

CHESHIRE EAST COUNCIL

Cabinet

Date of Meeting: 24th June 2013
Report of: Head of Public Protection and Enforcement
Subject/Title: Preferred Delivery Model for Leisure, Sport, Play and Development Services
Portfolio Holder: Councillor Janet Clowes

1.0 Report Summary

- 1.1 This report and its appendices set out the benefits, implications and proposed approach to the creation of a new delivery vehicle for the council's leisure facilities, sport, play and development services. It summarises the work of specialist leisure consultants FMG, who were appointed to look at the various different company models and then evaluate and report back on a preferred model that would safeguard the scope and quality of the existing service, whilst achieving the required efficiency savings as set out in the Council's three year plan.
- 1.2 The report seeks Members' agreement to set up a charitable trust (limited by way of guarantee), whereby the Council retains the freehold of the current physical assets.

2.0 Recommendations

It is recommended that

- 2.1 Cabinet note the findings of the options appraisal and consultation exercise that have concluded that the most appropriate delivery model is that of a new charitable trust. (The full options appraisal report is attached at appendix A for completeness);
- 2.2 Cabinet approve the formation of the Trust and the transfer of leisure services into it with an effective operational target date of 1st April 2014, with the trust being established by the end of the year (December 2013) at the latest. (The implementation date of the 1st April 2014 assumes that there will be no significant delays in relation to critical external dependencies (i.e.- Charity Commission registration));
- 2.3 Cabinet give delegated authority be to the Head of Public Protection and Enforcement (SRO for the project), the Borough Solicitor and the Section 151 Officer (or the officers that are devolved those powers) to commence the detailed implementation of the Trust, in consultation with

the Portfolio Holder and Leader of the Council, (this will involve (but is not limited to) an update on progress which will be presented to Cabinet in October 2013), using the following actions and timetable:

- Start formal consultation with staff and Trade unions- **July 2013-onwards**
- Development of a robust, detailed Business Plan, which includes an asset investment plan (for the Trust), performance specification and details of contract management- **Oct 2013**
- Complete formation and registration with the Charities Commission- **Nov 2013**
- Advertise intention to award contract – **Nov 2013**
- Recruitment and appointment of a board of trustees (see 2.4 below) - **Sept -2013**
- Recruitment and appointment of the Trust's Senior Management Board- **Nov 2013**
- Complete condition surveys for all the buildings at cost of approximately £20k- **Nov 2013**
- Commission the Pension Actuary to confirm cost of any bond - Approximately £5K - **Aug 2013**
- Finalisation of staff transfer arrangements and related HR, insurance considerations; and operating procedures.- **Dec 2013**
- Shadow Trust becomes operational- **Dec- 2013**
- Enter into lease(s) for all facilities with the Trust on terms and conditions to be agreed by the delegated officers- **Feb- March 2014**
- Novation of current joint use agreements and other service contracts **March 2014**
- Entering into pension admissions agreement and staff transfer agreement plus formal transfer of staff and services - **April 2014**

2.4 Cabinet nominate two elected members to serve as the Council's representatives on the Trust Board, subject to approval by full Council in July 2013.

3.0 Reasons for Recommendations

- 3.1 There is a need to achieve best value for the services that the Council directly commissions and provides, and to reduce net operating cost wherever possible, whilst at the same time maintaining the best possible service for its residents in line with the Council's agreed three year plan.
- 3.2 The establishment of a charitable trust means that the Council's leisure facilities and related services will not be outsourced to the private sector. A trust will also help to achieve the key objectives set out in 3.1 (above), whilst also maximising opportunity for local partner engagement (eg Town and Parish Councils) and promoting high quality service delivery, (eg through enhanced or newly built Leisure facilities).
- 3.3 The detailed options appraisal (appendix A) has concluded that the most viable option for future service delivery is a charitable trust and this should be in the form of one newly created by the Council for this purpose. The charitable trust will seek the advancement of health and sport and recreation across the borough as their primary objective.
- 3.4 The principal benefits of this option over all the others considered is that it allows the Council to focus its delivery of leisure services through an independent company. This will enable significant VAT and NNDR savings to be made and allow the company's management and staff to have a single focus free from the distractions of the Councils day-to-day operational requirements, which should in turn lead to an improved and enhanced service. At the same time, the Trust will have access to financial and other resources to enhance service delivery which are not available to the Council.
- 3.5 A four week consultation exercise has been undertaken with current service users and the evaluation of the responses received shows that 62% were supportive of the Charitable Trust option. A number of responses were also received from Schools and Parish Councils. (The full consultation analysis is attached at appendix B)
- 3.6 The project has been through the Council's Project Gateway process for review and was given endorsement on 14th May to proceed, subject to Cabinet approval. The project is a major change project and therefore will be included as part of the Council's Highlight Report framework.

4.0 Wards Affected

- 4.1 All Wards are affected

5.0 Local Ward Members

- 5.1 All Local Ward Members

6.0 Policy Implications

6.1 The project is in line with the Council's three year plan and is instrumental in the achievement of:

- The Council's agreed three year plan outcome 5 –People live well and for longer- in particular that "local people have healthy lifestyles and access to good cultural, leisure and recreational facilities".
- The Council's Business Plan identifies efficiency savings linked to Leisure services (Priority 6. Redefining the Council's role in core place-based services- 6.1: Develop new delivery model for leisure operations).

7.0 Financial Implications

7.1 The financial savings associated with the establishment of the Trust do not currently include any potential savings arising from a revision of staff terms and conditions, following the transfer of Council staff in this service to the Trust. This will be explored in more detail and any potential savings will be in addition to those that are mentioned later in this report.

7.2 The external consultant's report commissioned to review the various delivery vehicle options calculated that the trust model delivers the highest amount of annual savings for the Council, with an existing trust providing a greater level of savings than a new trust. This is mainly because an established trust has lower management costs, easier access to capital funds that can be invested to generate additional income, greater economies of scale and new expertise that a new trust could not offer in the short term. This was confirmed in the net present cost modelling of each option over a 25 year period (see table below). However as identified in section 10.2 of this report in non-financial terms, the service and community benefits associated with a trust model provide a clear driver for setting up a new trust that can become a strong delivery vehicle across leisure and other, related services in the future.

7.3 No consideration has yet been made as to the length of the service delivery agreement with the trust or the lengths of leases to the trust. This will form part of the detailed Business Plan development process

7.4 There is further work required to review the figures provided in the consultant's report and to investigate further costs of implementation. In particular, the additional staff pension costs, the impact on the Council's support services costs, and the nature and level of further savings that could be delivered.

7.5 However, it is clear at this stage that the NNDR and VAT savings alone present a strong business case for the move to trust status. The report

indicates that a saving of 20% of net direct service costs could be saved through NNDR and VAT benefits:

	In-House (Base)	£ Private Sector £	Existing Trust £	New Trust £	New CIC £
Total 25 year cost	£94,940,205	£91,424,170	£77,234,553	£84,664,134	£105,451,700
Net Present Cost (including set-up costs)	£60,473,754	£58,516,256	£49,477,942	£54,180,446	£67,421,434
25 Year Benefit compared to base NPC	£0	£1,957,498	£10,995,812	£6,293,307	-£6,947,681

Figures provided by FMG

The recommendation is to establish a new charitable trust, as this will provide a good level of saving and will deliver the greatest non-financial benefits to the Council, particularly in relation to meeting the Council's strategic priorities and the integration of related services. All current sites within the Council's Leisure facilities will be included in the scope of the new Trust.

- 7.6 The total cost of implementation of the preferred model is in the region of £200k and funding is already in place for this. However, members should be aware that examples from other authorities have indicated that this could be as high £400k. The costs of implementation will be monitored closely by the project manager.

Within the £200k, allowance has been made for external legal advice, a dedicated Project Manager and extra capacity to support the assets service. Delivering the project within this budget will depend on whether any unexpected implementation costs are incurred and the capacity of the other corporate enablers (HR, Finance, Procurement) to deliver. So, if a shorter time frame is required than that recommended at 2.2 (above), then the cost will be considerably more, and further work will be required to establish a clear budget for the establishment of the charitable trust before work on this could start.

8.0 Legal Implications

Procurement

- 8.1 Unless the Council is outsourcing the service delivery to a company that is wholly controlled by Cheshire East Council it will be necessary to undertake a procurement exercise.

Contracts for the provision of leisure services are “Part B” Services for the purposes of the EU procurement rules. Part B Services contracts should ordinarily be competed under EC Treaty principles where there is a realistic prospect of cross-border interest for the award. If this arises then a proportionate level of European wide advertisement and competition should be carried out in order to open up the opportunity to fair and transparent competition in the European provider market. The form of advertisement need not be by Contract Notice in the OJEU (although this is often used as an effective way of discharging this obligation).

- 8.2 As the value of the service contract exceeds £173,934, the contract is also further subject to limited application of the Public Contracts Regulations 2006 (as amended) and, in particular, in relation to non-discriminatory technical specifications; requirements to treat bidders equally and in a non-discriminatory way; and also to act transparently. The level of representation on the trust board cannot exceed 20% otherwise the trust cannot be seen to be independent for charitable purposes. In order to achieve the full tax benefits, a charitable trust cannot be wholly controlled by the Council. This is pertinent because the only exemption from the procurement requirements is in a situation where the services are being transferred to a company that is a wholly owned and controlled company (this is called the *Teckal* exemption). External legal advice has confirmed that transferring the service to a wholly owned company (the *Teckal* company) and then, subsequently, transferring the company into the ownership of the leisure trust would not provide a more viable route since, in disposing of the *Teckal* company, the new ownership arrangements introducing private interests would invalidate the *Teckal* status of that company and therefore it would not be able to retain the arrangement to provide services back to the Council. Indeed, the establishment of a *Teckal* body for the purposes of an imminent onward sale could, in itself, be considered a single linked transaction in breach of the procurement rules.
- 8.3 In the event that the Council, following due diligence, concludes that there is not sufficient cross-border interest in the leisure service, it can make a direct contract award to a trust. However, this is open to challenge. If successfully challenged, the contract could be set aside as ineffective and the staff and service will revert back to the Council. If a procurement challenge is brought under the Public Contracts Regulations 2006 for the award (or prospective award), then the complainant would normally only have 30 days to bring proceedings

from when they first knew, or ought to have known, the grounds of starting proceedings arising. The courts have discretion to extend this to 3 months in exceptional circumstances. Therefore, market notification (in terms of a press release or award notice in the OJEU) may be sufficient to commence time running for this purpose. This may not be attractive as it would mean drawing attention to the issue, but would serve as a means of revealing possible industry objection. A challenge on the basis of a judicial review of the Council's decision, on the basis of non-compliance with the EC Treaty principles, would have to commence within 3 months from when the grounds for challenge first arose.

A complainant could raise a complaint with the European Commission which would then investigate the issue with the UK government. If it is unsatisfied with the justification in response, it could ultimately refer the issue to the European Courts. Such actions would lie against the UK government (rather than directly against the Council), which could ultimately result in the member state being fined (though this is rare). There is no time-limit for such a complaint being brought to the Commission. Expert legal advice will be required in the event that the award is challenged and this will be in addition to the external legal resource already figured into the project cost.

- 8.4 The Council will also need to consider the risk of any funding to the Trust being deemed unlawful state aid. State Aid may arise where the Council provides aid to select undertakings (any entity which puts goods or services on the given market), which has the potential to distort competition and affect trade between member states of the European Union. The outsourcing of Glasgow's leisure and cultural services to a leisure trust was, for example, formally challenged on state aid grounds; the challenge was however turned down by the European Commission. It will be important therefore to ensure that state aid is properly considered as part of the decision making over the structure of the detailed arrangements in this case.

The council has a duty to obtain best consideration under section 123 of the Local Government Act 1972, if it grants any lease for more than 7 years.

Governance and joint use arrangements

- 8.5 Where leisure facilities have shared use with schools, the Council has inherited contracts in place currently with those schools, that set out the terms of joint use of the facility and the responsibility for payments. The majority of these contracts will run until 2015 at the earliest and any transfer must be subject to the trust honouring those contracts. If legally permissible, the contracts will be novated to the Trust. Other contracts, for example catering and vending contracts, will also require novation, and due diligence is required at each site to identify these service contracts. Once the joint use contracts have come to an end, the trust will be free to re- negotiate them with the individual schools. This could

provide additional benefit to the trust as, at this point, the new contracts ought to more closely reflect the true cost of the service provided.

- 8.6 If service delivery is transferred to a Trust, the Council will not maintain controlling influence over decision making and it will not be able to depend on transferring further services to the Trust, should it decide to do so in the future, as this will need agreement by the Trust.
- 8.7 The Trust will have its own governance arrangements and approval process for appointing people as Trustees. The only representation on the Board the Council is permitted is an allocation for appointing people as Trustees. of less than 20 percent of the Trustees. A balanced trust board (including elected members and senior officers) would allow the Council to retain a degree of strategic influence, to seek to, ensure service delivery is aligned with the priorities of the Council.
- 8.8 A detailed outcome specification and performance management system from the Council will ensure services and standards are focused on the priorities of the Council and the needs of local residents, with any management fee linked to the delivery of agreed outcomes.

8.9 Company Limited by Guarantee (CLG)

A charitable company limited by guarantee is a legal entity incorporated under the Companies Act 1985. Unlike the most common company structures, it does not issue shares but instead the members of the company undertake to guarantee to contribute a sum of money (normally a nominal value) in the event that the company is wound up,

The members of the company have limited liability to the level of their guarantee. These companies are regulated by the Charity Commission and are also subject to the requirements set out in the Companies Acts. It is considered that this approach offers flexibility compared to other NPDO models and they are able to change their rules to meet the needs of the business.

The Directors of the Company are called the Trustees and it is they that are responsible for compliance with the Companies Act and Charities Act and this requires a higher level of skill and knowledge in the company's administration.

This structure has the benefit of receiving NNDR relief and VAT benefits as registered charities.

TUPE and Staff Considerations

- 8.10 Transferring the service delivery to an arm's length company such as a Trust will trigger a TUPE transfer of current Council staff who are working in or for the leisure service immediately before the transfer.

- 8.11 The Council will have to undertake the necessary due diligence to identify which employees have the right to transfer to the Trust and to be able to provide the necessary employee liability information in accordance with the TUPE regulations. The Council and the Trust will also have to comply with the Regulations' consultation requirement, which stipulates that consultation on any planned changes to terms and conditions of employment (measures) needs to be conducted in good time before the transfer. In "good time" is not defined in the regulations, but a comparison is usually drawn with the timescale for redundancy consultation which is 45 days.
- 8.12 It is possible that, as part of this project, a review of employment terms and conditions will be undertaken to ensure the future success of the new model in its particular market. (This will form part of the early discussion between the Council regarding the new model and also part of the consultation with the Trade Unions). Where this reveals a need for different terms and conditions, these may apply to new employees from day one.

Under the TUPE regulations the terms and conditions of existing employees may not be changed in preparation for, or for reasons purely connected to the transfer, nor can redundancies be made in contemplation of the transfer without significant risk of challenge and claims against both the council and the trust which would inherit those risks from the point of transfer. In additions any changes made prior to the transfer could be deemed invalid in any event.

Under the TUPE regulations post transfer, terms and conditions may be changed and employees can be made redundant if there is an economic, technical or organisational reason and if this entails changes to the workforce.

NB: The Government is currently consulting on possible changes to the TUPE regulations. These changes may be enacted by October 2013. Legal services will advise on any impact which these changes may have on this project as soon as there is clarity on the changes.

- 8.13 It is possible that the Trust will want to adopt a form of performance related pay. This will require research into the differing models of PRP in relation to the industry within which the model operates. Potential costs of this will need to be factored in to any business case proposals to ensure adequate funding post-transfer.

Ultimately, the decision on and implementation of performance related pay will be a matter for the Trust - which may seek expert advice in relation to the same.

- 8.14 Specialist pension/actuary advice will be required on transferred staff pension issues and confirmation of the potential bond costs will need to be established, which could be considerable in relation to the

transferring staff. If the Trust chooses not to offer access to the LGPS pension for any new starters it will also have to seek expert pension advice in relation to what pension fund to offer new starters and the required implementation and associated costs.

- 8.15 As part of the implementation plan, the Board of Trustees will be appointed and this board will become responsible, as part of its early activities, for forming and recruiting to the management structure of the Trust.

9.0 Risk Management

There are number of risks associated with the project. These are captured in detail along with mitigating actions as a part of the Project governance. Those set out below represent the pertinent risks that it is felt necessary to bring to the attention of members at this stage of decision making.

- 9.1 Early and continued engagement with trade unions and the existing workforce even at this early stage will be key to successfully delivering the outcomes of the review and also in transitioning to a new delivery model successfully and with no discontinuity of service provision.
- 9.2 Early and continued engagement will also be required with the Cheshire Pension fund in relation to the actuary reports required in relation to the transferring employees, bond requirements and pension changes, and the completion of a Pension Admission Agreement. The Cheshire Pension Fund are already aware of the request and, once a decision is made by Cabinet to proceed, they will be formally instructed to commence the work.
- 9.3 The creation of the Trust well in advance of the anticipated transfer of service date will ensure that the Trust is able to undertake all the necessary preparatory steps prior to the transfer and to engage in the necessary consultation both with the employees and the Council.
- 9.4 Considerable input from Legal and Assets Services will be needed to ensure the Council's ownership of the related physical assets is protected, in order to secure the future use of the assets for leisure and recreational purposes. Members of staff from the legal service form part of the project team and allowance has been made within the implementation costs for the required assets work to be carried out.
- 9.5 There will be a number of Procurement issues that will need to be considered further as part of the in-depth review of the preferred delivery model. These will include current regulations that address asset and service transfer. Guidance suggests that there are different routes depending upon whether the asset is to be transferred or a service is to be transferred.

- 9.6 The ongoing issues with maintenance and development of the Council's physical asset stock mean that major investment will be required in the near future to deliver the planned new local Lifestyle Hubs. This level of major asset work can be incorporated into any future delivery model, but it is more complex if a private outsourcing model is selected, due to the contractual nature of the relationship with a third party provider, and this is compounded if the likely outcome of the asset strategy is unknown when the contract is entered into. This will be further explored as part of the review.
- 9.7 In order to achieve the fiscal benefits of a trust model, it is also likely that the existing and any future leisure facilities will be leased to the company, with appropriate safeguards around facility maintenance and service delivery, so as to protect the Council's interests.
- 9.8 Whilst a different delivery model could realise revenue budget savings in relation to changes in VAT status, care will need to be taken in respect of arrangements for future capital investment (i.e. to avoid incidence of significant irrecoverable VAT on developments).
- 9.9 Currently the Shared Services Single Legal Entity is being established. As part of this implementation process consideration will need to be made as to whether it will be possible to oblige the Trust to continue using the shared services arrangements on an interim basis. Dependant upon this clarification savings from this element may take longer to realise. It needs to be noted however that the final decision on the provider of these services will be made by the Trust.
- 9.10 Similarly, the impact on the Council's other support services associated with this project will need to be managed effectively, as part of the project. This will ensure the Trust retains the necessary expenditure and staff resources to deliver the core business, whilst reducing the likelihood of any residual overhead remaining with the Council.

10.0 Background and Options

- 10.1 The establishment of a trust to deliver leisure operations was considered in the early life of CEC and was deemed by elected Members to be the preferred delivery model at that time. This report has concluded that this is still the most appropriate option.
- 10.2 Initial advice has indicated, in financial terms, that a transfer of leisure facilities, either to a new trust or existing trust model, is likely to provide the greatest potential for savings. In non-financial terms, the service and community benefits associated with a trust model provide a clear driver for setting up a new trust that can become a strong delivery vehicle across leisure and other, related services in the future.

Action Plan for implementation

10.3 In order to implement a delivery model, there is a large amount of documentation to be prepared and legal requirements to be met. This will require a specialist dedicated Project Manager with in-depth knowledge of the area and a dedicated internal project team will be needed. With this in place, the preferred model should be achieved in time for the next financial year.

11.0 Consideration of Options

11.1 The purpose of the options report was to deliver an appraisal for leisure services and to determine the future delivery models which also include leisure, sports and play development services. The analysis covered both the financial and non-financial implications of different management vehicles and has covered a wide range of potential options, including:

- Continued in-house management;
- Outsourced management – either through a private company or an existing charitable company (Trust); and
- Establishing a new company – either charitable or non-charitable, covering the following options:
 - Unincorporated Charitable NPDO;
 - Industrial and Provident Society (IPS);
 - Company Limited by Guarantee (CLG);
 - Charitable Incorporated Organisation (CIO);
 - Limited liability partnership (LLP);

11.2 The report assessed the financial implications of the outsourcing options being considered based on the following key income and expenditure areas:

- the current net direct costs of the services;
- the impact of VAT and NNDR on the different models;
- the impact arising from central support costs;
- profit, contingency and overheads;
- the impact on pension costs to the Council and operator;
- set-up costs and timescales;
- operational changes to increase revenue or reduce costs; and
- implications of including other services within the commissioning opportunity.
- The potential to work more closely with partner organisations, including Town and Parish Councils, in alternative delivery models.

11.3 The external consultant's report commissioned to review the various delivery vehicle options calculated that the trust model delivers the highest amount of annual savings for the Council, with an existing trust providing a greater level of savings than a new trust. This is mainly because an established trust has lower management costs, easier

access to capital funds that can be invested to generate additional income, greater economies of scale and new expertise than a new trust could not offer in the short term. This was confirmed in the net present cost modelling of each option over a 25 year period.

- 11.4 However, the recommendation is to establish a new trust charitable trust, as this will provide a good level of saving and will deliver the greatest non-financial benefits to the Council, particularly in relation to meeting the Council's strategic priorities and integration of services. All current sites within Leisure facilities will be included. Joining an established trust would not give this option.

12.0 Financing the Vehicle

- 12.1 Whilst the Council will not be able to direct and control the Trust, it will continue to invest significantly (to be determined as part of the Business planning process) by way of payment for the management and the delivery of the services. There will need to be a detailed service specification that clearly outlines the required service levels and outcomes for local people from this significant spending. It must be noted that this specification will be flexible and renegotiated over time as will the payment to the Trust, both of which will reflect the changing outcomes required of the Trust by the Council

It is imperative that the Council maintains sufficient expert internal resource to manage the contract, ensuring the client/contactor role is maintained to ensure that:

- the Trust is meeting the required outputs within the service specification; and
- future negotiations around adding or removing services (including possible transfer to town and parish councils, schools or other local service providers) are properly facilitated

- 12.2 The Trust will be responsible for all operational aspects of the services and it will be up to its Board members to set fees and charges. The Trust must be financially viable and will be a commercial enterprise competing for business in what is a highly competitive market. Therefore, it is unlikely that the prices will increase much above inflation year on year, (but that cannot be guaranteed by the Council). But this, in turn, would enable the Trust to potentially have a flexible pricing policy that targets increased public participation in key areas.

- 12.3 As part of the detailed implementation of the Trust, further work is needed on exactly how the funding schedule will be managed, including performance penalties. The level of funding will need to be determined on an annual basis, prior to the anniversary of the formation the Trust, but this must take into account, in the early years of the Trust, the issue of ongoing sustainably, until it has become fully established. It is expected that, over a number of years, the subsidy required will become

less. It is essential that the Council does not provide grant aid to the Trust, as this could constitute state aid. Payment to the Trust must be commensurate with reasonable market payment to a third party to deliver management services.

- 12.4 There will need to be a considerable amount of work, prior to an agreed financial position being discussed with trustees, to ensure that the payment made to the Trust is in line with true actual spend on a site by site basis.
- 12.5 Further consideration needs to be given to the ongoing routine maintenance and capital repairs of the Leisure facilities, there may be significant financial savings for both the Trust and the council by CEC retaining the responsibility for these works- Further work is currently been under taken to confirm this and will be reported back to Cabinet in October.
- 12.6 There will need to be a clearly defined scoping exercise around the transition to new financial and monitoring systems for the Trust. This will be a key issue in terms of the work currently undertaken by the Council's corporate core, which will be subject to the new Finance and HR single legal entity arrangements.

13.0 Access to Information

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