

# Environment, Development and Transport Committee

<b>Report title:</b>	<b>Commercialisation of Highways Services</b>
<b>Date of meeting:</b>	<b>7 September 2018</b>
<b>Responsible Chief Officer:</b>	<b>Tom McCabe - Executive Director, Community and Environmental Services</b>
<b>Strategic impact</b> In September 2016, EDT Committee received a report detailing eight alternative service models which offered the potential to create opportunities to expand to other markets on a commercial basis - and so reduce the net cost of delivering the Highways Service.	

## Executive summary

A Strategic Review of EDT services in 2016 recognised that highways generates income through selling of services externally. It also noted that there were additional commercial opportunities associated with this. Members commissioned further work so that the opportunities could be better understood, and a more detailed report on outline options was considered by the Committee in late 2016.

The highways service is locally delivered and has a strong brand and reputation, particularly with Members and communities (parish and town councils). It is important that whatever model is put in place, it offers the best service to communities and best value for the County Council.

Significant work has been carried out looking in detail at a range of potential options for commercialisation. The services that have been considered are: Highway works (the in-house routine maintenance service including emergency works and Winter Service (gritting); Highways Laboratory (an in-house highways laboratory service); CES Fleet Services (our vehicle fleet unit based in Hethersett) and Fast Lane Training Services (a small training unit who provide highways training).

This work has identified alternative approaches:-

- A more efficient in-house delivery model
- An arm's length company approach

The conclusion of the work carried out is that an arm's length company approach would provide the greatest opportunity and benefit to the County Council. This would deliver an ongoing saving in excess of £0.5m per annum, with no reduction in quality. As such, an agreement with the NORSE group is recommended.

### Recommendation:

- 1. Consider the opportunities, benefits and risks outlined in this paper and agree a way forward.**

## **1. Proposal**

- 1.1. EDT Committee have previously considered a report on opportunities to increase commercial activity for the highways service. This followed on from a strategic review of all the services reporting to EDT Committee, which had been overseen by a Member Working Group
- 1.2. In previous years, Members had been clear that they wished to retain routine highway maintenance activities (in particular our roadworker workforce - the Highway Rangers) in-house as the service was providing an effective service and demonstrating locality working.
- 1.3. Since that time, highways services have continued to seek opportunities to generate income, and the volume of work delivered for external third parties on a commercial basis has increased. The Committee received a report in September 2016 about business models. Given the context of the Council's overall budget gap and ambition to commercialise and generate more income, the Committee asked officers to explore business model options in detail with a view to developing a business case to enable a more commercial approach.

## **2. Scoping**

- 2.1. Significant work has subsequently been carried out to assess potential opportunities in the market and develop a proposal.
- 2.2. One workstream has looked closely at which highways services offer the most potential in terms of a more commercial approach. The following have been identified on the basis that they already operate on a significant commercial basis and there is appetite in the market for these services, both in Norfolk and other areas. They are essentially the blue collar elements of work:-
  - 2.2.1. Highway works – this is the in-house routine maintenance service carrying out a range of planned and emergency works across Norfolk, including Winter Service (gritting). More commonly known as the Highway Ranger service, there are around 125 roadworkers, along with relevant management and support staff. They are also empowered to carry out essential work that they identify while out and about, without the need to check back with the office. In addition, they undertake a significant range of individual construction projects within the county.

The Client function will remain within Norfolk County Council and will continue to report via management to Elected Members. Client staff based in highway area offices are the first point of contact for local engagement and include Highway Engineers, Area Managers and Highway Inspectors. They will continue to identify work requirements, through the current inspection function, retain customer, Parish Council and Member liaison and deal with enquiries. Also, the responsibility for the supervision, quality and health and safety auditing of works delivery will remain with the Client team.
  - 2.2.2. Highways Laboratory – we are one of a small number (around 10) local authorities that has an in-house specialist highways laboratory service. The Laboratory is nationally recognised and has significant credibility in the market. Although we do not actively advertise our services, around 60% (circa £1m) of our work is from external sources, and we have scaled up to deliver this (currently 27 ftes).
  - 2.2.3. CES Fleet Services – our vehicle fleet unit with some 15 ftes based in Hethersett. Over the last year we have developed a joint fleet service with highways and Norfolk Fire and Rescue Service, and the vehicle fleet maintained includes fire appliances (and associated equipment) and our winter gritting fleet. Day fleet (e.g. vehicles used during the day by roadworkers) is currently

provided by an external contractor as this provides the best value.

- 2.2.4. Fast Lane Training Services – this is a small training unit (2 ftes) who provide bespoke training to Highway works, and others e.g. regional contractors, utilities and other local authorities.
- 2.3. There are other highway services that may be suitable to commercialise further in the future (for example the highway design service) but the four identified above provide the best initial opportunities. This is based on our current experience in the market and appetite in the market (based on discussions with external providers, including NORSE).

### **3. Delivery Models**

- 3.1. The EDT Committee considered 8 specific service delivery options in September 2016. Detailed consideration was given to these, and the options were narrowed down to two which offered the best potential:

#### **3.2. Option A – a more efficient in-house model**

- 3.2.1. A number of efficiency improvements have been made to the service in recent years. These include providing our roadworkers with electronic devices so that they can access the information they need remotely and log issues on site using gps locations (we are one of a few authorities who have successfully done this) and installed trackers on vehicles to enable better route optimisation and work tracking.
- 3.2.2. There is still more that could be done to improve efficiency, and we need to balance between investment and return e.g. bespoke ICT systems can be costly and resource intensive to implement. We are aligned with the Commercialisation workstream within the Norfolk Futures programme which has identified opportunities to enable trading services to operate more commercially.
- 3.2.3. Based on our understanding of our business and from discussions with existing providers we have identified a number of improvements. IT improvements would include:
  - Job costing – allowing labour, plant and materials to be attributed accurately to each job ordered, thus providing an accurate picture of costs per job. This, in turn will facilitate wider review, analysis, and discussion around how to further improve the service and deliver additional cost-saving efficiencies.
  - Dynamic scheduling – building upon the existing use of mobile technology by NCC, this would allocate work to gangs / operatives in real time. To do this, the system will identify the gangs / operatives with the necessary skill sets, closest to the location to each job (whilst also taking the priority of each job in to account).
  - Use of improved and more powerful mobile devices able to run this software
  - Business analytic resource which would provide day to day admin for the work scheduling/optimising software and reporting and management information on operational and financial performance.
- 3.2.4. As part of our options analysis we have reviewed the financial transactions of the service and tested the validity of our existing model and the assumptions behind the NORSE business plan. It is clear that the IT and works scheduling improvements would need both capital and ongoing revenue investment. NORSE would benefit from having existing expertise and systems that they would utilise, but these would still require additional annual costs of some £130,000. If we were to deliver an in-house service we would incur at least these costs and an estimated one off cost in order of £250,000 to access the necessary systems.
- 3.2.5. A challenge for any in-house model is how they compare with external

organisations in the way that we manage performance and reward; operate sickness absence management; adjust employment conditions and salaries to reflect market conditions; and streamline HR, finance and other back office functions to reflect commercial best practice. A range of changes would be necessary for us to match the costs and focus of a commercial organisation.

- 3.2.6. In the in-house model, the County Council remains in total control of the service, but also retains all the associated risks. There are also legal limitations including that 80% of our turnover must be with the County Council.

### 3.3. **Option B – an arm's length company approach**

- 3.3.1. There are a number of different models for an arm's length company approach, from setting up a new company, utilising existing companies or working with other authorities. One key element of this type of approach is the share of risk, both service delivery risk and commercial risk.
- 3.3.2. An arm's length company would have commercial freedom and can decide how it best operates to meet the commercial aspirations of its shareholders.
- 3.3.3. We have explored a number of potential avenues for this, including discussions with CORMAC Contracting Ltd (a company wholly owned by Cornwall County Council who provide highway services for a number of authorities) and NORSE Group.
- 3.3.4. NORSE have an aspiration to expand their public sector offer into the highways services market, and have proposed setting up a Partnership arrangement with the County Council. This would mean setting up a trading arm within NORSE and transferring the services to be carried out under the NORSE umbrella, underpinned by a Service Level Agreement (SLA).
- 3.3.5. There are a number of particular benefits from this approach with NORSE:
- Profit made from the Highways arrangement will be returned to NCC as part of our ownership of the NORSE Group. This will also include profit from any highways operation developed outside Norfolk.
  - A SLA would be developed between NCC and NORSE that would set out the level of service that is required by the Council, detailing:
    - the quality standard and specification, including metrics to demonstrate satisfactory delivery and details of any corrective action and redress if required;
    - the value of net saving that will be guaranteed annually and confirmation that this would be underwritten by NORSE. This profile is illustrated as per the table in paragraph 5.2.
    - Working arrangements and expectations between the NCC client function and NORSE Highways.
  - NORSE already have a significant number of contracts with many local authorities and so have a broad range of contacts and relationships in place. This geographic footprint provides the springboard to expand outside Norfolk.
  - Through such an arrangement NORSE will be able to access the technical and professional highways skills and experience, which they do not currently have within their business. Conversely, the highways service will be able to access the more commercial resource, systems, processes, marketing/branding and client contacts from NORSE, which we do not currently have access to.
  - There is scope to achieve additional efficiencies from the service, e.g. by being able to tap into the buying power of a large commercial entity and

streamlined management arrangements.

- Expanding the highways service into other areas of the country should help to make the Norfolk service more resilient. If we are able to increase volumes of work, there is scope to increase the number of specialist posts. There is also a challenge each year in securing sufficient resource for winter maintenance, and NORSE will enable access to a greater pool of this resource.
- It enables the County Council to focus on being a strong client. The County Council would continue to be in control of the service through commissioning and monitoring. The County Council would continue to hold the budget and if there is an underspend then the County Council would hold this.
- The NORSE Group is owned by the County Council, and so benefits via annual dividends from NORSE.

#### **4. The recommended option**

- 4.1. Based on the detailed work carried out, the option that it is considered will provide the greatest opportunities and benefits to the County Council is an arm's length company approach, under the NORSE umbrella. This also has the potential to offer increased job security and opportunities to existing staff.
- 4.2. During the last 8 months, officers have been working with staff from NORSE to develop a business case and to quantify the benefits from such a model. This level of analysis has provided NORSE with the confidence to underwrite the savings in excess of £0.5m per annum set out below.
- 4.3. It is recommended that we further progress the model with NORSE as the preferred approach, offering the benefits as per the detailed full business case, with a view to implementing the new model from 1 April 2019 (or as soon as possible after this date). Given the commercial nature of the business case, this document will remain confidential and not made public, but it has been included as an exempt item on the agenda for this meeting.
- 4.4. The establishment of a new trading entity within NORSE will require the approval of the Policy and Resources Committee, as would appointment of Directors to any associated Board. The Executive Director of Finance and Commercial Services would need to take a report to Policy and Resources Committee on these matters as necessary.

#### **5. Financial Implications**

- 5.1. There will be costs associated with setting up a new arrangement with NORSE, and these have been assessed within the business case.
- 5.2. It is anticipated that the proposal with NORSE will provide a range of savings. Assuming an implementation date of 1 April 2019, there are some savings that can be delivered from 2019/20. A net total annual (and ongoing) saving of over £500,000 is anticipated from 2022/23, with savings offered in the years preceding that as detailed below:

All values are at FY17/18

	Yr1 FY19/20	Yr2 FY20/21	Yr3 FY21/22	Yr4 FY22/23	Yr5 FY23/24
£K					
Business Analysis	88	88	88	88	88
Operational IT Systems	41	41	41	41	41
Gross Operational Efficiencies	-209	-370	-520	-640	-640
<b>Net Saving</b>	<b>- 80</b>	<b>-241</b>	<b>-391</b>	<b>-511</b>	<b>-511</b>

Operational Efficiencies identified by Norse comprise more efficient use of subcontractors and hired plant in operational areas, improved rates for casual staff, better works scheduling (enabled by the investment in improved IT systems) and improved working processes. These savings have been offset by the investment required which is also detailed in the table.

These savings would be guaranteed, and any dividend from the trading organisation will be over and above these figures.

- 5.3. Existing staff working in these services would be eligible to transfer to the new body under TUPE arrangements. There will be associated pension liabilities that are currently being worked through.
- 5.4. The only transfer of assets to NORSE under the proposed arrangements would be the operational small plant and tools and vehicles ('day fleet') needed for the daily operation of the highways services together with a limited volume of materials held as stock. All gritting vehicles (and winter grit) will remain the property of NCC. This will enable us to retain the flexibility and control to procure and deploy as required (although the gritting service would be delivered by NORSE operatives). All Fire and Rescue appliances and associated equipment will also continue to be the property of the County Council.
- 5.5. Property to be occupied by NORSE to enable the delivery of the services (ie highways depots and the laboratory) will be leased to NORSE at market rates. At the end of the partnership arrangements, the equivalent assets to those transferred will be returned to NCC in a comparable condition as at the start of the relationship.

## **6. Issues and risks**

- 6.1. One of the most valuable elements of the existing highways service is that it can be flexible to respond to changing needs and priorities. It will be important to ensure that any new arrangement recognises the need to continue to deliver a flexible and responsive service. We need to agree an approach that retains the ethos of public service going forward, delivering good quality work, on time, to local communities. Any arrangement would need to have a focus on working collaboratively to deliver services and not creating an unhelpful adversarial contract that could create additional work to resolve issues.
- 6.2. In addition, there will be a need to ensure that any arrangements for Fire and Rescue Fleet are appropriate and the client function for this element of service will be from within Fire and Rescue to ensure there can be strong oversight. There will be a specific service specification to set out the arrangements for Fire and Rescue to ensure that their requirements can be understood and delivered.
- 6.3. NORSE have a number of Joint Venture/Partnership arrangements in place and have a tried and tested approach to the structure and governance of these that would enable us to demonstrate Teckal compliance. This is important as it means that we could commission work directly from NORSE without the need to go through a procurement exercise in the market, should we wish to do so.
- 6.4. It will be necessary under the Teckal compliance to demonstrate that there will be no financial support from NCC. We will ensure that NORSE does not benefit from a subsidised service when competing with other providers for 3<sup>rd</sup> party work.
- 6.5. We also need to ensure that any arrangement is beneficial for the County Council and does not present a risk that the service cost would increase. The development of the SLA that will underpin the relationship will consider this risk and others identified during the process.

## Officer Contact

If you have any questions about matters contained in this paper or want to see copies of any assessments, eg equality impact assessment, please get in touch with:

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