

Inclusion of these services within the LACC presents the Councils with a better opportunity to respond in a coordinated manner with larger scale and service offering to meet market and future tender requirements. A consolidated services presents the LACC with experience in different collection methods (differences between the Councils) and the ability to leverage items such as trade waste opportunities where South Hams District Council have experience.

Having an outsourced contract would likely increase the contract management complexity within the Councils as they would be managing the LACC, as well as another large scale contract. The recyclables market fluctuates and currently back to the levels incorporated into current FCC contract.

PwC view:

- ***Economically the inclusion of waste and street cleansing services appears to represent an opportunity to generate some additional efficiencies, primarily through management as waste collection would remain as is, in meeting the needs and expectations of the West Devon community.***
- ***Inclusion of waste and street cleansing services into the LACC presents an opportunity to maximise the revenue potential through a higher overall Teckal threshold for additional revenue.***

Commercial Case

The commercial case considered the organisational implications that the inclusion of waste and street cleansing within the LACC is likely to result in. This includes:

<<This information has been removed due to commercial sensitivities>>

Inclusion of these services within the LACC presents West Devon with an increased contractual footing as the overall value of the services purchased from the LACC would be greater. Keeping these services separate would significantly distort the value of services purchased from the LACC when compared to South Hams District Council.

PwC view:

- ***The inclusion of waste and street cleansing services in the LACC improves the balance of services provided to the Councils by the LACC.***
- ***Continuation of outsourced arrangements would significantly distort the value of services purchased by West Devon Borough Council from the LACC, i.e. could be in excess of 20%.***

Financial Case

The details are included in the financial appendix. The key findings include:

- Ultimately inclusion of these services within the LACC improves overall performance;
- Adoption of Option 2 – 6 month delay - could provide operational cost savings of c£<< figures removed – commercially confidential>> by 2024 and payback of the Combined costs of forming the LACC by 2021;Scope to generate future combined efficiencies and third party profits from the establishment of an in-house operation; and
- Establishment of a LACC is able to respond to either of the options considered.

PwC view:

- ***Financially the inclusion of waste and street cleansing services improves the payback period.***
- ***The assumption of no additional revenue for the LACC generated from third parties presents an opportunity to appropriately plan and not rush the process of incorporating within the LACC.***

Management Case

The management case presents an opportunity to leverage existing South Hams District Council experience in managing and operating waste collection, recyclables and trade waste services to provide greater benefits to the LACC.

The inclusion of these services in the LACC will increase the transfer requirements and management responsibility; however, over time the skills developed will provide the LACC with an improved position if tendering for external waste collection, trade waste or street cleansing contracts.

With the current FCC contract ending on 31 March 2017, it is likely that this option would create additional pressure on establishing the LACC. The other options that provide more time to consider management implications and efficiencies present the opportunity to better plan for the transition.

PwC view:

- ***The establishment of a LACC is not dependent on inclusion of waste and street cleansing services in West Devon.***
- ***The LACC is able to accommodate the option identified through provisions and transition timing.***

Summary

Our assessment of waste and street cleansing services in West Devon found:

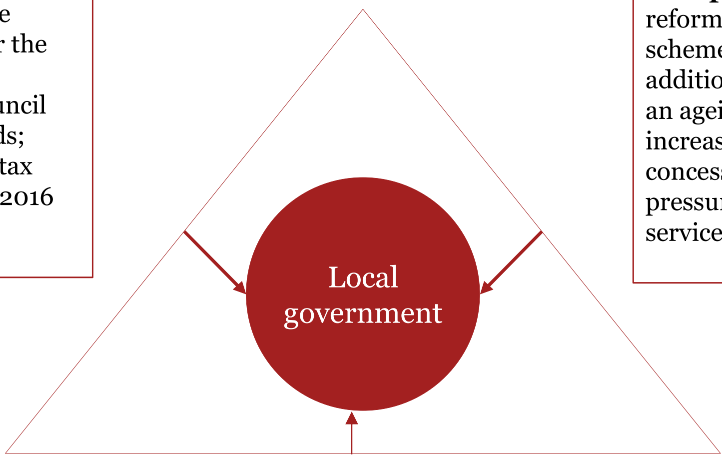
- That inclusion of these services into the LACC improves the overall offering of the LACC;
- That inclusion of these services better represents West Devon Borough Council interest in the LACC as a proportion of the potential service fee;
- The transition phase of the LACC does not need to be driven by these services as management mechanisms are available to respond to West Devon Borough Councils decision on its preferred option.

3. Strategic Case Appendices

3.1. Strategic Context

The 'English Devolution Local Solutions For A Successful Nation (2015)' paper identified that the Local Government Pressures include:

Funding pressures: A 40 per cent real terms cut to core government funding over the life of the parliament; consistently reducing council tax referendum thresholds; £1bn cut to local council tax support funding to April 2016



Cost pressures: Care service reforms (deferred payment schemes, social care cost cap); additional public health duties; an ageing population; increasing costs of concessionary fares schemes; pressures on social housing services; inflation

Other pressures: business rate appeals; welfare reform, including the benefit cap, social sector size criteria and Universal Credit; potential changes to interest rates

In order to avoid cuts to services, authorities are increasingly looking for ways to restructure service delivery to ensure that services remain fit for purpose in the context of smaller budgets.

A number of conclusions of the paper include:

- The Government must recognise that local government is fast approaching a state where, under the current circumstances, continued efficiency savings alone are not enough to tackle funding cuts for some councils
- Local authorities see a way ahead and many are already working closely together and with other local partners to reform and restructure local services by managing demand and agreeing joint objectives.

The Local Government Association responded to the Spending Review and identified:

- The refreshed Future Funding Outlook analysis suggests if things do not change, local government is set to face a funding gap of £9.5bnby 2020. With limited scope for further efficiencies, this can only put at risk valued public services
- Councils have been increasingly inventive in managing costs through collective purchasing, shared services and smarter contract management. Their appetite for innovation has been a major contributing factor to the success in tackling cuts. Working on their own and in partnership with other councils and organisations, they have repeatedly demonstrated their ability to do things differently, save money and improve the services on which their residents rely.

3.2. PwC Understanding of Local Government

PwC undertake an annual survey, 'Local State We're In'. In 2015 the survey asked over 100 Chief Executives and Leaders of local authorities around Great Britain about the challenges facing local government and their responses to them.

Five years on from our original 'Local State We're In' survey, councils have been successful in managing the significant cuts to date. But local authorities are now facing challenges on all fronts: financial pressures continue while demand and public expectations grow with the way ahead being challenging, but full of opportunity that the sector has the confidence to tackle and face.

Chief Executives and Leaders have recognised the need to do things differently, looking beyond their organisational boundaries and taking a place-based, whole systems approach to solving the challenges of growth and reform in their areas.

As the realisation grows that councils cannot operate in isolation, partnership working has also risen up the agenda.

Chris Buttress, PwC partner and local government leader comments:

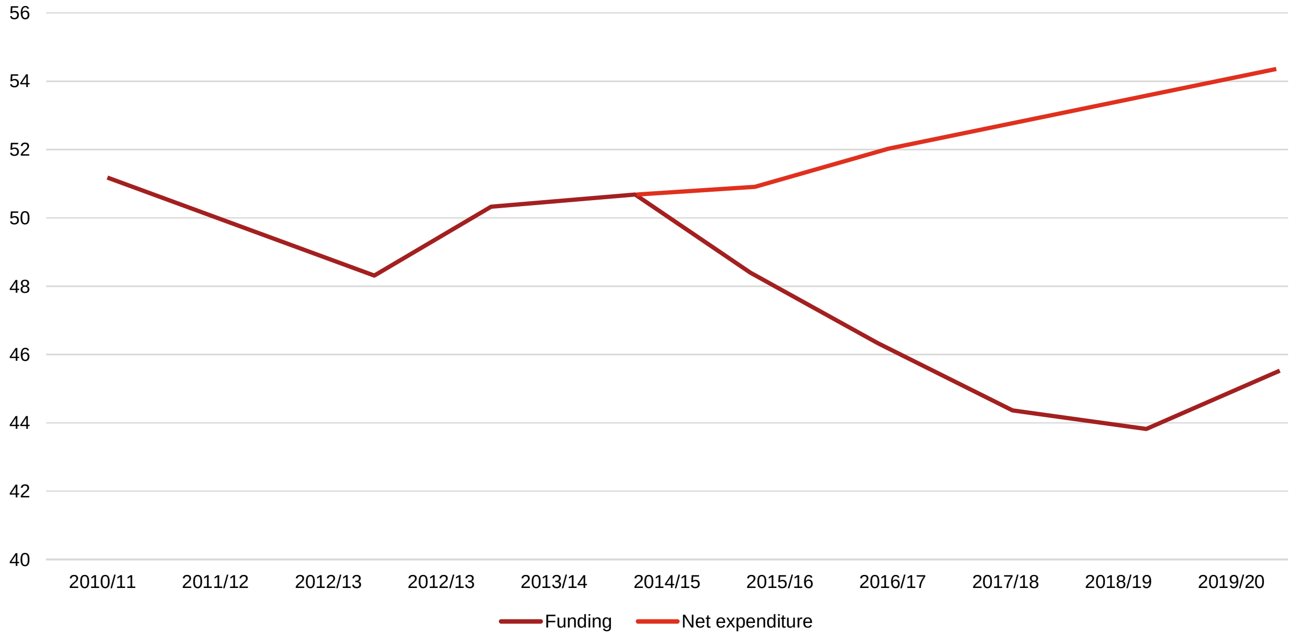
"It is clear, speaking with council leaders and their Chief Executives, that Councils are now considering more radical options – from rethinking relationships with customers and communities and better use of digital technologies, to deeper collaboration with partners. The business model of the public sector is changing rapidly as decision makers are considering what is the role of the public sector within a local area."
"Local authorities have largely responded well to the budget gap of the last four years. They are now anticipating having to do the same again, with less and less certainty of how to achieve this. We have no doubt that the future business model for public services will change significantly in the next four years - and those leading the sector in localities will be the ones who will deliver this new model – changes won't all necessarily be centrally driven."

3.3. Future funding for local authorities

The Future Funding outlook for councils 2019/2020 (Interim 2015 Update) identified:

- Councils are continuing to balance their budgets and fulfil their statutory obligations as well as delivering a range of services to promote growth and community cohesion. Each year they close the funding gap in the face of funding cuts and expenditure pressures;
- With social care and waste spending absorbing a rising proportion of the resources available to councils, funding for other council services drops by 35 per cent in cash terms by the end of the decade, from £26.6bn in 2010/11 to £17.2bn in 2019/20. To put this in context, this £9.3bn drop is greater than the £7.7bn total expenditure (in 2014/15) on central services, 'other' services and capital financing combined;
- The challenge cannot be solved by back-office efficiencies alone;
- There is also the introduction of the single state pension, which will increase employers' national insurance contributions for councils with no compensating new burdens payment. Different local areas will have their own local pressures and priorities, such as policies on the introduction of the Living Wage for council staff. These are dependent on local circumstances which present uncertainty and potential risks; and
- We can now bring together the analysis of projected income and expenditure trends to form a picture of Local Authority funding overall. This shows that the overall funding gap starts at just over £3bn in 2015/16 and reaches over £10bn by 2018/19, before shrinking to £9.5bn by 2019/20.

This identifies a potential reduction of approximately 20% in real terms. Income against expenditure 2010/11 to 2019/20 demonstrates:



3.4. Business Rates Uncertainty

Business rates are a property tax paid by occupants of non-domestic properties which Local authorities collect. In England, this function falls to district councils. Before April 2013 all business rate income collected by councils formed a single, national pot, which was then distributed by government to councils in the form of formula grant. The Local Government Finance Act (2012) gave local authorities power to keep half of the business rate in their area. The other half being used by Central Government to provide grant funding for Local Authorities.

The paper 'Business Rate Retention: the story continues (March 2015)', outlines that the primary challenges are the level of financial risk that councils face due to appeals and dependence on a small number of large businesses for a significant proportion of business rate income. It also identified that mechanisms which were to encourage local authorities to grow their economies are a counterproductive feature of the new system.

A Briefing Paper to the House of Commons on Business Rates (April 2016) outlines a number of reliefs and discounts including:

- Permanent reliefs include:
  - Premises occupied by small businesses in England
  - Properties occupies by charitable organisations
  - Rural rate relief for public houses or petrol stations in rural areas
  - Discretionary relief.
- Temporary reliefs include:
  - Flood relief, i.e. business affected by severe flooding in 2014 were entitled to three months relief
  - Retail relief is a discount of £1,500 on premises with a rateable value up to £50,000
  - Reoccupation relief is a 50% discount for new occupants in previously empty premises
  - Enterprise zones where relocating provides for 100% discount for 5 years.
- Local newspaper relief is a discount of £1,500 for office space
- Empty properties are exempt for three months and six months for industrial and storage premises.

The Briefing Paper also outlines there are a number of business rates supplements available to Local Authorities, including levying a supplement. However the only supplement scheme in use so far is a 2%

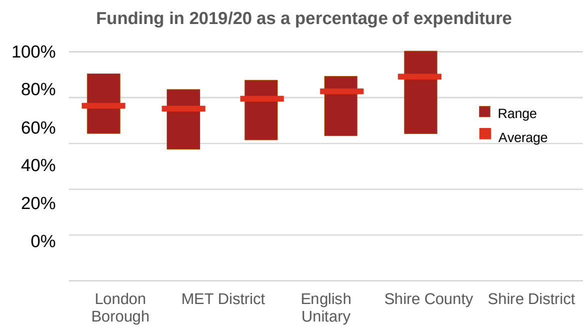
supplement for Crossrail in London. There may also be powers available through devolution deals to directly elected mayors in the future.

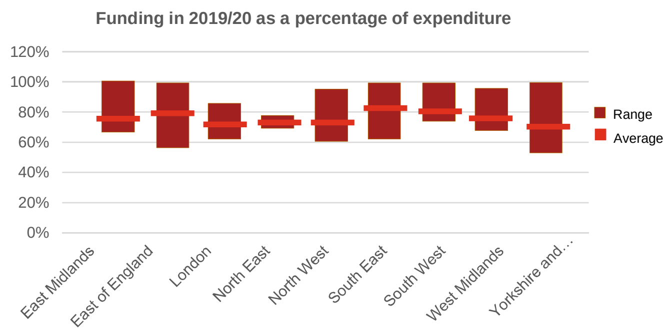
Business rates provides complexity for Local Authorities and a number of these risks are currently impacting the Councils, with business rate appeals potentially impact the funding available.

In summarising the national context, there are significant policy drivers of Central Government funding that will continue to influence the way local authorities deliver services and value for money.

3.5. Regional Context

In considering the national drivers of changes in local services, the Future funding outlook for councils from 2010/11 to 2019/20 Local Government Association (July 2013) identified impacts on authorities and regions. The charts below show the total funding level for the group (i.e. total income as a percentage of expenditure), as well as the maximum and minimum funding level for individual councils within that group and the region.





This demonstrate the variance between authorities and also within classes of authorities. All authorities are experiencing cuts in funding and are having to take difficult decisions to deliver savings over the forthcoming period. This demonstrates that County and District Councils in the South West have the highest percentage of funding requirement when compared to expenditure, representing they have a higher reliance on external funding than other authorities. Simply this shows that the Councils are comparatively more reliant on grant funding than other Local Authorities.

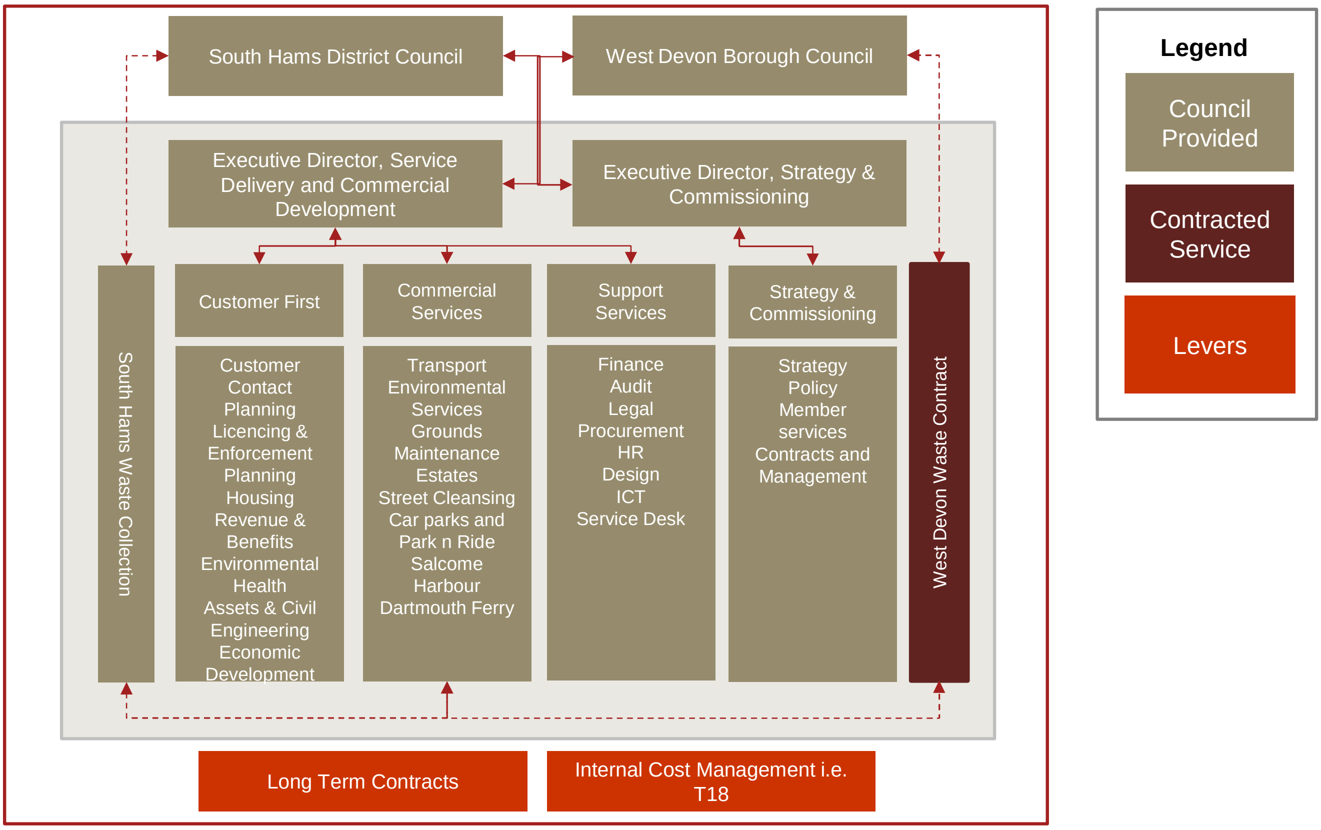
3.6. Current Operating Model

Section 3.3.1 provided an overview of the main functions of the Councils operating model and the following figure demonstrates our understanding of the current model. The key features of the operating model established through the T18 Programme are:

- The Councils share management and resources and deliver majority of services in-house;
- West Devon Waste is contracted whilst South Hams waste services are in-house;
- Leisure services management is currently being procured and likely to be a long term contract of 25 years;
- Current levers available to the Councils to drive change and realise efficiencies include, contracting for delivery of services (i.e. Leisure and West Devon Waste) or cost management for efficiencies and productivity improvements;
- No additional revenue is generated from providing existing services to other parties.

The Councils do generate some revenues through leasing out existing office space and charging for services within their existing structure with the majority of their revenue coming from Council Taxes, Business Rates and Government Grants.

Current Operating Model



It is evident that the current model is not able to respond to or maximise the opportunities presented by the market overview in assisting the Councils to offset the project funding gap. A broader options assessment was undertaken to consider how best to maximise these opportunities.

4. Economic Case Appendix

4.1. Market Size

Trying to identify the market size and penetration potential for the range of services provided by the Councils presented a number difficulties. The key difficulties were with regard to scope, timing and locational influences. We established a high level assessment to try and quantify the market size for services provided by the Councils. The approach adopted considered other local authorities and their budget spend on services. This was then broken down further to focus on key services that could potentially be provided by the Councils. To provide further support we have identified a range of contracts anticipated to be released to market within the near future.

Our research identified that the combined Local Authorities in the South West have a budget spend of approximately £4.6bn. (Source: Local authority revenue expenditure and financing England: 2015 to 2016 budget as released by the Department for Communities and Local Government.)

The market analysis did not consider in detail budgets of Parish Councils across the region due to the lack of information available. This presents further opportunity to leverage the Councils assets and service delivery model in addition to those identified for larger authorities across the South West region.

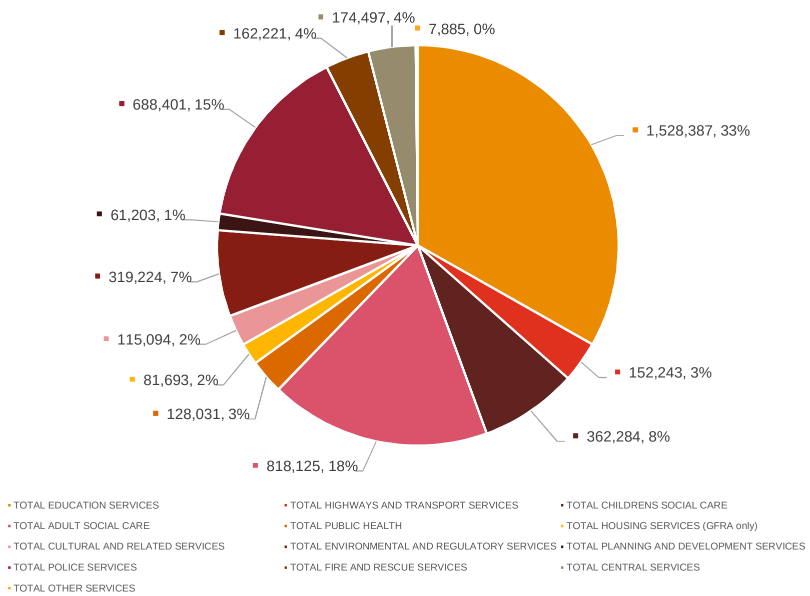
The Outsourcing Yearbook 2016 produced by the National Outsourcing Association outlines that research conducted by NelsonHall showed that UK public sector outsourcing deals rose by 168 percent in 2014. 75 percent of these were kept within the UK and over half were first time deals. IT was the most widely outsourced sector with business services, contact centre services, HR, pensions and payroll are now commonly outsourced.

The Briefing Paper Local government: alternative models of service delivery to the House of Commons (Number 05950, 20 May 2016) identified that there is no central repository of statistics showing the number of local authority companies, their revenue, capitalisation, or functions. Localis's March 2015 report Commercial Councils states:

- 94% of authorities share some services with another council;
- More than half of councils (58%) own a trading company, and at the rate it is increasing, full coverage by 2020 is a possibility;
- A majority of councils (57%) operate a joint venture with the private sector;
- Over a third of councils are using entrepreneurial methods in areas such as waste (46%), leisure and tourism (38%), IT/back office (38%) and housing (36%);
- Without these entrepreneurial activities, eight out of ten councils say they would have to cut services and raise taxes.

Localis's report provides the following table showing income, expenditure and profit of English local authority external trading services with a combined profit of approximately £300m:

(£m)	Income	Expenditure	Profit
2006-07	1093	799	294
2007-08	1104	792	312
2008-09	1139	828	311
2009-10	1158	886	272
2010-11	1130	838	292
2011-12	1131	815	316
2012-13	1092	791	301
Average	1121	821.3	299.7



South Hams District Council and West Devon Borough Council

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

Local authority	Total education services	Total highways and transport services	Total children's social care	Total adult social care	Total public health	Total housing services (GFRA only)	Total cultural and related services
North Somerset UA	112,947	9,783	21,225	57,229	9,229	9,406	5,271
Cornwall UA	252,088	24,028	65,773	140,571	25,644	15,770	19,742
Plymouth UA	133,315	16,325	45,646	71,965	14,925	5,976	8,031
Torbay UA	53,190	5,235	30,183	39,096	8,890	3,449	6,068
Devon	417,868	54,833	82,355	210,280	26,767	2,841	11,313
East Devon	0	-1,974	0	0	0	1,271	3,340
Exeter	0	-3,740	0	0	0	3,351	5,505
Mid Devon	0	-209	0	0	0	1,033	714
North Devon	0	-1,577	0	0	0	1,703	1,437
South Hams	0	-1,784	0	0	0	1,493	1,416
Teignbridge	0	-1,952	0	0	0	2,229	2,659
Torridge	0	-427	0	0	0	1,247	876
West Devon	0	-296	0	0	0	1,139	655
Poole UA	65,748	6,801	19,899	41,518	7,344	4,444	7,001
Dorset	248,577	26,602	39,658	120,558	15,156	139	8,895
East Dorset	0	-108	0	0	0	1,179	1,274
North Dorset	0	-294	0	0	0	410	244
Purbeck	0	-121	0	0	0	845	466
West Dorset	0	-1,299	3	0	0	1,736	1,769
Weymouth & Portland	0	-996	4	0	0	1,703	1,251
Forest of Dean	0	-26	0	0	0	925	933
Stroud	0	-200	0	0	0	1,453	2,076
Tewkesbury	0	-354	0	0	0	1,145	714
Somerset	244,654	29,095	57,538	136,908	20,076	6,015	10,338
Mendip	0	-1,090	0	0	0	4,033	1,103
Sedgemoor	0	-425	0	0	0	1,428	1,775
Taunton Deane	0	-2,486	0	0	0	2,075	2,361
South Somerset	0	-823	0	0	0	2,592	2,978
West Somerset	0	-238	0	0	0	663	324
Dartmoor National Park Authority	0	-3	0	0	0	0	2,405
Exmoor National Park Authority	0	-37	0	0	0	0	2,160
	1,528,387	**152,243**	**362,284**	**818,125**	**128,031**	**81,693**	**115,094**

Revenue Account Budget (RA): 2015-16 data
Net current expenditure (£ thousand)

Local authority	Total environmental and regulatory	Total planning and development services	Total police services	Total fire and rescue services	Total central services	Total other services	Total service expenditure
North Somerset UA	20,194	637	0	0	7,462	0	253,383
Cornwall UA	68,175	5,647	0	21,234	28,025	0	666,697
Plymouth UA	23,934	1,770	0	0	16,819	157	338,863
Torbay UA	12,842	4,074	0	0	8,305	692	172,024
Devon	37,360	6,784	0	0	20,185	0	870,586
East Devon	7,562	2,498	0	0	3,737	142	16,576
Exeter	4,954	1,641	0	0	4,597	-16	16,292
Mid Devon	2,921	1,241	0	0	2,688	0	8,388
North Devon	4,956	1,599	0	0	3,477	0	11,595
South Hams	4,163	224	0	0	3,522	0	9,034
Teignbridge	6,757	1,475	0	0	4,728	224	16,120
Torridge	3,078	938	0	0	2,557	0	8,269
West Devon	3,268	1,162	0	0	2,980	75	8,983
Poole UA	12,034	2,647	0	0	6,744	-439	173,741
Dorset	22,348	4,208	0	0	3,449	0	489,591
East Dorset	3,485	1,232	0	0	2,624	0	9,686
North Dorset	2,569	1,606	0	0	2,381	30	6,946
Purbeck	2,007	977	0	0	1,566	-183	5,557
West Dorset	5,411	1,859	0	0	3,070	0	12,549
Weymouth & Portland	3,987	1,157	0	0	2,717	0	9,823
Forest of Dean	4,109	941	0	0	3,837	0	10,719
Stroud	5,004	1,764	0	0	2,815	1,027	13,939
Tewkesbury	2,360	1,061	0	0	4,374	-108	9,192
Somerset	30,753	3,536	0	0	12,026	5,615	556,553
Mendip	4,729	1,317	0	0	2,676	732	13,501
Sedgemoor	6,096	2,381	0	0	3,530	-561	14,224
Taunton Deane	4,424	1,955	0	0	1,328	0	9,657
South Somerset	7,551	3,005	0	0	2,936	498	18,737
West Somerset	1,983	602	0	0	1,437	0	4,770
Avon Combined Fire and Rescue Authority	0	0	0	41,066	876	0	41,942
Dorset Combined Fire and Rescue Authority	0	0	0	28,778	2,036	0	30,814
Devon and Somerset Combined Fire and Rescue Authority	0	0	0	71,143	600	0	71,743
Dartmoor National Park Authority	103	758	0	0	338	0	3,601
Exmoor National Park Authority	107	507	0	0	283	0	3,020
Dorset Police and Crime Commissioner and Chief Constable	0	0	125,455	0	889	0	126,344
Avon & Somerset Police and Crime Commissioner and Chief Constable	0	0	281,950	0	1,315	0	283,265
Devon & Cornwall Police and Crime Commissioner and Chief Constable	0	0	280,996	0	1,568	0	282,564
	319,224	**61,203**	**688,401**	**162,221**	**174,497**	**7,885**	**4,599,288**

Breaking this down further identified a potential market within the South West Local Authority Area for those services currently provided by the Councils to be approximately £500m per annum.

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

Local authority	Transport planning, policy and strategy	Structural maintenance	Environmental, safety and routine maintenance	Winter service	Street lighting (including energy costs)	Traffic management and road safety: road safety education and safe routes (including school crossing patrols)	Traffic management and road safety: other	Parking services	Airports, harbours and toll facilities	Highways and transport services
North Somerset	1,289	2,175	1,712	356	1,639	9	32	-769	0	9,783
Cornwall	4,519	326	8,552	1,281	2,165	1,169	595	-9,312	2,670	24,028
Plymouth	2,541	1,019	2,616	0	2,204	559	1,608	-518	-357	16,325
Torbay	111	1,793	969	141	1,083	241	0	-3,480	-345	5,235
Devon	1,042	2,603	25,047	3,282	5,465	1,017	389	-528	0	54,833
East Devon	0	0	0	0	0	0	0	-1,988	0	-1,974
Exeter	44	0	118	0	59	0	0	-3,978	0	-3,740
Mid Devon	0	0	0	0	0	0	0	-199	0	-209
North Devon	0	0	0	0	0	0	48	-1,712	100	-1,577
South Hams	0	0	0	0	0	0	0	-1,626	-158	-1,784
Teignbridge	0	0	0	0	0	0	0	-1,952	0	-1,952
Torridge	0	0	0	0	0	0	0	-482	50	-427
West Devon	0	0	0	0	0	0	0	-317	0	-296
Poole UA	469	1,285	1,577	135	1,138	371	0	-2,522	0	6,801
Dorset	1,361	324	7,098	884	6,669	471	1,508	-511	0	26,602
East Dorset	0	0	0	0	0	0	25	-214	0	-108
North Dorset	0	0	0	0	0	0	12	-306	0	-294
Purbeck	0	0	8	0	0	0	0	-129	0	-121
West Dorset	0	0	15	0	0	0	0	-1,503	184	-1,299
Weymouth & Portland	-70	0	63	0	0	0	0	-1,568	579	-996
Forest of Dean	0	0	0	0	0	0	0	-26	0	-26
Stroud	-6	0	0	0	0	0	0	-195	0	-200
Tewkesbury	2	0	0	0	0	0	0	-356	0	-354
Somerset	2,682	1,642	6,130	1,266	4,254	1,502	0	74	0	29,095
Mendip	29	0	0	0	0	0	0	-1,119	0	-1,090

South Hams District Council and West Devon Borough Council

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

Local authority	Transport planning, policy and strategy	Structural maintenance	Environmental, safety and routine maintenance	Winter service	Street lighting (including energy costs)	Traffic management and road safety: road safety education and safe routes (including school crossing patrols)	Traffic management and road safety: other	Parking services	Airports, harbours and toll facilities	Highways and transport services
Sedgemoor	66	0	125	0	0	0	2	-627	0	-425
Taunton Deane	0	0	0	0	0	0	0	-2,588	0	-2,486
South Somerset	39	0	257	0	0	0	0	-1,181	0	-823
West Somerset	0	0	0	0	0	0	0	-267	29	-238
	14,118	**11,167**	**54,287**	**7,345**	**24,676**	**5,339**	**4,219**	**-39,939**	**2,752**	**152,243**

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

Local authority	Housing, advice, advances, enabling, renewals and licensing	Homelessness	Archives	Culture and heritage (excluding Archives)	Recreation and sport	Open spaces	Tourism	Library service	Cemetery, cremation and mortuary services	Regulatory services: Trading standards
North Somerset	1,289	2,175	1,712	356	1,639	9	32	-769	0	9,783
Cornwall	4,519	326	8,552	1,281	2,165	1,169	595	-9,312	2,670	24,028
Plymouth	2,541	1,019	2,616	0	2,204	559	1,608	-518	-357	16,325
Torbay	111	1,793	969	141	1,083	241	0	-3,480	-345	5,235
Devon	1,042	2,603	25,047	3,282	5,465	1,017	389	-528	0	54,833
East Devon	0	0	0	0	0	0	0	-1,988	0	-1,974
Exeter	44	0	118	0	59	0	0	-3,978	0	-3,740
Mid Devon	0	0	0	0	0	0	0	-199	0	-209
North Devon	0	0	0	0	0	0	48	-1,712	100	-1,577
South Hams	0	0	0	0	0	0	0	-1,626	-158	-1,784
Teignbridge	0	0	0	0	0	0	0	-1,952	0	-1,952
Torridge	0	0	0	0	0	0	0	-482	50	-427
West Devon	0	0	0	0	0	0	0	-317	0	-296
Poole UA	469	1,285	1,577	135	1,138	371	0	-2,522	0	6,801
Dorset	1,361	324	7,098	884	6,669	471	1,508	-511	0	26,602
East Dorset	0	0	0	0	0	0	25	-214	0	-108
North Dorset	0	0	0	0	0	0	12	-306	0	-294
Purbeck	0	0	8	0	0	0	0	-129	0	-121
West Dorset	0	0	15	0	0	0	0	-1,503	184	-1,299
Weymouth & Portland	-70	0	63	0	0	0	0	-1,568	579	-996
Forest of Dean	0	0	0	0	0	0	0	-26	0	-26
Stroud	-6	0	0	0	0	0	0	-195	0	-200
Tewkesbury	2	0	0	0	0	0	0	-356	0	-354
Somerset	2,682	1,642	6,130	1,266	4,254	1,502	0	74	0	29,095
Mendip	29	0	0	0	0	0	0	-1,119	0	-1,090
Sedgemoor	528	666	0	29	939	807	0	0	56	0
Taunton Deane	855	372	0	167	875	1,205	114	0	-517	0
South Somerset	249	1,053	0	517	1,098	1,193	170	0	-105	0

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

Local authority	Housing, advice, advances, enabling, renewals and licensing	Homelessness	Archives	Culture and heritage (excluding Archives)	Recreation and sport	Open spaces	Tourism	Library service	Cemetery, cremation and mortuary services	Regulatory services: Trading standards
West Somerset	323	111	0	0	0	271	53	0	48	0
Dartmoor National Park Authority	0	0	0	219	0	1,891	295	0	0	0
Exmoor National Park Authority	0	0	0	305	0	1,493	362	0	0	0
	15,042	**16,008**	**2,525**	**15,222**	**24,730**	**35,085**	**4,712**	**32,821**	**-3,662**	**6,796**

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

Local authority	Regulatory services: Food safety	Regulatory services: Environmental protection; noise and nuisance	Regulatory services: Housing standards	Regulatory services: Health and safety	Regulatory services: Pest control	Regulatory services: Public conveniences	Regulatory services: Animal and public health; infectious disease	Regulatory services: Licensing - Alcohol and entertainment licensing; taxi licensing	Community safety (Crime reduction)	Community safety (Safety services)
North Somerset	451	479	0	0	-11	128	194	-98	303	0
Cornwall	1,867	2,639	1,460	53	0	1,395	198	394	1,540	0
Plymouth	480	433	18	315	31	227	463	-191	1,060	306
Torbay	489	480	356	10	22	901	111	114	354	161
Devon	335	0	0	0	0	0	527	0	0	0
East Devon	240	378	282	197	14	619	69	-11	50	171
Exeter	-7	150	208	120	0	392	82	239	0	-29
Mid Devon	83	120	0	0	16	79	128	15	71	0
North Devon	275	229	72	60	11	434	142	30	243	7
South Hams	248	147	112	155	15	587	116	-42	0	113
Teignbridge	349	484	77	44	14	591	84	-27	83	41
Torridge	175	244	82	56	19	219	93	38	60	118
West Devon	91	0	0	0	14	188	594	94	44	0
Poole UA	313	559	0	187	44	313	124	50	0	590
Dorset	0	0	0	0	0	0	0	0	0	1
East Dorset	196	222	0	218	64	157	206	106	38	0
North Dorset	0	0	0	0	8	0	476	35	0	80
Purbeck	122	118	0	31	6	91	121	31	32	35
West Dorset	352	270	335	80	74	514	119	36	0	0
Weymouth & Portland	302	230	148	0	0	375	100	-64	0	102
Forest of Dean	99	148	0	0	85	158	0	103	439	0
Stroud	206	289	0	124	118	220	208	-36	147	341
Tewkesbury	136	104	19	133	14	0	73	-4	0	79
Somerset	3	406	0	0	0	0	559	-128	591	99
Mendip	-1	-7	135	358	6	90	38	268	0	63
Sedgemoor	169	111	2	87	26	124	209	71	114	18
Taunton Deane	328	212	0	9	30	297	120	-24	0	0

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

Local authority	Regulatory services: Food safety	Regulatory services: Environmental protection; noise and nuisance	Regulatory services: Housing standards	Regulatory services: Health and safety	Regulatory services: Pest control	Regulatory services: Public conveniences	Regulatory services: Animal and public health; infectious disease	Regulatory services: Licensing - Alcohol and entertainment licensing; taxi licensing	Community safety (Crime reduction)	Community safety (Safety services)
South Somerset	384	93	216	330	102	171	159	36	0	60
West Somerset	57	0	0	8	0	138	20	-17	0	0
Dartmoor National Park Authority	0	0	0	0	0	103	0	0	0	0
Exmoor National Park Authority	0	0	0	0	0	107	0	0	0	0
	7,742	**8,538**	**3,522**	**2,575**	**722**	**8,618**	**5,333**	**1,018**	**5,169**	**2,356**

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

Local authority	Community safety (CCTV)	Defences against flooding	Land drainage and related work (excluding levy / Special levies)	Land drainage and related work - Levy / Special levies	Coast protection	Agriculture and fisheries services	Street cleansing (not chargeable to Highways)	Waste collection	Waste disposal	Trade waste
North Somerset	452	368	168	503	0	53	1,437	6,499	8,995	0
Cornwall	125	0	104	0	714	-933	5,769	8,371	37,751	-7
Plymouth	168	64	0	0	0	39	3,719	741	15,626	-363
Torbay	152	71	0	0	165	-598	2,030	3,538	4,860	0
Devon	0	1,158	0	0	28	-284	0	0	24,482	20
East Devon	29	163	0	0	103	31	1,289	1,991	2	0
Exeter	565	0	125	0	0	0	1,483	1,604	0	-236
Mid Devon	17	0	82	0	0	0	386	1,391	0	-103
North Devon	181	16	0	0	7	-25	667	1,954	0	37
South Hams	0	49	0	0	27	0	819	1,647	0	-81
Teignbridge	2	220	6	0	116	0	1,252	1,225	0	0
Torridge	154	1	3	0	2	0	580	694	0	0
West Devon	0	99	0	0	0	0	509	1,635	0	0
Poole UA	307	0	231	0	116	48	1,838	2,217	7,533	-32
Dorset	0	0	0	0	0	0	0	0	12,551	0
East Dorset	0	0	44	0	0	0	27	2,207	0	0
North Dorset	0	14	0	0	0	0	37	1,908	0	0
Purbeck	0	26	0	0	18	0	372	554	0	0
West Dorset	146	0	255	0	279	0	5	2,943	0	0
Weymouth & Portland	174	0	22	0	297	0	1,146	1,746	0	0
Forest of Dean	0	55	0	0	0	0	544	1,575	0	0
Stroud	43	0	74	103	0	0	706	1,647	5	0
Tewkesbury	0	0	116	5	0	0	478	894	0	16
Somerset	0	684	0	0	3	-136	0	0	21,601	0
Mendip	136	1	1	113	0	0	702	3,170	0	0
Sedgemoor	168	126	2	1,234	7	0	653	2,910	0	0
Taunton Deane	252	128	0	20	0	0	733	1,550	0	0

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

South Somerset	51	138	55	0	0	0	1,294	2,487	132	0
West Somerset	46	23	0	0	25	0	479	1,161	0	0
	3,168	**3,404**	**1,288**	**1,978**	**1,907**	**-1,805**	**28,954**	**58,259**	**133,538**	**-749**

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

Local authority	Recycling	Waste minimisation	Climate change costs	Building control	Development control	Planning policy	Environmental initiatives	Economic development	Community development	Economic research	Business Support	Emergency planning	Central services to the public: other
North Somerset	0	115	0	-42	403	728	0	103	0	0	-555	68	712
Cornwall	4,244	0	0	-70	2,098	1,920	-1,693	2,922	1,748	0	-1,278	398	1,404
Plymouth	1,792	0	0	5	482	798	368	-1,712	1,813	16	0	200	914
Torbay	119	12	0	65	278	879	39	1,920	537	0	356	136	855
Devon	8,945	294	272	0	1,090	421	2,448	621	1,550	129	525	184	1,268
East Devon	1,795	0	0	155	1,079	564	0	-3	416	0	287	54	680
Exeter	94	0	0	42	723	56	0	684	136	0	0	17	540
Mid Devon	433	0	0	80	422	334	6	68	331	0	0	0	313
North Devon	624	0	0	-1	605	184	6	454	100	0	251	47	369
South Hams	197	0	0	52	366	206	27	-590	133	2	28	28	215
Teignbridge	1,645	348	49	0	734	701	0	-133	143	0	30	38	808
Torridge	552	0	0	90	236	418	72	67	55	0	0	27	404
West Devon	0	0	0	32	595	198	0	0	125	0	212	2	224
Poole UA	-1,817	0	0	98	953	491	90	59	502	454	0	153	589
Dorset	8,474	0	0	0	428	1,026	1,708	375	711	0	-39	191	130
East Dorset	0	0	0	108	658	251	7	198	10	0	0	41	239
North Dorset	0	0	0	72	560	548	29	180	217	0	0	48	342
Purbeck	442	0	0	52	419	421	22	41	22	0	0	39	276
West Dorset	0	0	0	189	598	567	0	161	344	0	0	144	107
Weymouth & Portland	0	0	0	121	393	335	0	134	174	0	0	85	-418
Forest of Dean	877	0	0	-15	466	173	23	122	172	0	0	107	293
Stroud	657	28	0	88	590	349	217	432	88	0	0	85	694
Tewkesbury	250	0	0	29	205	401	37	54	309	0	26	33	509
Somerset	6,476	0	0	0	398	709	1	907	968	207	346	260	636
Mendip	-381	0	28	108	101	318	608	0	-139	0	322	25	269
Sedgemoor	0	0	0	67	703	364	48	731	440	28	0	50	395

Revenue Account Budget (RA): 2015-16 data

Net current expenditure (£ thousand)

Taunton Deane	1,284	0	2	74	75	620	0	1,070	116	0	0	96	484
South Somerset	1,948	0	0	116	452	682	39	858	767	107	-16	170	202
West Somerset	0	0	0	114	13	257	0	124	42	0	53	0	195
Avon Combined Fire and Rescue Authority	0	0	0	0	0	0	0	0	0	0	0	66	0
Dartmoor National Park Authority	0	0	0	0	515	243	0	0	0	0	0	0	0
Exmoor National Park Authority	0	0	0	0	238	0	200	69	0	0	0	0	0
	38,650	**797**	**351**	**1,629**	**16,876**	**15,162**	**4,302**	**9,916**	**11,830**	**943**	**548**	**2,792**	**15,160**

4.2. Potential Contracts

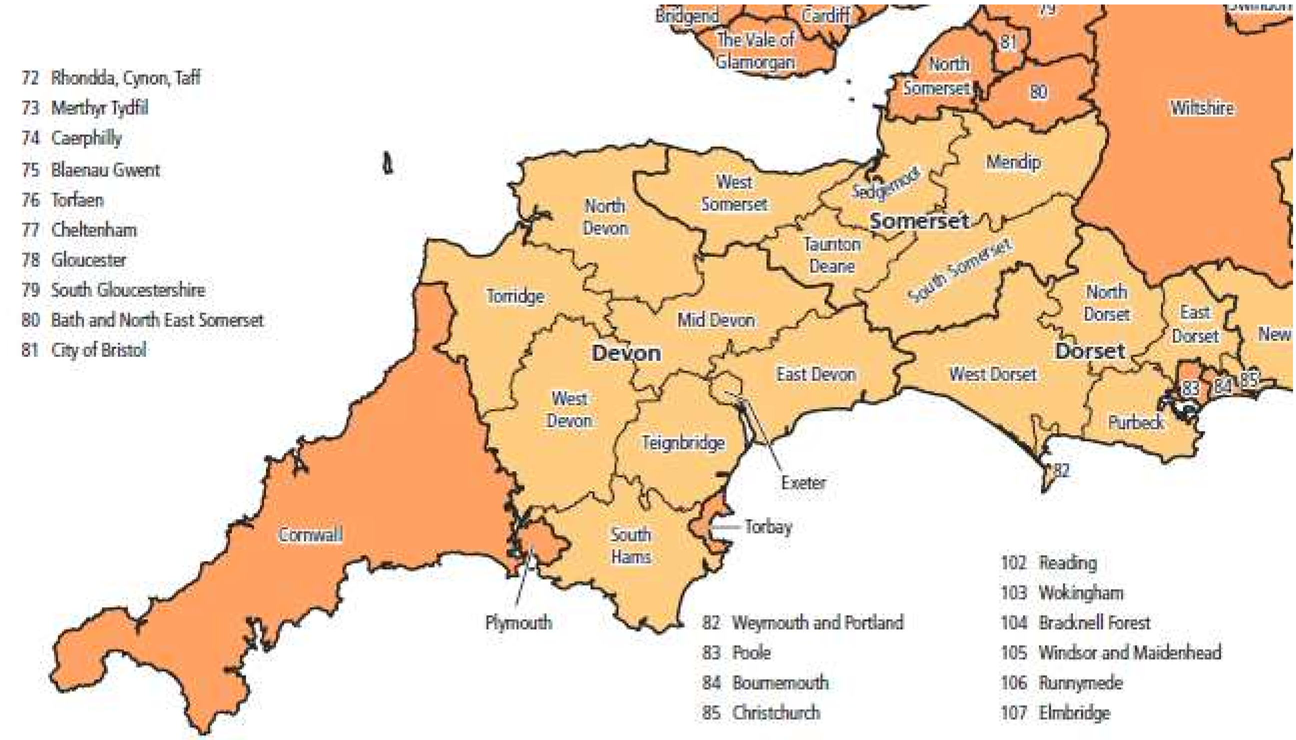
We have identified in excess of 70 potential contracts coming to market in the next 4 years in the South West. These are of varying value and term and we have included a selection of these contracts below:

Contract	Contract Value (£)	Contract End Date
Grounds & Facilities- Services in South West (Plymouth & Exeter)	£80k pa	2019
Environmental Health Services - Plymouth University	£180k pa	2018
Stock Management Tool for Somerset County Council	£133k pa	2019
Project Management Support- Development of Single IT Service for Tri-Council Partnership	£70k	2016
Cornwall Transformation Challenge Award (TCA) Service Design and Support	£25kpa	2017
Building Cleaning- South Devon College	£800k pa	2018
Cornwall Housing Maintenance Framework (Lot 1: Planned Mechanical and Electrical Maintenance)	£2.5m pa	2017
Cornwall Housing Maintenance Framework (Lot 2: Planned Ground Work Maintenance)	£2.5m pa	2017
Cornwall Housing Maintenance Framework (Lot 5: Planned General Building Maintenance (Under £150k East))	£2.5m pa	2017
Cornwall Housing Maintenance Framework (Lot 6: Planned General Building Maintenance (Under £150k West))	£2.5m pa	2017
Cornwall Housing Maintenance Framework (Lot 7: Planned General Building Maintenance (£150k to £500k))	£2.5m pa	2017
Waste and recycling collections and beach and street cleaning services - Cornwall Council	£15.6m pa	2020
Refuse and Recycling Products (including wheeled bins) - ESPO Framework 860 Iss 11 - Cornwall Council	£500k pa	2018
Schools Maintenance, Access and Minor Works Programme 2015 - Cornwall Council	-	2017
Framework Agreement for the Manufacture, Delivery and Assembly on site of Beach Huts, on behalf of Cornwall Council and other nominated organisations - Cornwall Council	£500k pa	2019
Academy Support - Cornwall Council	£99k pa	2017
Payment Collection Services - Cornwall Council - Cornwall Council	£125k pa	2020
Collection and processing of domestic refuse and recycling - Tandrige District Council	£2.4m pa	2019
CP1123-15 Committee Management System - Devon County Council	-	2018
CP1172-15 The Devon Maintenance Panel Agreement - Devon County Council	-	2020
Dorset Public Sector Network (DPSN) FRAMEWORK - Dorset County Council	£20m pa	2018
Growth Hub Service for the Heart of the South West LEP - North Somerset Council	£500k pa	2019
Vehicle Parts Managed Service Contract - Dorset County Council	£1m pa	2019
Waste Treatment and Disposal Contract - Dorset County Council	£1.3m pa	2020

4.3. Responding to the Market

Regional considerations

In considering the market we next considered the regional opportunities for other Local Authorities. We understand that previous discussions between the Councils and Torridge District Councils identified that they did not wish to participate in establishing a LACC at this time. We also understand that an existing relationship exists with Teignbridge District Council who provide specialised procurement services to the Councils on a part time basis.



(Extract: http://www.cpag.org.uk/sites/default/files/ONS%20Map%20UK%20local%20authorities%202009.pdf)

The proximity of Cornwall, Plymouth and others in Devon including Torridge, Mid Devon, Teignbridge, Exeter and North Devon present opportunities for provision of services to other local authorities. These also present opportunities to either enter partnerships or joint ventures with to leverage local operations. In the short term it is likely that operations will be focused locally but longer term opportunities may be presented further afield in Somerset or other areas to the north. For example Norse Group who have established joint operations nationally.

The table below summarises the key features across the southwest:

Council	Summary
Cornwall Council	Has a demonstrated history of outsourcing including major contracts with BT for IT and back office support services, as well as establishing arm's length trading organisations for the airport, housing, leisure, social care and environmental services. Established Cormac as a LACC for provision of highway and maintenance services.
Torbay Council	Has a demonstrated history of outsourcing a range of functions including waste, grounds maintenance and cleansing services. Also uses Virgin Care for children's health and social care.
Dorset Council	Traditionally hasn't outsourced a lot of functions.
Devon County Council	Involved in the Building Control Partnership as well as with Virgin Care for children's health and social care.
Plymouth City Council	Have outsourced IT and social care, as well as with Virgin Care for children's health and social care.

Somerset County Council	Have outsourced IT functions and established Southwest ONE with IBM and Avon to provide shared services including, Customer Contact Centre, Corporate Services, Design & Print, Enquiry Office, Finance Services, Human Resources, Property Services, Strategic Procurement Service and Technology Services.
Hampshire County Council	Have an integrated business centre with shared services arrangements for back office and support functions.
Gloucestershire City Council	Have outsourced IT functions as well as adult social care.
Bath and North Easter Somerset Council	Primarily outsourced health and social care with the remainder of services in-house.
Bristol City Council	Traditionally haven't outsourced a lot of administrative functions. Recently established a power supply company and outsource waste collection.

The majority of Local Authorities appear to outsource waste services.

Other Public Sector Entities

In addition to Local Authorities, we considered potential for other public sector entities and their requirements for services that the LACC could potentially provide.

There are a number of health facilities in the region. With an ageing population forecast to increase in the future provision of health services has the potential to expand in the South West region. There is also a large number of privately owned and operated hospitals and health facilities across Cornwall and Devon. Nuffield Health and Ramsay are two major providers active in the region. Consideration would need to be given to the service offering available to these entities following an establishment and proving period with public facilities. There may also be opportunity to leverage waste and cleaning services in expanding into clinical waste treatment, as an example.

The Government is also pursuing a drive to increase autonomy in the education sector through increasing the number of academy schools. There are a large number of schools across the region and Schoolsnet outlines that across Cornwall and Devon there are approximately 730 preparatory, primary and secondary schools.

In addition to health and education other government bodies including:

- Communities and local government;
- Business, innovation and skills;
- Environment, food and rural affairs;
- Food standards agency;
- National parks;
- National trust, heritage or charitable organisations.

These organisations have varying degrees of operation within the region and could present opportunity to provide a range of services.

Private Sector

In considering the external opportunities in the region, it was identified that these are likely to be limited in the near term. There could be medium term opportunities but market penetration will be dependent on skills development with regard to pricing and tendering. This will be significant in the Councils' ability to generate additional revenues.

A desktop review identified that there are existing suppliers of a range of the services to be provided by the LACC. The Councils would need to consider their unique selling proposition when engaging with the private sector to enhance their brand to improve their ability to compete established private sector suppliers.

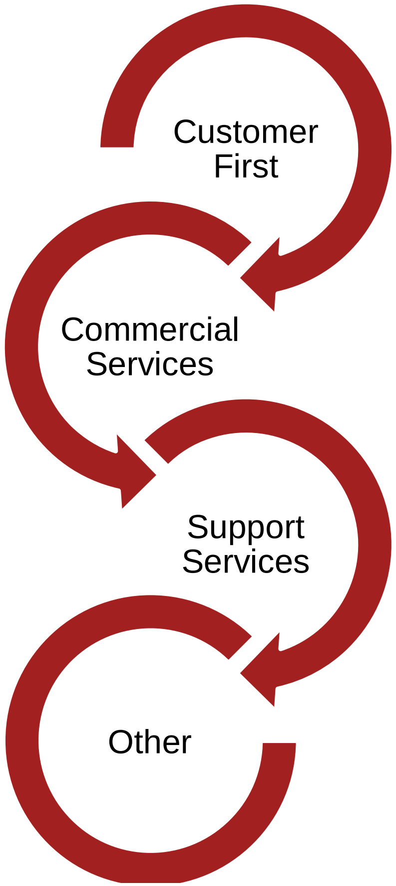
In the short term the Councils should focus on functions and areas that are more familiar, for example, other local authorities and/or other public sector entities within the Councils' geographic area.

4.4. Business Needs and Service Requirements

The T18 Programme involved the redesign of all services. The figure below summarises the scale of the service provision within the partnership across:

- Customer First
- Commercial Services
- Support Services
- Other functions

The Councils advised significant work has been undertaken on establishing the current operating model and consideration should not be given to any further amendments or restructure of the model as part of this engagement.



Services			Staff	Locations	Other
Field based customer contact teams Customer contact centre/reception Planning Licencing and Enforcement Strategic Planning / Development management Building Inspections Food Inspections/Hygiene Coastal Management Taxi's	Housing Advice Revenue & Benefits Environmental Health Assets and Civil Engineering Economic Development Building Control Asylum Seekers Crime and Antisocial behaviour Emergency Management Street collections and trading	Markets, events and exhibitions Flood Management Funerals Gambling Grants Traveller sites Health and Safety Homelessness Licensing, permits and policies Pests, noise and pollution	155 FTE's	Kilworthy Follaton Okehampton	Council Owned assets and locations Services jointly provided between Councils Building Control provided in in partnership with Teignbridge District Council, which is currently hosted in Teignbridge District Council.
West Devon Waste Contract Management Waste Management Services (South Hams, including trade waste) Transport Grounds Maintenance Winter Services Waste Education Recycling and education	Estates Maintenance Street Cleansing Car Parks and Park & Ride Litter cleaning and education Salcombe Harbour Management Dartmouth Lower Ferry Management Roadside removal (i.e. deceased animals) Facilities management		170 FTE's	Waste & cleansing: SH has 2 main depots plus a headquarters, WD has 2 depot sites Transport: SH only depot Estates: Totnes depot Maintenance: SH only Salcombe Dartmouth	Primarily Council owned assets and locations Material recycling plant at WD on a long term lease WD contact for Waste services is with FCC Environment and expires March 2017
Finance Audit Accounts Payable Management Accounting Financial Analysis Treasury Management Legal Procurement Human Resources	Support Services Desk ICT Design Employment services Insurances Technology Project Management		66 FTE's	Primarily Follaton House, South Hams	Procurement services contracted from Teignbridge Council at 2 days per week Audit services in partnership with Devon Audit Partnership who provide the professional management of the team
West Devon Waste Leisure Centre Strategy and Commissioning					Leisure Centre contract in procurement and likely to be for 20-25 years.

4.5. Options Assessment

The Councils have already undertaken significant work in considering options available for service delivery through internal and external channels. Our approach in assessing options included:

- Identifying the objectives in conjunction with the Councils;
- Reviewing the previous work undertaken provided by the Councils, including:
  - Operating company options;
  - Options for West Devon Waste and cleansing services.
- Undertaking a high level options assessment;
- Identifying and agreeing the assessment criteria with the Councils, including weightings;
- Assessing the options against a broad base of criteria;
- Identifying shortlisted options to be considered further for quantitative impacts.

Another consideration in assessing the options was a comparative risk assessment.

A Multi-Criteria Assessment (MCA) was utilised to qualitatively assess the options. The options assessment included scoring and ranking the options on both a weighted and unweighted basis to determine the relative impacts of each option.

With regard to the options assessment:

- The options did not include assessing opportunities to increase revenues through current sources (i.e. taxes, rates, grants etc) or identification of reduced services. These were outside the scope of our engagement;
- The Local Government Act (2003) grants councils the power to trade in function related activities but this must be as a company and not as a Limited Partnership or a Limited Liability Partnership.

The key considerations that underpinned the options assessment covered 6 broad categories including:

1. Strategic Fit: How best does the option fit with the strategic intent, drivers and goals of the Councils;
2. Social Benefits and Impacts: What benefits are provided to society by the option;
3. Governance: Is appropriate governance able to be implemented;
4. Commercial: Is the option able to be structured appropriately to clearly articulate roles, responsibilities and also to provide flexibility in being able to respond to change;
5. Financial: What are the likely tax implications and opportunities to generate additional revenues;
6. Implementation and Delivery: What are the transition impacts and opportunities for example, Teckal procurement exemptions.

The MCA of the options identified that the combined model, Option 6 scored the highest on both unweighted score and weighted score.

Option 5 scored equal second with Option 1 on unweighted scores but higher on weighted. As there are a number of similarities between Option 5 and 6 it was agreed that Option 6 would be further assessed against 'As Is' model, Option 1 for commercial and financial implications. These are covered in subsequent chapters.

The table below summarises the outcomes of the qualitative options assessment including unweighted and weighted scoring.

	1	6
Ranking	Base Case- 'As Is' with Customer First, Commercial Services, Support Service, contracted services for Waste in West Devon, Leisure	A Combined model (a combination of insource for Strategy and Commissioning, outsource for leisure, and LACC for Customer First, Commercial Services, Support Services)
Unweighted Score	52	59
Unweighted Rank	2	1
Weighted Score	58.125	76.250
Weighted Rank	4	1
Assessment Summary	This option scored well on the raw unweighted score but a lot lower when weighed. This demonstrates that there were key criteria that this option did not support, in particular the ability to generate additional revenue to offset the projected funding gap.	This option scored highest on both weighted and unweighted. This demonstrates that it was clearly the preferred option to be further considered in this Business Case.

Multi Criteria Analysis (MCA) **South Hams and West Devon Options Appraisal**

Options

						1		2		3		4		5		6		
	Note: where items are not applicable to an option, that option has been scored the maximum score of 4					**Base Case- 'As Is' with Customer First, Commercial Services, Support Service, contracted services for Waste in West Devon, Leisure**		**Council provide (In-house) all services including waste across the Councils (potential exceptions where skills not available)**		**Contract or outsource all services including administrative functions (either holistically or separately)**		**Establish a Joint Trading Arm between the Councils for commercial services within current Authority structure/ agreements**		**Establish a LACC as a Company limited by Shares for CF, CS and SS, also including members services, communications, strategy and commissioning**		**A Combined model (a combination of insource for member services, outsource leisure, and LACC for Customer First, Commercial Services, Support Services)**		**Comments**
	Strategic Category	**Category Weighting**	**Sub Criteria No.**	**Measure**	**Sub-criteria Weighting**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	
Strategic Alignment Criteria		5.0%	1.1	Improves Councils identity and culture and has the ability to meet policy requirements	2.5%	3	1.88	2	1.25	1	0.63	2	1.25	2	1.25	3	1.88	Options 1 and 6 scored the highest as it was deemed they utilise skills and enabled them to retain identity, culture and local presence and meet policy requirements. Option 3 scored the lowest as it was be seen as outsourcing Councils services.
			1.2	Does it support the Councils vision and objectives	2.5%	3	1.88	1	0.63	1	0.63	2	1.25	2	1.25	3	1.88	Options 1 and 6 scored the highest as they reflect the Councils vision of service provision and commercial focus. Options 2 and 3 do not support Councils vision as the extremes.
	Social benefits and impacts	10.0%	2.1	Impact on community and employees	2.5%	3	1.88	3	1.88	2	1.25	3	1.88	2	1.25	2	1.25	Options 1, 2 and 4 scored the same as would have equal impact on employees. Option 2 also considers impacts of bringing outsourced services in-house. Option 5 and 6 scored lowest as they would potentially have the greatest impact.
			2.2	Community perception	2.5%	4	2.50	4	2.50	1	0.63	2	1.25	2	1.25	3	1.88	Option 1 and 2 scored highest as deemed meeting community expectations of local Councils. Option 3 scored slightly less as it presents a better mix to meet community perceptions.
			2.3	Impacts on service quality	5.0%	1	1.25	1	1.25	2	2.50	2	2.50	3	3.75	3	3.75	Options 5 and 6 scored highest as they could have the greatest impact on maintaining services. Options 1 and 2 scored lowest as it was deemed to present the least opportunity to improve community outcomes. This also considers bringing currently outsourced services.
	Governance	10.0%	3.1	Ability to implement appropriate governance	10.0%	3	7.50	3	7.50	2	5.00	3	7.50	2	5.00	3	7.50	Options 1, 2, 4 and 6 scored highest as they utilise existing governance arrangements. Options 3 and 5 scored slightly lower as they require new arrangements, all of which were deemed manageable.
	Commercial	25.0%	4.1	Ability to operate commercially	10.0%	2	5.00	1	2.50	2	5.00	3	7.50	3	7.50	3	7.50	Options 4, 5 and 6 scored highest as they are deemed to be commercial operations. Option 1 scored lowest as in-house services deemed hardest to operate commercially.

Multi Criteria Analysis (MCA) **South Hams and West Devon Options Appraisal**

Options

Note: where items are not applicable to an option, that option has been scored the maximum score of 4

Strategic Category	Category Weighting	Sub Criteria No.	Measure	Sub-criteria Weighting	1. Base Case- 'As Is' with Customer First, Commercial Services, Support Service, contracted services for Waste in West Devon, Leisure: Rating	1: Weighted Score	2. Council provide (In-house) all services including waste across the Councils (potential exceptions where skills not available): Rating	2: Weighted Score	3. Contract or outsource all services including administrative functions (either holistically or separately): Rating	3: Weighted Score	4. Establish a Joint Trading Arm between the Councils for commercial services within current Authority structure/ agreements: Rating	4: Weighted Score	5. Establish a LACC as a Company limited by Shares for CF, CS and SS, also including members services, communications, strategy and commissioning: Rating	5: Weighted Score	6. A Combined model (a combination of insource for member services, outsource leisure, and LACC for Customer First, Commercial Services, Support Services): Rating	6: Weighted Score	Comments
		4.2	Ability to respond to changes (i.e. political/budget)	2.5%	4	2.50	4	2.50	1	0.63	3	1.88	2	1.25	3	1.88	Options 1 and 2 scored highest as with greater control changes would be able to be made easier. Options 4 and 6 were next and provided a different mix of structures to flex control. Option 5 was seen as being a more rigid structure, even though Councils retain ownership, their ability to respond is constrained. Option 3 has the least control with a range of external contracts.
		4.3	Flexibility to expand and take on new partners	5.0%	1	1.25	0	0.00	1	1.25	3	3.75	4	5.00	3	3.75	Option 2 scored lowest as it doesn't present a lot of opportunity to expand or take on new work or partners (i.e. .other agencies or private sector). Option 5 scored the highest as it presented clear avenues for additional work or partners. Options 4 and 6 present opportunity to engagement with external partners but not to the extent of Option 5. Option 1 and 3 generates third party engagement through various contracts or partnerships.
		4.4	Council skills & experience- Contract Management and tendering	7.5%	2	3.75	3	5.63	1	1.88	3	5.63	2	3.75	3	5.63	Options 2, 4 and 6 scored the same as Councils retain a greater influence on policy development and delivery. Option 3 scored the lowest as it would be harder to delivery policy across contracted services. Options 1 and 5 may require additional skills not currently catered for within the Council.
Financial	25.0%	5.1	Ability to generate revenues	10.0%	1	2.50	1	2.50	1	2.50	2	5.00	4	10.00	3	7.50	Option 5 scored highest as it presents the best structure for generating revenues. Option 6 presented opportunity to generate external revenues. Options 1, 2 and 3 don't present major opportunity to generate additional revenues over current levels, therefore scored the lowest.
		5.2	Tax impacts including Corporation Tax, VAT, SDLT	5.0%	4	5.00	4	5.00	4	5.00	3	3.75	2	2.50	3	3.75	Options 1, 2 and 3 scored highest as under these there would be no changes or need for Tax. Options 3 and 6 scored next best although they were deemed to attract Tax liability. Option 5 scored lowest as it would potentially have a greater tax impact.

Multi Criteria Analysis (MCA) **South Hams and West Devon Options Appraisal**

Options

Note: where items are not applicable to an option, that option has been scored the maximum score of 4

					1		2		3		4		5		6		
					Base Case- 'As Is' with Customer First, Commercial Services, Support Service, contracted services for Waste in West Devon, Leisure		Council provide (In-house) all services including waste across the Councils (potential exceptions where skills not available)		Contract or outsource all services including administrative functions (either holistically or separately)		Establish a Joint Trading Arm between the Councils for commercial services within current Authority structure/ agreements		Establish a LACC as a Company limited by Shares for CF, CS and SS, also including members services, communications, strategy and commissioning		A Combined model (a combination of insource for member services, outsource leisure, and LACC for Customer First, Commercial Services, Support Services)		Comments
Strategic Category	**Category Weighting**	**Sub Criteria No.**	**Measure**	**Sub-criteria Weighting**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	
		5.3	Flexibility of staff terms and conditions	5.0%	4	5.00	4	5.00	4	5.00	3	3.75	3	3.75	3	3.75	Options 1, 2 and 3 scored highest as there would be minimal changes for Employee Taxes or pension liabilities. Options 4, 5 and 6 scored lowest as they were deemed to incur Employee Tax changes or pension liabilities.
		5.4	State Aid impacts	2.5%	4	2.50	4	2.50	4	2.50	3	1.88	2	1.25	3	1.88	Options 1, 2 and 3 scored highest as they were deemed to not present any State Aid implications over the current model. Options 4 and 6 were next as they presented different structures into the mix. Option 5 scored lowest as different legal structure could potentially create some State Aid risks. For options 4, 5 and 6 structures were deemed to be manageable.
		5.5	Ability to raise external funding (i.e. borrowings)	2.5%	0	0.00	0	0.00	0	0.00	0	0.00	3	1.88	2	1.25	Options 1, 2, 3 and 4 scored lowest as they do not present any opportunity to raise external funding. Options 4 and 5 scores reflect that they could potentially borrow once operations established and credit worthiness established.
Implementation and Delivery	25.0%	6.1	Transition Impacts, including staffing and service delivery - Teckal exemptions (procurement)	10.0%	1	2.50	2	5.00	2	5.00	2	5.00	4	10.00	4	10.00	Options 2, 3 and 4 scored the same as they create transitional risks. Risks were deemed manageable. This considers transition of outsourced items back in-house. Options 5 and 6 scored highest as they also take advantage of Teckal exemptions for procurement and revenue generation. Option 1 scored lowest as it doesn't take advantage of Teckal exemptions.
		6.2	Ability to manage Interfaces / Interdependencies, both now and ongoing	2.5%	2	1.25	2	1.25	1	0.63	3	1.88	2	1.25	3	1.88	Options 4 and 6 scored highest as they present opportunity to manage interfaces and interdependencies across the businesses. Options 1, 2 and 5 were next best as they present different risk profiles which may not be able to be managed as well as the other options. Option 3 scored lowest as it would involve a range of outsourced contracts creating risks for interfaces and interdependencies.

Multi Criteria Analysis (MCA) **South Hams and West Devon Options Appraisal**

					Options												
					1		**2**		**3**		**4**		**5**		**6**		
Note: where items are not applicable to an option, that option has been scored the maximum score of 4					**Base Case- 'As Is' with Customer First, Commercial Services, Support Service, contracted services for Waste in West Devon, Leisure**		**Council provide (In-house) all services including waste across the Councils (potential exceptions where skills not available)**		**Contract or outsource all services including administrative functions (either holistically or separately)**		**Establish a Joint Trading Arm between the Councils for commercial services within current Authority structure/ agreements**		**Establish a LACC as a Company limited by Shares for CF, CS and SS, also including members services, communications, strategy and commissioning**		**A Combined model (a combination of insource for member services, outsource leisure, and LACC for Customer First, Commercial Services, Support Services)**		**Comments**
Strategic Category	**Category Weighting**	**Sub Criteria No.**	**Measure**	**Sub-criteria Weighting**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	
		6.3	Operating Risks, including asset management	5.0%	2	2.50	2	2.50	1	1.25	2	2.50	3	3.75	3	3.75	Options 5 and 6 scored highest as structures that transfer operational risks. Option 3 presents complexities across a number of contracts and scored lowest. Options 1, 2 and 4 scored in the middle with comparative operating risk profiles.
		6.4	Exit Strategy / Requirements (i.e. TUPE)	2.5%	4	2.50	4	2.50	2	1.25	3	1.88	3	1.88	3	1.88	Options 1 and 2 scored highest as the exit strategies are manageable and understood. Although potential outsourcing or partnering could be deemed exit strategies in this context. Option 3 scored lowest as it presented the greatest risk of exit strategy if contracts are not performing or managed appropriately. Options 4, 5 and 6 scored in the middle as each requires an element of exit strategy consideration.
		6.5	Deliverability and ease of implementation	5.0%	4	5.00	1	1.25	1	1.25	3	3.75	2	2.50	3	3.75	Option 1 scored highest as they best reflect as it is the current delivery model. Options 4 and 6 present slightly higher risk of deliverability. Options 2 and 3 reflect the ability to manage bringing services in-house or contracting out respectively. Option 5 presents potential issues with contract and scope of services delivered.
	100.0%		**Total Weighting**	**100.0%**	**52**	**58.125**	**46**	**53.13**	**34**	**43.75**	**50**	**63.75**	**52**	**70.00**	**59**	**76.25**	
			Total Available Score		**80**		**80**		**80**		**80**		**80**		**80**		
			MCA Unweighted Score		52		46		34		50		52		59		
			MCA Weighted Score			58.125		53.125		43.75		63.75		70		76.25	
			MCA Unweighted Score		2		5		6		3		2		***1***		
			MCA Weighted Score			4		5		6		3		2		***1***	

Options:

Number	Overview	Definition	Overall Comment

Multi Criteria Analysis (MCA) **South Hams and West Devon Options Appraisal**

Options

Note: where items are not applicable to an option, that option has been scored the maximum score of 4					1		2		3		4		5		6		
					Base Case- 'As Is' with Customer First, Commercial Services, Support Service, contracted services for Waste in West Devon, Leisure		Council provide (In-house) all services including waste across the Councils (potential exceptions where skills not available)		Contract or outsource all services including administrative functions (either holistically or separately)		Establish a Joint Trading Arm between the Councils for commercial services within current Authority structure/ agreements		Establish a LACC as a Company limited by Shares for CF, CS and SS, also including members services, communications, strategy and commissioning		A Combined model (a combination of insource for member services, outsource leisure, and LACC for Customer First, Commercial Services, Support Services)		Comments
Strategic Category	**Category Weighting**	**Sub Criteria No.**	**Measure**	**Sub-criteria Weighting**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	**Rating**	**Weighted Score**	

Option	Description	Services	Comments
1	Base Case- 'As Is' with Customer First, Commercial Services, Support Service, contracted services for Waste in West Devon, Leisure	In-house- Customer First, Commercial Services, Support Services. Contracted- Leisure centre management contracted, West Devon Waste contracted	This option scored well on the raw unweighted score but a lot lower when weighed. This demonstrates that there were key criteria that this option did not support, in particular the ability to generate additional revenue to offset the projected funding gap.
2	Council provide (in-house) all services including waste across the Councils (potential exceptions where skills not available)	In-house- Customer First, Commercial Services, Support Services, including transition of WDW back in-house. Contracted- Leisure centre management contracted	This option scored relatively low on both counts as it does not support Councils objectives nor was it anticipated to improve services outcomes. This option did not demonstrate that it would provide greater value for money.
3	Contract or outsource all services including administrative functions (either holistically or separately)	Contracted/outsourced- Customer First, Commercial Services, Support Services (including Leisure Centre management), Harbours, Member Services, Communications in-house- Contract management	This option scored lowest on both weighted and unweighted scores. Contracting out would create greater complexity and result in less control over service provision.
4	Establish a Joint Trading Arm between the Councils for commercial services within current Authority structure/ agreements	in-house- Contract Management, Harbours, Customer First, Support Services Contracted- Leisure centre management contracted Trading Arm- Commercial Services (and other services able to be sold, i.e. call centre)	This option scored comparatively well on both weighted an unweighted scores as it provided some scope for generating additional revenues but did not necessarily demonstrate benefits to the extent of other options.
5	Establish a LACC as a Company limited by Shares for CF, CS and SS, also including members services, communications, strategy and commissioning	in-house (i.e. 5% of combined budgets)- Contract management LACC by Shares (i.e. 95% of combined budgets)- Customer First, Commercial Services (including waste), Support Services, Harbours, Member Services, Communications, ICT, management of Leisure centre contract	This option scored the same as Option 1 on unweighted scores. When weighted this option ranked higher than Option 1.
6	A Combined model (a combination of insource for member services, outsource leisure, and LACC for Customer First, Commercial Services, Support Services)	in-house (i.e. 10% of combined budgets)- Contract management, Harbours, Member services, election support, Communications, ICT LACC by Shares (i.e. 75% of combined budgets)- Customer First, Commercial Services (including consolidated waste services across Councils), Support Services Contracted (i.e. 15% of combined budgets)- Leisure centre management contracted	This option scored highest on both weighted and unweighted. This demonstrates that it was clearly the preferred option to be further considered in this Business Case.

Rating	Qualitative rating
0	Represents no scope to contribute to criteria
1	Represents negligible scope to contribute to criteria
2	Represents some scope to contribute to criteria
3	Represents reasonable scope to contribute to criteria
4	Represents excellent scope to contribute to criteria

Multi Criteria Analysis (MCA) **South Hams and West Devon Options Appraisal**

					Options												
					1		2		3		4		5		6		
Note: where items are not applicable to an option, that option has been scored the maximum score of 4					Base Case- 'As Is' with Customer First, Commercial Services, Support Service, contracted services for Waste in West Devon, Leisure		Council provide (In-house) all services including waste across the Councils (potential exceptions where skills not available)		Contract or outsource all services including administrative functions (either holistically or separately)		Establish a Joint Trading Arm between the Councils for commercial services within current Authority structure/ agreements		Establish a LACC as a Company limited by Shares for CF, CS and SS, also including members services, communications, strategy and commissioning		A Combined model (a combination of insource for member services, outsource leisure, and LACC for Customer First, Commercial Services, Support Services)		Comments
Strategic Category	Category Weighting	Sub Criteria No.	Measure	Sub-criteria Weighting	Rating	Weighted Score	Rating	Weighted Score	Rating	Weighted Score	Rating	Weighted Score	Rating	Weighted Score	Rating	Weighted Score	

5. Commercial Case Appendix

5.1. Operational Requirements

Commercial considerations in this case are quite different to either establishing a new company or expanding services of a Local Authority. The key considerations for the commercial requirements include:

- The different levels of participation of the Councils:
  - Service use;
  - Asset use;
  - Financial return.
- Voting rights;
- The flexibility to change and include new partners;
- The level of control;
- Teckal requirements;
- Pensions and TUPE;
- Tax implications.

5.2. Commercial Structure

Considering the operational requirements outlined above this section explores the likely commercial arrangements to be developed in establishing an alternate structure, such as a LACC. The current model is unlikely to have any adverse commercial implications, as such this section focusses on the commercial requirements of a LACC.

The Councils are considering establishing a LACC which it controls and contracts with to provide and receive services. The LACC would be owned and controlled by the Councils and would comply with the two tests in the Teckal case making it possible to trade with external parties and provide flexibility for procurement.

Conceptually a LACC presents:

- Greater risks, new opportunities and potentially greater reward compared to the current model;
- Potential to offset costs through generating additional revenue that respond to a changing market;
- Builds on the culture developed as part of the T18 Programme to develop a more commercial operating model.

The Teckal case (2006) set out an exemption for contracts awarded by Contracting Authorities (CAs) to legal persons under their control that took these outside the application of the procurement rules. It is often known as the in-house exemption. Similarly, the Hamburg case set out an exemption for contracts involving co-operation between public sector bodies.

The LACC must comply with the two Teckal tests (a) the company should behave and be controlled as a department of the local authority and (b) the major part of the Company's business must be with the local authority owner, so that public procurement exemptions can be accessed.

The Teckal procurement exemption applies where a contracting authority contracts with a legally distinct entity, the LACC, either on its own or with others, to provide services to the Councils. The conditions for the exemption are that:

- The service provider carries out the principal part of its activities with the authority;
- The authority exercises the same kind of control over the service provider as it does over its own departments;
- There is no private sector ownership of the service provider nor any intention that there should be any.

Further tests and expansion of this has provided clarity with regard to subsidiaries etc. which will enable expansion in the future. The Teckal trading exemption applies where in excess of 80% of the LACCs income comes from those who exercise control over the LACC Board. Teckal exemption presents the Councils with the opportunity to streamline procurement and delivery of services through the element of control over the LACC.

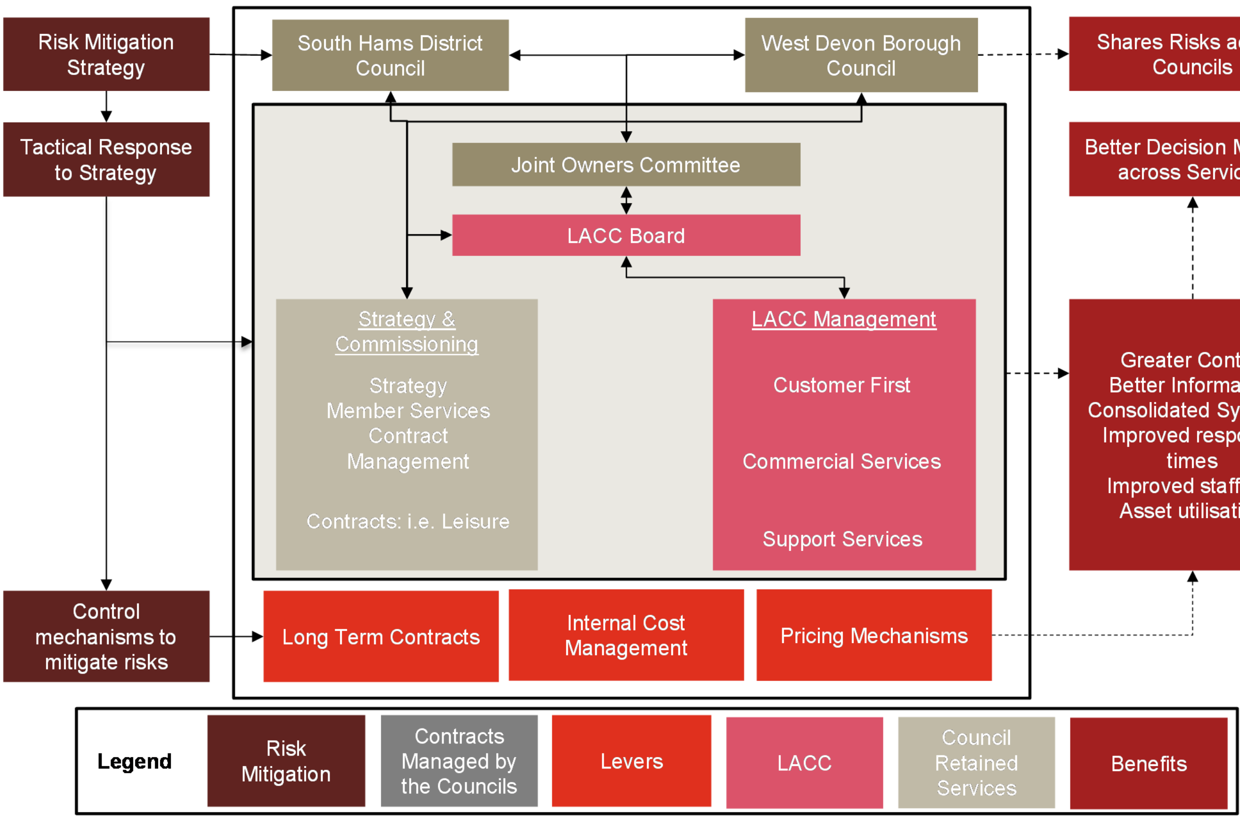
5.3. Governance

Establishing a LACC requires development of a new commercial operating model. The figure below demonstrates the proposed operating model. The key differences to the current operating model include:

- Shareholder agreements, including the preservation of essential services that could potentially be loss making over the longer term, going against commercial priorities of a LACC;
- Management agreements between the LACC and the Councils and other interfacing contracts;
- Senior leadership is likely to be split between the Councils (i.e. Executive Director, Strategy and Commissioning) and with the LACC (i.e. Executive Director, Commercial);
- Strategy and Commissioning will be responsible for strategy and policy direction, member services, harbours and contract management (including LACC and others such as leisure);
- LACC will be responsible for providing services currently provided within Commercial Services, Customer First and Support Services back to the Councils;
- Change mechanisms and levers including pricing and cost controls will be jointly managed within the contract management team;
- LACC management will be responsible for external opportunities, pricing and business development;
- Strategy and Commissioning will be responsible for setting lease, ICT and asset management strategies in line with LACC and Councils requirements; and
- Benefits realisation processes should be incorporated into the governance structure to maintain a focus on achieving the outcomes.

These items are further explained in this section.

Proposed Operating Model



5.4. Corporation Tax

5.4.1. Mutual trading and ALMOs

CTM40955 - Particular Trades: mutual concerns: surplus from mutual trading not liable

The case of Ayrshire Employers' Mutual Insurance Association Ltd v CIR (1946) 27TC331, confirmed that no tax had to be paid on surpluses from mutual trading. This is as a result of the principle that 'a man cannot trade with himself'. If a group of people join together for a common purpose their transactions with the umbrella body can be seen as mutual if:

- the body's legal framework passes the tests for mutuality, and
- its transactions are with customers who are also members and accord with its legal framework.

If a body is incorporated, its legal framework will be set out in its constitutional documents (articles). If not incorporated, in rules or whatever instrument sets out its constitution. There may also be agreements, contracts for services for example, which deal with transactions between the body and its members.

The bodies are only free from tax on their trading activities. They remain taxable on all other income and gains, including income from property or bank interest, without relief for management expenses.

There is no relief for losses made on mutual trading, and no capital allowances available on capital expenditure.

BIM 58210 - Grant aided bodies: arm's length management organisations (ALMOs)

Background

The typical ALMO is set up by a local council as a company limited by guarantee without share capital and the council is its sole member. ALMOs manage, repair, improve and maintain the council's housing stock. The ownership of the housing stock remains with the council which is also the legal landlord, and tenants remain secure tenants of the council. ALMOs also undertake a range of other services for their council that help deliver broader local authority functions, for example advice to council tenants, dealing with arrears, debt counselling, tenancy enforcement, allocations and lettings, administering the homeless and private sector housing functions such as grant administration, collecting rents from the tenants as agent for the council, grounds maintenance and community safety initiatives.

Funding

The council funds the ALMO for carrying out these services on its behalf by way of a 'management/contract fee'. The funding comes from the council's housing revenue account (HRA) and in the event of the ALMO being wound up or otherwise dissolved the memorandum and articles of association will normally state that any surplus remaining must be paid or transferred back to the council's HRA. Any monies held by an ALMO must be applied solely towards the promotion of its objects as set out in its memorandum of association. Therefore the funding received from the council must be applied by the ALMO in meeting its council member's objectives.

Taxation status

An ALMO is a separate legal entity from the controlling local authority/council and therefore it does not benefit from the exemption from Corporation Tax granted to local authorities. As an incorporated entity it comes within the tax definition of 'company' and is therefore within the charge to Corporation Tax.

We have reviewed in detail a typical ALMO, and have had discussions with the National Federation of ALMOs. The arrangements that we have seen, between an ALMO and its council member, lack the necessary element of commerciality to amount to trading.

When dealing with an ALMO, provided its memorandum and articles of association and arrangements are in line with that described in the preceding paragraphs, you may accept that the transactions between the ALMO and its council member do not amount to trading.

However, where the ALMO offers its services to third parties for reward, those transactions will be trading transactions.

Because transactions between an ALMO and its council are not trading at all, there can be no question of them being mutual trading transactions.

Any case of doubt or difficulty not covered by this guidance, and any cases where the trading status of ALMOs is in question, should be referred to CTISA (Technical) prior to the commencement of enquiries.

5.4.2. Transfer pricing and diverted profits tax

The UK's current transfer pricing rules (TIOPA 2010, Part 4) were enacted in February 2010 and took effect for all accounting periods ending on or after 1 April 2010.

The rules are widely drafted and intended to cover almost every kind of transaction including those between UK resident enterprises.

UK tax legislation requires large enterprises/groups to recognise all transactions between group companies on an arm's length basis or to adjust the results of such activities for UK taxation purposes.

The arms' length principle is that transactions between connected parties should be treated for tax purposes by reference to the amount of profit that would have arisen if the same transactions had been executed by unconnected parties. Any transactions not at arm's length should be accounted for in the company's self-assessment tax return.

The UK to UK transfer pricing potentially has an impact where there is tax at stake, either because of particular tax planning arrangements or where some more routine aspect of the tax system (such as losses in one company in the group which cannot be offset) means that there is tax to be collected.

One particular area where the rules have an effect is where no charge is made, for example, for services or for the use of assets (including intellectual property).

It would appear that HMRC has no great desire to tie up resources investigating UK to UK transactions where the tax risk is low and our experience of the level of such enquiries by HMRC since the UK to UK rules were introduced generally supports this.

Small and medium enterprises are exempted from the transfer pricing legislation completely.

The financial limits for the exemptions are:

	Maximum number of staff	And less than one of the following limits: Annual turnover	Balance sheet asset total
Small Enterprise	50	€10m/£7.6m	€10m/£7.6m
Medium Enterprise	250	€50m/£38.1m	€43m/£32.8m

**assuming exchange rate of £1/€1.31

"Enterprise" for transfer pricing purposes is defined as "the carrying on of any business".

Where an entity is a member of a group or has an associated entity the limits apply to the whole of the group in aggregate.

Based on the information we have, transactions between South Hams Borough Council, West Devon District Council and their LACC will be subject to transfer pricing as the group in aggregate exceeds the limits for exemption.

Whilst the LAs are statutorily exempt from tax on the whole of their profits and capital gains, the transfer pricing policy adopted between them and their LACC could impact the tax liabilities of the LACC. This might take many forms but the main ones are by applying a higher sales price to the LACC or a reduction in the price charged for services provided by the LACC to the LA.

The LAs, as administrative functions, are unlikely to be considered on their own as enterprises, however, as the transfer pricing limits apply to groups in aggregate it is almost certain that the LAs and their LACC will breach the employee or turnover exemption limits and the transfer pricing legislation will apply.

There is no guidance on how the rules will apply in the context of Local Authorities but HMRC has published commentary on how it will expect Charities and their subsidiaries to transact.

HMRC manuals state that Charities may find themselves within the transfer pricing regulations if they have entered into arrangements with their subsidiary companies that are not in accordance with the Charity Commission guidelines, or in instances of tax avoidance.

Applying this guidance to the LAs we recommend that all transactions between the LAs and their LACC are at market value to avoid any potential transfer pricing issues arising.

Diverted Profits Tax (DPT) is a tax, charged at 25% on profits that are considered to be artificially diverted from a UK tax charge. The legislation is complex and unlikely to be targeted at LAs/LACCs where there is no avoidance motive. Nonetheless it is mentioned here for completeness.

There are two sets of conditions where DPT would be applicable, and often both will apply to the same fact pattern.

DPT might apply to:

- a company which has UK sales being made by a related non UK company or Permanent Establishment ("PE"); and/or
- a UK company/PE which has a significant transaction with a related company – as might be the case here

and, in either case, any related income ends up in a related company with a low tax rate/concessionary tax treatment.

Please note:

- There is no exemption from the legislation for Local Authorities;
- In principle any tax exempt body making charges to or receiving services from its subsidiary could be caught by DPT, if it removes profit from UK taxation (the LA has a statutory exemption on all profits and gains).

A detailed commentary of DPT is outside the scope of this document. We would be happy to carry out further analysis if requested.

5.5. VAT

In this section, we have considered the potential VAT impact of transferring activities to the new Local Authority Controlled Company (LACC). We have undertaken our analysis based upon our understanding of the activities undertaken by the two authorities. In some instances, it has not been possible to provide a definitive position at this stage as further information will be required regarding the nature of the activities. However, to the extent it is possible, we have sought to provide an indication as to the VAT position that could be achieved to inform your decision making process.

Overview

Local Authorities (LA) benefit from a special legal regime provided for by s.33 of the VAT Act 1994. The effect of this is that LAs are able to recover VAT incurred on their non-business activities. In addition to this, LAs enjoy a favourable treatment in respect of costs incurred in relation to their exempt supplies, in that they can recover all of the VAT incurred in relation to these (i.e. the exempt input tax), provided that its total value does not exceed 5% of total input tax.

Normal businesses that do not fall to be treated as s.33 bodies are generally not able to recover VAT incurred in relation to non-business or exempt activities. The LACC will fall into this second category and as such, care will need to be taken in respect of the transfer of activities to the LACC to offset the risk of creating an irrecoverable VAT cost where one did not exist previously. For the LACC, the irrecoverable VAT costs will include any related to assets that are transferred to the LACC and operated by that entity but which are not income generating as this could be a non-business activity in the hands of the LACC.

The LAs will be able to recover any VAT charged to them by the LACC in line with their current position. However, the outsourcing of activities will lead to an increase in VAT being incurred by the LAs. Whilst there will be an increase in exempt input tax, there should be a proportionally larger increase in the 5% ceiling.

Analysis of Activities and Comments

It appears from our analysis that most of the activities that will fall to be undertaken will be taxable activities for VAT purposes and as such, entitle the LACC to VAT recovery.

Of the activities that will be transferred by the LAs to the LACC, the ones that potentially qualify for exemption and could lead to an irrecoverable VAT cost for the LACC are as follows:

- Interests over land (residential accommodation/commercial lets (where no option to tax in place);
- Provision of sporting/leisure facilities (subject to certain conditions);
- Burial and cremation services;
- Vocational Training (where centrally funded).

Exemption is available in other areas however they would not appear to be relevant here.

Assets retained by the LA

In terms of the above, with the exception of vocational training, if the LAs do not transfer the assets in question (i.e. properties/community parks/cemeteries etc.) and retain the right to derive any income, which is our understanding of the intention at this point, then it is likely that the supply by the LACC to the LA will be a taxable supply of management services only. As such, there will be no restriction to VAT recovery in the LACC and the LAs VAT position will remain broadly unchanged apart from the increase in VAT incurred as outlined above.

Assets transferred to LACC

The first point to note is that if the assets were physically transferred to the LACC, the specific nature of that transfer (sale/lease etc.) and the associated VAT treatment would need to be considered along with its effect on VAT recovery for the LA.

Should the physical assets be transferred to the LACC along with the right to collect and retain any income from their operation, the position will be different and the parties would need to factor in the potential for an irrecoverable VAT cost.

We have calculated that this cost would amount to c£1.3m pa based on the current level of expenditure. Please note that in reality this amount is likely to be overstated as it makes the following assumptions:

- All property rental income to be exempt. In reality, it is likely that the LACC will opt to tax any commercial properties, meaning that VAT incurred will be fully recoverable;
- Leaving aside whether or not leisure centre activities have already been outsourced, if these facilities were to be outsourced to the LACC (which owned and operated the assets), further consideration would need to be given to whether the LACC could qualify to be an eligible body for the purposes of the sporting exemption. If not, the significant proportion of expenditure would relate to taxable activities and be recoverable.

There would also be a restriction on residual VAT recovery, which is more difficult to quantify at this stage but is not likely to be significant given the preponderance of taxable activity.

Other Considerations

As noted above, if the assets are retained by the LAs, the VAT impact should be minimal, with the LACC able to recover most if not all of the VAT it incurs (the only exception possibly being VAT incurred in relation to exempt vocational training) and the LAs' VAT position remaining broadly unchanged apart from the increase in input tax relating to all of its business (taxable and exempt) and non-business activities. The LA's entitlement to recover that input tax will be in line with the current position.

In our experience LAs are usually on monthly VAT returns (albeit this has not been confirmed for South Hams and West Devon). It is likely that the LACC's output tax will exceed its input tax and as such, it would be recommended that the LACC requests quarterly VAT. It is of course possible that the level of net VAT due to HMRC will mean that the LACC will be subject to the Payment on Accounts Scheme.

Subject to any other commercial issues, consideration should be given to the timing of payments/invoicing. For example the LACC might consider raising invoices for its services at the start of its VAT period so that it is able to receive payment from the LAs before the end of the period, thus ensuring it has sufficient funds to make payment to HMRC. If this invoice is raised near the end of the monthly VAT period for the LA's it might be possible for them to receive the input tax from HMRC before making payment to the LACC thus mitigating the impact on their cash-flow position.

6. Financial Case Appendix

6.1. Funding Split

The funding of the existing Council services, if transferred through to the LACC, is assumed to be based on the level of activity of the Council. In simple terms, if one Council has spend of £60k and the other has spend of £40k then the transfer of this spend to the LACC will be funded in a 60:40 split.

If West Devon waste management is included within the LACC then this will adjust the original funding ratio, so that West Devon Council fund this spend. For instance, South Hams waste management spend is c£2.5m, which without the inclusion of West Devon waste management would be fully funded by South Hams. Including a c£2m West Devon waste management spend into the LACC, would lower the percentage of waste management that South Hams should fund (100% to 55%). The total cost of £4.5m would then be split upon these percentages, £2.5m (55%) to South Hams and £2.0m to West Devon (45%), which results in both Councils still funding their share of the level of activity.

This is the principle used in our work, although the exact details of this can be determined during the implementation phase. If activity levels are considered to have changed then we would assume that the funding ratio should be revisited.

Assets are assumed to be leased by the LACC from the individual Council to support the services of that specific Council within the LACC. The lease cost from each Council is thus funded in full by each Council in a circular mechanism. If West Devon waste management is not transferred to the LACC then it is assumed that the South Hams waste management lease cost would be funded by South Hams.

We have assumed that private profits are split on this ratio. The exact details of this split can be determined during the implementation phase upon negotiation between the Councils; however, it is our view that profits should not be split based on geographical source of these profits. The reasons for this is due to the principles of shared management. The management team should be motivated to maximise combined profitability and not be deviated in their strategy by conflicts of interest. It is also true that the current partnership agreement adopts the same principles.

We have assumed that set-up and on-going LACC costs, such as audit expense, are split equally.

We present below the funding split used for the scenario that West Devon waste management is LACC provided after 6 months of delay. The movement relates to the slight difference in level of activity per Council held within the LACC.

Table A

Illustrative funding split	Year before West Devon Waste Management	Year after West Devon Waste Management
South Hams	60%	58%
West Devon	40%	42%
	100%	100%

6.2. Current Net Expenditure

6.2.1. South Hams and West Devon Council Budgets

The following net expenditure profile is for South Hams and West Devon. This reflects the base case net expenditure (expenditure less income) of council delivered services (i.e. no LACC), using the council budget for 15/16 and annualised cost inflation of 2.5%. The Councils budgets for 2015/16 have been adjusted to exclude transfers to and from earmarked reserves and adjustments for IAS 19 Pension Accounting, to present a normalised net expenditure profile.

South Hams and West Devon Councils – Base Case Net Expenditure Profile

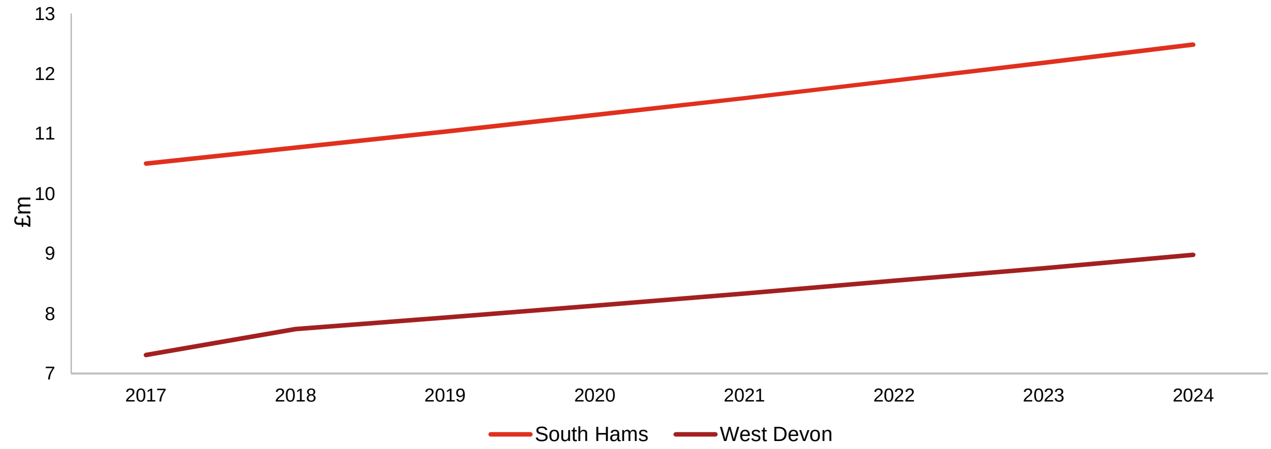


Table B

Net Expenditure Profile (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
South Hams	10,503	10,766	11,035	11,311	11,593	11,883	12,180	12,485
West Devon	7,310	7,811	8,006	8,206	8,411	8,621	8,837	9,058
Combined	17,813	18,576	19,040	19,516	20,004	20,505	21,017	21,543
South Hams % of total	59.0%	58.0%	58.0%	58.0%	58.0%	58.0%	58.0%	58.0%
West Devon % of total	41.0%	42.0%	42.0%	42.0%	42.0%	42.0%	42.0%	42.0%

If the services remain delivered by the Councils (i.e. 'As Is'), then there is an assumed re-tender cost of c£50k in 2016/17 in relation to the West Devon waste management service. The re-tendered outsourced cost has also been incorporated into the West Devon base case net expenditure profile, resulting in slight movements in the mix of annual net expenditure between the Councils. On average we can see that South Hams net expenditure profile is c58% (West Devon is c42%) of the Combined net expenditure as it currently stands.

6.2.2. West Devon Waste Management re-tendered cost profile

Table C

Current outsourced (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	Total
Re-tender costs	<<Figures removed- commercially confidential pending possible procurement>>								
Outsourced annual cost									
Total expenditure									

Table C shows the cost profile of delivering waste management on a re-tendered costs. Councils' management has provided us with the assumption that the 2016/17 outsourced cost is increased under the re-tendered by £<commercially confidential>> in 2017/18 to £<commercially confidential>> . This cost is then increased annually by the assumed 2.5% inflation. This is the base position used upon the formation of the LACC as West Devon Waste Management is not transferred.

6.3. Cashflow implications of establishing a LACC

6.3.1. Cashflow implications

We have presented the expenditure profile in our report. There are, however, cashflow considerations resulting from the transfer of services to the LACC.

Creditors

Currently the Councils make payments on 30 day terms to their non-employee related suppliers. We have assumed that the LACC would be provided with similar payment terms.

The initial proposal is that the Councils fund the LACC in advance for the provision of services. This would impose a short term cash flow burden of a month upon the Councils, which is currently not the case due to the 30 day terms to its non-employee related suppliers.

It should be possible for an arrangement to be put in place between the Councils and the LACC to delay the actual payment until the point that the LACC needs to make payment. This system could be fully integrated.

VAT on creditors

The transfer of service provision to the LACC results in the Councils receiving supplies from the LACC via service agreements. In circumstances where, to do this, the LACC subcontracts the work to another party there could be an additional short term VAT cash flow burden. This is because the Councils would pay the VAT inclusive amount to the LACC, so that the LACC can pay the subcontractor the VAT inclusive cost in 30 days time.

As discussed above, this could be avoided if the cashflows between the parties are managed so that actual payment is only made to the LACC when required.

In practice, the cost of paying staff wages will also be a cost component of the supplies by the LACC to the Councils. If the Council did not transfer its services to the LACC, the Councils would only be required to pay its own employee costs in the relevant month, which would not include VAT. However, reflecting the value of these staff costs in the supply from the LACC to the Councils imposes an additional 20% short term cashflow burden, as the Council would be required to fund the VAT inclusive employee costs in advance and not be able to reclaim from HMRC until the following month (assuming the Councils have monthly VAT return periods).

It should also be possible to put in place an arrangement to remove the cashflow impact of VAT on employee cost component of the supplies by the LACC. If the Councils were to fund the employee cost portion of the recharge in advance, so that the LACC could pay its employees, then the Councils could pay the remaining cash when the LACC is required to make payment to HMRC (payable on a quarterly basis). By this point the Council should have recovered VAT from HMRC and would not be in a worse cashflow position.

Assumption for report

We have assumed that arrangements can be put in place to ensure that cashflow impacts are removed. As a result, our analysis presents the expenditure profile and thus differences arising from non-cashflow elements.

6.4. Costs and other implications of establishing a LACC

6.4.1. Expenditure considerations for setting up a LACC – 'most likely'/base scenario

Forming a LACC and transferring the current service delivery of the Councils to the LACC should not change the fundamental costs of delivering these services; however, the LACC will incur both one off set up and annual on-going costs in addition to the service delivery costs.

We have assumed that the costs of delivering the services, now delivered within the LACC, would be invoiced to the individual Council based on the ratio of the expenditure transferred. This is explored further in Appendix 6.1.

Some of the services are not assumed to be transferred to the LACC. This includes strategy and commissioning costs (e.g. election costs) and leisure services. We have been provided by the Councils' finance team with the assumed normalised budget of the costs not transferred to the LACC. The delivery of West Devon waste management is currently contracted to FCC. We have assumed that in the base case scenario this contract is re-tendered and not transferred to the LACC.

We have assumed that all existing income (including trade waste, car parking, ferry and grant income) as well as payments relating to such things as benefits are retained by the Councils. We have assumed that separate sub-contracts are set up between the Councils and the LACC to manage this income generation to the value of the existing expenditure.

Assets owned by the Councils are assumed to be retained by the Councils and a lease cost charged to the LACC for the use of these assets. The Councils' finance team have provided us with an assumed market rate for these lease costs. We have assumed that the assets are used as part of the service to the Council providing the asset and thus forms part of the invoice to that Council.

As per the assumptions included in the Corporation Tax section there would most likely be no tax to pay on profits generated on transactions between the LACC and the Councils. As a result, an arm's length margin is not required on the transactions, as it would not in these circumstances be required within the company's self-assessment tax return. The application of this assumption results in the Council having the same net expenditure with a LACC as without a LACC.

In order for the LACC to be able to generate future reserves of its own, then this can be achieved from one or more of the following; charging a margin to the Councils, retaining any efficiencies generated and/or retaining third party profits. This is to be considered during the implementation phase and is not considered further in this paper.

We have assumed that there is no change in VAT recoverability due to the transfer of service delivery to a LACC. All costs remain recoverable. We have assumed that VAT is charged on the invoices to the Councils, and that this is fully recoverable.

6.4.2. LACC set up cost expenditure

We have assumed that set up costs required for the formation of the LACC are split equally between the Councils and are paid during financial year 2016/17.

Table D

Net expenditure Profile with set up costs (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
South Hams	10,703	10,766	11,035	11,311	11,593	11,883	12,180	12,485
West Devon	7,510	7,742	7,935	8,134	8,337	8,546	8,759	8,978

Table E

Change in net expenditure due to set up costs (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
South Hams	200	-	-	-	-	-	-	-
West Devon	200	-	-	-	-	-	-	-

6.4.3. LACC on going cost expenditure

The assumed on-going cost expenditure following the formation of the LACC has the following impact on the net expenditure profile shown in the base case position included in Appendix 6.2.1. Assumed indexation of 2.5% has been applied from 2019 onwards.

Table F

Net expenditure profile with on-going costs (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
South Hams	10,503	10,796	11,065	11,342	11,626	11,916	12,214	12,520
West Devon	7,310	7,772	7,966	8,165	8,369	8,579	8,793	9,013

Table G

Change in net expenditure due to on-going costs (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
South Hams	-	30	31	32	32	33	34	35
West Devon	-	30	31	32	32	33	34	35

Table H shows the cumulative change in net expenditure as a result of establishing the LACC.

Table H

Cumulative change in net expenditure due to on-going costs (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
South Hams	-	30	61	92	125	158	192	226
West Devon	-	30	61	92	125	158	192	226

6.4.4. LACC all additional costs

The impact on the net expenditure profile of all the assumed additional costs in relation to the formation of a LACC is as follows :

Table I

Net expenditure profile with all additional costs (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
South Hams	10,703	10,796	11,065	11,342	11,626	11,916	12,214	12,520
West Devon	7,510	7,772	7,966	8,165	8,369	8,579	8,793	9,013

Table J

Change in net expenditure due to additional costs (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
South Hams	200	30	31	32	32	33	34	35
West Devon	200	30	31	32	32	33	34	35

Table K shows the cumulative impact of the additional costs that forms the basis of the graph in the Financial Case

Table K

Cumulative Change in net expenditure due to additional costs (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
South Hams	200	200	200	200	200	200	200	200
West Devon	200	200	200	200	200	200	200	200
LACC	-	60	122	185	249	315	383	453
Combined	400	460	522	585	649	715	783	853

6.5. Opportunities as a result of establishing a LACC

6.5.1. Opportunities as a result of establishing a LACC

We have assumed that the majority of efficiencies for service delivery have already been realised by Councils management and that these do not specifically relate to the formation of a LACC.

For the purposes of the Financial Case, we have assumed that the only cost saving opportunities are in relation to West Devon waste management and the potential to cease the outsourced provision of waste services and deliver these within the LACC ("LACC provision" or "LACC provided" or "in-house").

6.5.1.1. West Devon Waste Management options

There are 4 alternative options available to the re-tendering of the waste management contract:

Option 1 - Immediate establishment of a LACC provided operation from April 2017;

Option 2 - 6 month delay in the establishment of a LACC provided operation from October 2017;

Option 3 - 1 year delay in the establishment of a LACC provided operation from April 2018;

Option 4 - Managed service provision – <<Information redacted due to commercial sensitivity>>

6.5.1.2. Acquisition of assets – Purchase of waste fleet vehicles

We have been advised by the Councils' management team that the assets to be acquired in order to establish a LACC provided operation would be acquired under finance lease. This policy would be consistent for the 4 options with the only exception being delays in acquiring the assets for option 2 and 3.

Grant Thornton's (GT) report "Options for Waste Services Delivery – January 2016" stated that the cost of acquiring the fleet would be £<<commercially confidential>>in 2015/16 prices, although we have been provided with an estimate from the Councils' management team that this cost would be £<<commercially confidential>> which we have used in our report. We have assumed that there would then be a 2.5% increase (reflecting inflation) if the assets were acquired next year (options 1,2 and 4) and then further inflation of 2.5% a year later (option 3).

We have assumed that the term of the finance lease would be 7 years and that there is a borrowing rate of 3% (as advised by Council management).

The tables below show the estimated repayment and interest profiles for the different options under finance lease arrangements.

Profile for Option 1 and 4

Table L

Option 1 and 4 (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
Addition	<<Information removed as commercially confidential>>							
Interest								
Capital repayment								
Total Liability								

The addition in 2017/18 is the estimated cost of £<<commercially confidential>>inflated by 2.5%.

Profile for Option 2

Table M

Option 2 (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
Total								
Interest								
Capital repayment	<<Information removed as commercially confidential>>							
Total Liability								

As a result of the 6 month delay in acquiring the assets under option 2, the total capital repayments in 2017/18 are half those of option 1 and 4. The total liability of £<<commercially confidential>> at the end of 2023/24 reflects that there are still 6 months of the lease term remaining to be settled.

Profile for Option 3

Table N

Option 3 (£000)	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
Total	<<Information removed as commercially confidential>>							
Interest								
Capital repayment								
Total Liability								

The addition in 2018/19 is the estimated cost of £<<commercially confidential>>inflated by a compounded 2.5%. As a result of the 1 year delay in acquiring the assets under option 3, there are no capital repayments in 2017/18. The annual capital repayment is slightly higher than the other options (£<<commercially confidential>>) due to the higher cost of the additions. The total liability of £<<commercially confidential>> at the end of 2023/24 reflects that there is still one year of the lease term remaining to be settled.

6.5.1.3. Other cost implications

The option of LACC provided West Devon waste management has different assumed one-off cost implications for the different options:

<<This section redacted due to commercial sensitivity>>

6.5.2. Third Party Revenue – potential profits from a LACC

<<This section redacted due to commercial sensitivity>>

6.5.3. Combined opportunities

<<This section redacted due to commercial sensitivity>>

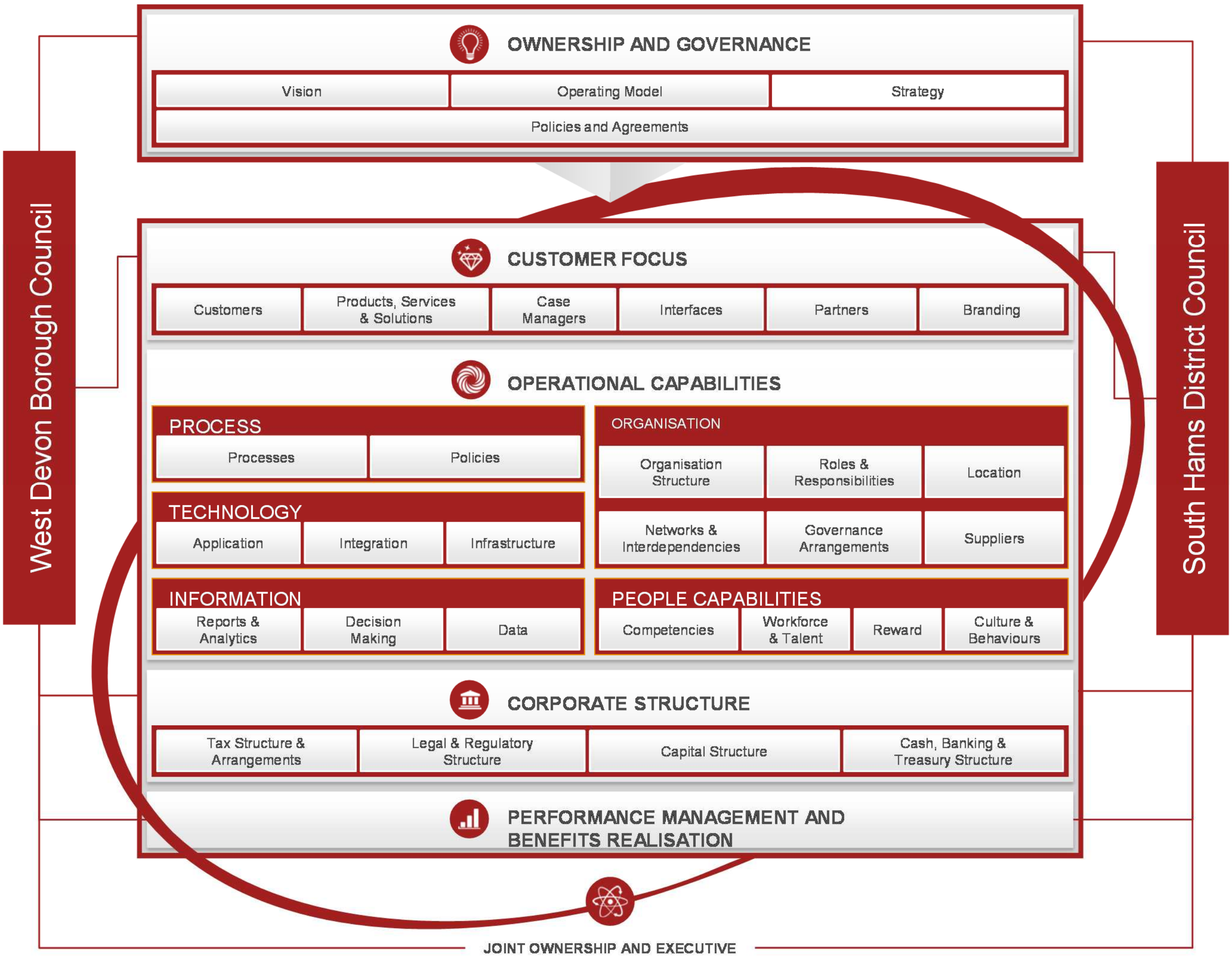
6.6. Table of assumptions used in Financial Case

<<This section redacted due to commercial sensitivity>>

7. Management Case Appendix

7.1. Transition

The figure below represents the key items to be considered in transitioning to a new operating model and each element should be incorporated into an implementation plan.



7.2. Key Considerations

This Business Case has been developed in a constrained timeframe and considered the previous assessment undertaken. We have identified a number of items that the Councils need to consider before progressing to delivery, including:

- Timing: A key driver is the termination date of the contract for the provision of waste services in West Devon and the Councils will need to consider the potential impacts of rushing the transition to a consolidated waste service across both regions. Whilst the additional cost of an extension to the current contract may appear unpalatable upon first inspection; this could be potentially offset over the longer term, with additional value being derived from the opportunity to undertake further waste service design and asset planning across the Councils. The outcome of this additional period may also indicate that re-tendering of the West Devon waste contract presents value for money.

- Skills: We have not undertaken an assessment of the current skills and capacity of the proposed management team, or their ability to deliver a successful LACC. Accordingly, there may be additional skills required that are not available currently and we would recommend a skills and capacity analysis is conducted as part of any subsequent mobilisation period, so that any additional requirements can be identified and addressed in a timely fashion.

7.3. Change Management

Market analysis identified that change management is a critical issue in the establishment of any successful LACC where traditionally one of the prime drivers for the establishment of a LACC is to develop a more commercial delivery model. Both Councils have already demonstrated through the T18 Programme that they possess both the desire and the capability to make significant changes in culture and transition to a more commercial operation.

As a result of the T18 Programme, the transition to a LACC model may not be such a significant challenge to that experienced by other councils. Change management will still need to be considered; however, throughout the life of the LACC, particularly in regard to the Councils legislative obligations to maintain employment terms and conditions of existing employees.

Further change may be required in the future to enable additional partners to join and also to develop tendering skills to capitalise on additional revenue opportunities available under the Teckal exemptions.

7.4. Stakeholder Engagement

In progressing with the preferred option a strong focus on stakeholder engagement will be required. Key stakeholders are likely to include:

- Elected members
- Internal Staff
- Administrative
- Operational (i.e. grounds, maintenance, South Hams waste); and
- Frontline
- Waste services
- South Hams
- West Devon
- Other

Different engagement strategies will be required for each of these groups. This section provides an overview of the stakeholders and key engagement to be progressed post approval of the Business Case.

Elected members

We understand that a number of briefings have already been undertaken with members regarding the strategic directions of the Councils which has included the potential for a LACC.

Internal

A number of briefings have already been had with staff regarding the strategic directions of the Councils which has included the potential of a LACC. The Councils have an established dialogue with internal stakeholders through the T18 Programme and further engagement will be required to ensure that staff understand the implications of the change to the preferred option.

Waste Services

With the transition to a new operating model, the major opportunity is the consolidation of waste services and the key items include:

- Engagement with the current provider of waste services in West Devon to agree and extension to the current contract to October 2017 to enable transition;
- Engagement with employees of the contractor in West Devon regarding opportunities in the consolidated function;

- South Hams waste services regarding assets and operational impacts or changes in transition to a consolidated service across the Councils.

Other

Further to this engagement with surrounding local authorities regarding opportunities should be established.

7.5. Implementation Plan

	Delivery Tasks	Description	Timing	Jul-Sep 2016	Oct-Dec 2016	Jan-Mar 2017	Apr-Jun 2017	Beyond July 2017
1	Approval of Business Case	Each of the Councils will consider the merits of establishing a LACC and determine whether to proceed to establish the LACC.	July 2016					
2	Transition Plan Development	Transition planning for a LACC is likely to continue in parallel with the approvals process so as to not lose time in planning the transition requirements of establishing a LACC. Transition planning will be used to define operational requirements for services provided by the LACC to the Councils and its own specific requirements. This should also include consideration of interim skills requirements, i.e. for market development.	July 2016					
3	Engage specialist advisors (Legal / Financial)	The Councils will need to seek legal and financial/commercial advice in establishing a LACC and the documentation required to support its implementation. Engagement of advisors can occur in parallel to the approvals process.	July 2016					
4	Apply to HMRC regarding exemptions	HMRC may grant an exemption to the LACC from Corporation Tax relating to income generated through trading solely with the Councils. Engagement should be undertaken early with finalised if the Councils proceed to establish a LACC.	July 2016					
5	Shareholder/ Joint Agreement development	Building on the current Collaboration agreement between the Councils formal shareholder agreements will need to be developed and negotiated between the Councils. Each Council should seek independent legal advice throughout this process.	July-August 2016					
6	Company structure agreed	Informed by the Shareholder agreement the final company structure will be determined with key articles outlined.	August 2016					
7	Governance, management structure and decision making framework developed	Informed by the Shareholder agreement the governance and decision making framework can be developed, agreed and finalised.	August 2016					

	Delivery Tasks	Description	Timing	Jul-Sep 2016	Oct-Dec 2016	Jan-Mar 2017	Apr-Jun 2017	Beyond July 2017
8	Combined waste fleet strategy	To facilitate management of waste services across the Councils from within the LACC a combined waste fleet strategy should be developed to identify opportunities to leverage existing assets. Waste collection will remain separate as each of the Councils has distinct needs which the current collection processes address. This will also identify timing.	August 2016					
9	Building Control Partnership engagement	Engagement with partners to determine involvement of the Building Control Partnerships role within a LACC structure, i.e. a subsidiary or identify what is required to consolidate into the LACC if deemed appropriate.	August-September 2016					
10	TUPE process commence, pensions calculations and registration	Following approval by the Councils the TUPE process should commence and include calculations and specific pension requirements. This is likely to require agreements between the LACC and the Councils and also with the Fund(s).	August-September 2016					
11	LACC scope of services defined	The T18 Programme has developed an operating model and this model should be confirmed and the services to be provided to the Councils combined and to each of the Councils individually.	October 2016					
12	LACC Interfaces identified	With a confirmed understanding of the services to be provided to each of the Councils by the LACC key interfaces will need to be identified, i.e. financial reporting and controls across each of the parties.	November 2016					
13	Lease agreements (assets and vehicles)	With the Councils retaining their respective assets appropriate lease agreements between each of the Councils and the LACC will need to be developed.	December 2016					
14	Contractual arrangements	Consolidation of all contractual arrangements agreed and executed enabling establishment of the entity.	December 2016					
15	Financial Positions	Detailed financial positions agreed for services to be provided, payroll figures, cashflows, budgets, reporting and audit requirements identified.	December 2016					
16	Company registration	Registration of the LACC as a Company prior to trading.	February 2017					

	Delivery Tasks	Description	Timing	Jul-Sep 2016	Oct-Dec 2016	Jan-Mar 2017	Apr-Jun 2017	Beyond July 2017
17	Payroll establishment	Establishment of new payroll.	April 2017					
18	VAT registration	Registration of the LACC for VAT.	April 2017					
19	LACC commence	LACC commence operational transition (timing of waste services in West Devon to be determined). This may include interim performance measures to allow for issues to be resolved without penalties.	April 2017					
20	LACC fully operational	The LACC is operational with appropriate performance measures in place for services to be provided to the Councils. Ability to	October 2017					
21	Skills development for tendering	Following initial establishment and transition phase further analysis of skills required to generate additional revenue from outside of the Councils.	2018					
22	Market development (public sector)	Market development for public sector services currently provided by the LACC to the Councils.	2018					
23	Market development (private sector)	Market development for private sector parties for services provided by the LACC.	2019-2020					

7.6. Risk Matrix

			Option		Potential Impacts (quantitative)	Treatment/Mitigation
			6			
		Note: Comparative risk assessment considered against current operating model.	A Combined model (a combination of insource for member services, outsource leisure, and LACC for Customer First, Commercial Services, Support Services)			
			Unmitigated	**Mitigated**		
Political	**1**	The risk of not being able to meet Member requirements, causing complexity/disputes in the contract	Med	Low	Minimal impact as current service level should remain	Clear articulation of service provision to Members in agreements/contracts
Political	2	The risk of community backlash from the model cause restructure	Med	Low	Costs relevant to restructure the responsibility of the Councils	Communication program
Political	3	The risk that governance is not implemented appropriately causing confusion between ownership and management	High	Med	Minimal impact in £ but could cause delays which has an opportunity cost	Establishment of appropriate governance and management functions in the shareholder agreements
Political	4	The risk that local authority services are not able to successfully transition to commercial structure resulting in additional costs	Med	Low	Costs of additional transition costs responsibility of the Councils	Demonstrated success of T18 Programme and primary structural change is not service related
Political	5	The risk of creating a dual workforce with different employment terms and conditions	High	Med	The assumed efficiencies are likely to be minimal as significant progress (~30%) have already been made	Communication program for existing and new starters

			Option		Potential Impacts (quantitative)	Treatment/Mitigation
			6			
	6	The risk of contract terms resulting in delays to mobilisation in emergency situations	Med	Low	Potential additional mobilisation costs in emergency situations	Provisions in contracts with regard to emergency situations
	7	The risk of increasing complexity of pension schemes resulting in increased administration costs	Med	Low	Existing liability remains responsibility of each Council Impact is if efficiencies are not realised	TUPE planning and resource management
	8	The risk of a new model failing, resulting in political backlash	Med	Low	Any costs incurred as a result backlash	Communications program
	9	The risk of Government policy impacting Local Authority structures (i.e. Devolution)	Med	Med	Costs are not able to be estimated	Communications program Stakeholder engagement in DCLG
	10	The risk of legal challenge regarding staff transfer, resulting in delays and increased costs	Med	Low	Legal costs to be funded by the Councils	Communications program considering larger impacts such as service cuts
	11	The risk of challenge to services being transferred which are unable to be sold elsewhere	Med	Low	Any costs resulting from decisions made	Communications program outlining links between matrix model and reduced duplication across the Councils and the LACC
	12	The risk of not meeting budget constraints resulting in services being cut	Med	Med	Potential cashflow implications if additional short term cost impacts	Further efficiency planning and LACC retaining some cash reserves in scenarios where Council budgets are further constrained
Budget	13	The risk of complex financial arrangements between entities leading to confusion regarding cross subsidisation	High	Med	Additional cost control or financial assurance costs	Management and reporting structure developed from the outset

			Option		*Potential Impacts (quantitative)*	*Treatment/Mitigation*
			6			
	14	The risk of perceived differences between ownership, control, returns and rewards	Med	Low	n/a	Shareholder agreements and contract with LACC or articles to cover key issues from establishment
	15	The risk of financial failure resulting in step in (i.e. from Councils or DCLG)	Med	Med	Costs of step in if external specialist resources required	Thresholds included in shareholder agreements and contract for step in rights or rectification measures Exit strategy also included
	16	The risk that skills are not developed to enable successful tendering resulting in anticipated external revenues not being realised	Med	Low	Any additional costs associated with training or skills development Potential additional cost of sales force if internal skills not developed	Change management strategy development
	17	The risk that anticipated capacity or skills is not able to be met resulting in revenues/savings not being realised	High	Med	Additional costs of tendering	Change management strategy development
	18	The risk that locational influences do not enable additional partners or expansion, resulting in anticipated efficiencies not being realised	Med	Low	Additional costs associated with engagement of potential partners in other areas	Communications program
Capacity	19	The risk that Council assets are not able to appropriately accommodate commercial requirements, increasing costs if additional assets required	Med	Med	Any additional asset related costs Not anticipated to be significant as capacity available from T18 Programme	Asset management plan for each Council coordinated with LACC operational requirements

			Option		***Potential Impacts (quantitative)***	***Treatment/Mitigation***
			6			
	20	The risk that other Councils set up similar ventures creating more competition	High	Med	Costs associated with tendering, lesser margins if price competition	Sales strategy developed at the appropriate time
	21	The risk of ownership disputes between current or new partners	Med	Med	Any costs associated (i.e. legal) or resultant delays	Shareholder agreements and contract with LACC or articles to cover key issues from establishment with regard to dispute resolution procedures
	22	The risk HMRC exemption not realised resulting in tax uncertainty	High	Med	Potential for corporate tax payable Assumption being limited profitability in the immediate future, therefore not likely to be a major cost factor	Early engagement with HMRC
	23	The risk that specific efficiencies of consolidated waste services are not realised	High	Med	Likely that WDW services contract is going to be more than current, therefore extension impacts are the additional delta between the two costs	LACC operational planning
	24	The risk that this sets a precedent for all LAs that Central Government does not agree with and adverse action is taken or policies implemented	High	Med	Transition costs if arise would be responsibility of the Councils	Communications program and engagement with Central Government
Other	25	The risk of further unforeseen funding cuts impact the Councils ability to fund the LACC	Med	Med	Implications of the LACC operating at a loss are yet to be considered	Budget planning by each Council and the LACC retain cashflow as preventative measure

		Option		*Potential Impacts (quantitative)*	*Treatment/Mitigation*
		6			
26	The risk that service quality is reduced (real or perceived)	Med	Med	Any costs associated with rectifying service quality	Service quality standards in relevant contracts
27	The risk the LACC doesn't meet compliance obligations	Med	Med	Any additional costs relating to compliance incurred within the LACC	Establish reporting and management structure that meets compliance obligations
28	The risk the Councils don't meet their statutory obligations	Med	Low	Any additional costs relate to each Councils obligations	Establish reporting and management structure that meets compliance obligations
29	The risk that the financial assumptions change (i.e. tax)	Med	Med	Any additional changes would be within the LACC	Scenario modelling regarding potential downside and upside
30	The risk of going over the Teckal thresholds	Med	Med	Costs associated within the LACC to meet i.e. up to 20% additional capacity	Options and thresholds considered into decision making framework Positive position to be in and have demonstrated successful ability to further transition to company without need for Teckal exemptions
31	The risk that insurances impact ability to deliver services to external parties	Med	Med	Any additional costs over and above current insurance costs	Insurance strategy to be developed as part of Phase 2
32	The risk that legal advice changes assumptions in the business case	High	Med	n/a	Legal advice to be obtained early in Phase 2
	Overall	Med	Med		
	Comments				
	Scale:				

	Option	Potential Impacts (quantitative)	Treatment/Mitigation
	6		

High - High Risk

Medium - Moderate risks

Low - Low Risks

7.7. Post Implementation Review

Post implementation reviews will be incorporated into the benefits realisation plan to ascertain whether the anticipated benefits have been delivered. Reviews will take place six monthly for the year after transition and then incorporated into annual budget and funding cycles. The objectives of the reviews will be:

- Identify delivery against planned activities;
- Identify what was done well, and why it was done well;
- Identify what could have been improved and how;
- Confirm if the project achieved its main objectives and that the cost reductions are being realised.

Thereafter there will be on-going monthly monitoring, reporting and quarterly reviews.

7.8. Future Considerations

When considering the changes in the sector in the recent past it is hard to predict the future. In establishing a LACC the Council have a number of options, including:

- The ability to develop internal commercial skills to expand reach into potential markets;
- The ability to source external skills if required to supplement internal capability with regard to tendering;
- Potential to adapt the commercial structure if revenues increase to levels that exceed Teckal exemption;
- Opportunities to take on other owners (i.e. other Local Authorities) with restructured shareholdings to expand the overall value of the 20% to maintain Teckal exemptions.

A broad range of factors including timing, skills, market characteristics, services offered externally etc. As there are a number of permutations, we have not considered these in detail. Establishment of a LACC does not necessarily restrict expansion and is flexible enough to respond to market conditions and drivers of the Councils.

In a broader context, the Councils still retain the right to increase taxes or reduce services within the structure.