

CABINET ITEM COVERING SHEET PROFORMA

AGENDA ITEM 6

REPORT TO CABINET

27 NOVEMBER 2013

**REPORT OF CORPORATE
MANAGEMENT TEAM**

CABINET DECISION

Children and Young People – Lead Cabinet Member – Councillor Anne McCoy
Corporate Management and Finance – Lead Cabinet Member – Councillor David Harrington

EMPLOYEE MUTUALISATION - STOCKTON ICT UNIT (SICTU)

1. Summary

The Stockton ICT Unit (SICTU) is an in-house ICT support service for schools. It comprises 20 FTE staff and had a 2012/13 outturn expenditure of £2,827,876. Earlier this year the SICTU Service Manager, with the support of staff within the team put forward a proposal for the 'spin-out' of SICTU as an employee mutual. Management agreed that SICTU should set out their proposal in the form of an Outline Business Case.

The Outline Business Case was presented to the Children's Programme Board on 10 June 2013 for consideration. It set out the strategic case for employee mutualisation and an option appraisal which included three options:

1. Continue with in-house service provision;
2. Close the in-house service and facilitate outsourcing;
3. Public service mutualisation (recommended as preferred option).

It was agreed by the Children's Programme Board that the preferred option was public service mutualisation, subject to further work on a detailed Business Plan. The Business Plan was subsequently developed, working closely with nominated representatives from the Legal, Finance and HR teams.

The Business Plan was presented to the Children's Programme Board on 26 September 2013. It set out the work that had been undertaken in developing the plan including detailed unit costing and pricing of services, the proposed base budget, and growth, pricing and expenditure plans. This work culminated in a three year Profit and Loss Forecast and cash flow forecast. The Business Plan also set out transfer proposals, including proposals for assets, liabilities and staffing.

In summary, the detailed work on the Business Plan, including the three year Profit & Loss Forecasts and cash flow plans, demonstrated that the mutual is a viable proposition generating healthy surpluses which will be re-invested for social purpose and securing the continued provision of the service for schools.

It is important to note that the financial growth as set out in the Business Plan is on the basis that SICTU is a public service mutual that has the scope to secure significant growth outside of the Borough, the flexibility to be fleet of foot in responding to customers, and

develops a cost base that is in a position to continue to remain competitive within the marketplace.

The Business Case for mutualisation, together with the Business Plan was presented to the Corporate Management Team (CMT) on 21 October 2013. CMT approved the recommendation to progress with mutualisation, which would be subject to a legal agreement and Cabinet endorsement.

2. Recommendation

Cabinet is asked to note the proposal for the employee mutualisation of SICTU and endorse the decision to progress with implementation, subject to a final report and sign-off by the Lead Cabinet Members for Children & Young People and Corporate Management and Finance.

3. Reasons for the Recommendation/Decision

The employee mutualisation of SICTU will secure the future of the service and realise a number of benefits including:

- The ability to capitalise on growth opportunities and meet the changing customer base
- Mitigate future financial risks and bring wider resource benefits to the Council
- Provide the opportunity for local economic benefits and job creation
- Capitalise on the entrepreneurial vision of the staff
- Improve the ability to be flexible in meeting customer needs
- A social purpose entity with re-investment into the community
- Support current policy on opportunities for employee led mutualisation

4. Members' Interests

Members (including co-opted Members) should consider whether they have a personal interest in any item, as defined in **paragraphs 9 and 11** of the Council's code of conduct and, if so, declare the existence and nature of that interest in accordance with and/or taking account of **paragraphs 12 - 17** of the code.

Where a Member regards him/herself as having a personal interest, as described in **paragraph 16** of the code, in any business of the Council he/she must then, **in accordance with paragraph 18** of the code, consider whether that interest is one which a member of the public, with knowledge of the relevant facts, would reasonably regard as so significant that it is likely to prejudice the Member's judgement of the public interest and the business:-

- affects the members financial position or the financial position of a person or body described in **paragraph 17** of the code, or
- relates to the determining of any approval, consent, licence, permission or registration in relation to the member or any person or body described in **paragraph 17** of the code.

A Member with a personal interest, as described in **paragraph 18** of the code, may attend the meeting but must not take part in the consideration and voting upon the relevant item of

business. However, a member with such an interest may make representations, answer questions or give evidence relating to that business before the business is considered or voted on, provided the public are also allowed to attend the meeting for the same purpose whether under a statutory right or otherwise (**paragraph 19** of the code)

Members may participate in any discussion and vote on a matter in which they have an interest, as described in **paragraph 18** of the code, where that interest relates to functions of the Council detailed in **paragraph 20** of the code.

Disclosable Pecuniary Interests

It is a criminal offence for a member to participate in any discussion or vote on a matter in which he/she has a disclosable pecuniary interest (and where an appropriate dispensation has not been granted) **paragraph 21** of the code.

Members are required to comply with any procedural rule adopted by the Council which requires a member to leave the meeting room whilst the meeting is discussing a matter in which that member has a disclosable pecuniary interest (**paragraph 22** of the code)

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SUMMARY

The Stockton ICT Unit (SICTU) is an in-house ICT support service for schools. It comprises 20 FTE staff and had a 2012/13 outturn expenditure of £2,827,876. Earlier this year the SICTU Service Manager, with the support of staff within the team put forward a proposal for the 'spin-out' of SICTU as an employee mutual. Management agreed that SICTU should set out their proposal in the form of an Outline Business Case.

The Outline Business Case was presented to the Children's Programme Board on 10 June 2013 for consideration. It set out the strategic case for employee mutualisation and an option appraisal which included three options:

1. Continue with in-house service provision
2. Close the in-house service and facilitate outsourcing
3. Public service mutualisation (recommended as preferred option)

The benefits of the preferred option were summarised as:

- The ability to capitalise on growth opportunities and meet the changing customer base
- Mitigate future financial risks and bring wider resource benefits to the Council
- Provide the opportunity for local economic benefits and job creation
- Capitalise on the entrepreneurial vision of the staff
- Improve the ability to be flexible in meeting customer needs
- A social purpose entity with re-investment into the community
- Support current policy on opportunities for employee led mutualisation

It was agreed by the Children's Programme Board that the preferred option was public service mutualisation, subject to further work on a detailed Business Plan to demonstrate financial viability. The Business Plan was subsequently developed, working closely with nominated representatives from the Legal, Finance and HR teams.

The Business Plan was presented to the Children's Programme Board on 26 September 2013. It set out the work that had been undertaken in developing the plan including detailed unit costing and pricing of services, the proposed base budget, and growth, pricing and expenditure plans. This work culminated in a three year Profit and Loss Forecast and cash flow forecast. The Business Plan also set out transfer proposals, including proposals for assets, liabilities and staffing.

In summary, the detailed work on the Business Plan, including the three year Profit & Loss Forecasts and cash flow plans, demonstrated that the mutual is a viable proposition generating healthy surpluses which will be re-invested for social purpose and securing the continued provision of the service for schools.

It is important to note that the financial growth as set out in the Business Plan is on the basis that SICTU is a public service mutual that has the scope to secure significant growth outside of the Borough, the flexibility to be fleet of foot in responding to customers, and develops a cost base that is in a position to continue to remain competitive within the marketplace.

The Business Case for mutualisation, together with the Business Plan was presented to the Corporate Management Team (CMT) on 21 October 2013. CMT approved the recommendation to progress with mutualisation, which would be subject to a legal agreement and Cabinet endorsement.

RECOMMENDATION

Cabinet is asked to note the proposal for the employee mutualisation of SICTU and endorse the decision to progress with implementation, subject to a final report and sign-off by the Lead Cabinet Members for Children & Young People and Corporate Management and Finance.

DETAIL

1. The Stockton ICT Unit (SICTU) is an in-house ICT support service for schools. It comprises 20 FTE staff and had a 2012/13 outturn expenditure of £2,827,876. This expenditure was offset by income received directly from schools of £2,831,527. This income and expenditure represents a mix of service provision, broadband supply and equipment purchases. The net position for 2012/13 was a surplus of £3,651. SICTU does not operate as a trading account and the income and expenditure outlined above excludes corporate overhead costs. 70% of the income for service provision is generated from schools within the Borough, with the remaining 30% generated from schools out of borough. Services are provided to a mix of primary schools, secondary schools and academies.
2. The SICTU Service Manager, with the support of staff within the team has recently put forward a proposal for the 'spin-out' of SICTU as an employee mutual. It was agreed that SICTU should set out their proposal in the form of an Outline Business Case.

THE STRATEGIC CASE: DRIVERS FOR MUTUALISATION

3. There are a number of reasons as to why the proposal for SICTU to 'spin-out' as an employee mutual has emerged. These are outlined in this section, which aims to set out the strategic case for employee mutualisation and the drivers underpinning it.

CHANGING CUSTOMER BASE

4. In recent years the landscape in which ICT services are provided to schools has changed significantly. With greater autonomy over budgets schools now have the freedom to choose their service providers, including ICT. In addition, as more schools transfer to academy status, with even greater autonomy, the market for ICT services is becoming even more competitive.

5. As a consequence the traditional model of an in-house local authority service providing support exclusively to the schools within its geographical boundaries no longer applies. Local authority in-house services must now compete with external providers for business with each and every school, or in the case of some academies, consortiums of schools.
6. In response to this SICTU has sought to maintain and grow its customer base by expanding its customer base, both within the Borough through the new academies, and out of borough through a mix of primary, secondary and academies. This has been achieved largely through reputation and word of mouth rather than any targeted growth activities.
7. The key issue to consider is one of future viability and continued value for money. Critical mass and economies of scale are crucial if SICTU is to continue to provide a cost effective service. In a rapidly changing market the service will need to ensure that it remains competitive with other providers and continues to secure growth beyond its traditional geographical boundaries. SICTU believe that this will be best achieved through spin out to employee mutualisation.

OPPORTUNITIES FOR GROWTH

8. As outlined above, the market for schools ICT services is going through significant change. Whilst this presents potential threats to the existing customer base of SICTU, it also provides opportunities for growth. SICTU believe that they have the track record, reputation and expertise to capitalise on those growth opportunities, which will bring increased economies of scale and buying power for the benefit of customers.
9. Recognising that to be successful an employee mutual needs to remain financially viable, SICTU also believe that there are opportunities to grow in other market areas including the third and SME sectors. It is recognised that the service is positioned and has a transferable offer to any organisation that is too small for dedicated ICT support but large enough to be too complex to manage on a 'do-it-yourself' basis.
10. SICTU recognise that growth for growth sake is a meaningless objective, however, growth that increases buying power, brings greater economies of scale and potentially generates surplus that can be re-invested for social purpose has significant benefits for the existing customer base, i.e. the schools.

FINANCIAL BENEFITS TO THE COUNCIL

11. There are a number of potential benefits to the Council of employee mutualisation. A key benefit would be the removal of risk in terms of income generation to cover the service expenditure budget. As already outlined, the risk associated with income is increasing as the market segments and competition increases. In the longer term there is a risk that the Council will find itself subsidising a continued service to the Borough's schools if the customer base declines and economies of scale are reduced.
12. A further financial benefit relates to the fact that at present the Council is already subsidising the service as it does not operate on a trading account basis and income does not cover the cost of corporate overheads. This subsidisation applies to both schools in the Borough and out of borough and includes academies.
13. A third area of risk relates to the potential staffing liabilities. The potential redundancy costs for the service are in the region of £200k, with an additional £100k (approximate) in pension liabilities. With an appropriate legal agreement at transfer, the Council should be able to mitigate these risks for the future.

WIDER RESOURCE BENEFITS TO THE COUNCIL

14. The schools ICT service is non-statutory and does not need to be provided directly by the Council. Schools have the choice to procure the service from any provider of their choice. There are SLA's in place between SICTU and the individual schools, with no collaborative agreement in place. The service is not unique and there are providers in the market place capable of providing the service.
15. Spin-out of the service would transfer all responsibility for ICT services to schools and providers, and the Council would not need to be party to these arrangements in any way. This would free up management time to focus on the council's strategic relationship with schools and fulfilment of its statutory duties.

WIDER LOCAL ECONOMIC BENEFITS

16. It is intended that the employee mutual will be a Stockton-based entity, which will bring benefits to the local economy and if successful in its growth ambitions will create jobs.
17. Already employing 20 people full-time, all in professional and technical roles, spin-out as a local company could ensure that those employment opportunities remain local.

SOCIAL PURPOSE

18. Exploiting growth opportunities will enable investment in social purpose projects both within schools and their local communities and secure the continued re-investment in the service, developing new and innovative service offers for the benefit of schools and pupils, thereby keeping schools at the forefront of educational technology.

CAPITALISE ON ENTREPRENEURIAL VISION

19. The proposal for employee mutualisation comes from staff within the existing service. There is a genuine appetite to develop and grow the service, reaching beyond existing geographic boundaries and the schools sector.
20. Employee mutualisation is widely recognised as offering potential for greater staff commitment and motivation in pursuing continuous improvement, creativity and innovation, productivity, performance and value for money and customer focused service development and delivery.

ENABLE IMPROVED CUSTOMER FOCUS

21. As an employee mutual there is much greater scope for improved customer focus, enabling an operating environment that can be much more flexible, responsive, and fleet of foot in meeting the needs of customers.

ALIGN WITH CURRENT POLICY AGENDA

22. In May 2010 Prime Minister and Deputy Prime Minister, set out the Coalition Government's programme for Government. The programme set out radical plans for public service reform, including for a wide range of groups and organisations, such as mutuals, co-operatives, charities and social enterprises, to have much greater involvement in the running of public services.
23. The Minister of the Cabinet Office, built on this commitment in a speech later that year, where he set out his vision to empower public sector workers to release their 'entrepreneurial vigour' to take over the running of the services they provide, as part of opening up the delivery of public services beyond the traditional binary choice of public and

private. The Minister pointed out how ownership and control, through mutualisation, can empower employees to redesign services around users and communities freeing up their untapped entrepreneurial and innovative drive.

24. This was further reinforced through the publication of the White Paper Open Public Services, which positioned the role of mutuals at the heart of the Government's vision for public service reform. A key part of this is the replacement of top-down monopolies with open networks in which diverse and innovative providers compete to provide the best and most efficient services for the public. The role mutuals can play is clear. Instead of public services being run from a desk in Whitehall, mutuals are a way for entrepreneurial and committed public sector staff to take over the services they deliver.

OPTION APPRAISAL & PREFERRED OPTION

25. Within the context of the strategic case for SICTU mutualisation three options have been considered:

OPTION 1 - CONTINUE WITH IN-HOUSE SERVICE PROVISION

26. The option to retain the in-house ICT service does not necessarily mean that no change takes place. The key advantage of this option is that it would ensure continuity of service and little risk to future service delivery (assuming any income losses are underwritten by the Council and corporate overhead costs continue to subsidise the service).
27. Changes that could be considered include increasing charges to schools to ensure full cost recovery (i.e. to include corporate overhead costs) and explore potential for further efficiencies e.g. merge into Xentrall, the wider ICT shared service for the Council.
28. The main downside of this option is that many of the drivers and opportunities as set out in the strategic case for mutualisation may be lost, including:
- Growth opportunities and meeting the changing customer base – to ensure continued economies of scale the service will need to secure growth outside the geographic boundaries of the Borough and into new sectors. Whilst this may be possible under existing legal powers, it is arguable that there is no strategic case for the Council to be 'in the business' of ICT services.
 - Subject to appropriate transfer arrangements the mutual may provide scope for the mitigation of future financial liabilities associated with the service, for which a continued in-house provision would not.
 - Closure of the service at a future date may lead to a missed opportunity of mutualisation and securing local economic and employment benefits (assuming that in future services were provided by a company based outside the Borough).
 - As a non-statutory service, a subject to stakeholder support, the mutual would free up the management resource that is currently required to provide an in-house service.
 - The continuation of in-house provision would have an impact on the motivation of the existing team, which demonstrates a clear entrepreneurial vision to take forward the service as a successful mutualised entity.
 - As a stand-alone organisation, the mutual would have much greater ability to be fleet of foot in responding to customer needs, not constrained by the wider policies and processes that an in-house service is required to work within.

OPTION 2 - CLOSE IN-HOUSE SERVICE AND FACILITATE OUTSOURCING

29. In many ways mutualisation is very similar to the facilitation of outsourcing. As outlined earlier, the procurement and contractual arrangements are between the schools and provider. Therefore, it would be inappropriate for the Council to outsource the current in-house service, however, if it was to discontinue with in-house provision it could facilitate and support the schools to procure from an alternative providers e.g. through helping establish a schools procurement club for ICT services.
30. The benefits and risks of this option are very similar to the mutualisation option, growth opportunities and the meeting the changing customer base, scope for the mitigation of future financial liabilities associated with the service, free up the management resource that is currently required to provide an in-house service, greater ability to be fleet of foot in responding to customer needs. In addition, it may have advantage over the mutualisation option, in that there is scope to access private sector expertise and investment capability.
31. However, there may be a number of disadvantages of pursuing this option, in comparison to mutualisation.
- Closing the existing service and facilitating outsourcing will have TUPE implications and which may be further complicated by staffing issues arising from opposition to outsourcing and a strong desire to 'go it alone'.
 - Closure of the service may lead to a missed opportunity of mutualisation and securing local economic and employment benefits (assuming a future service was provided by a company based outside the Borough).
 - If the service is outsourced to a private sector provider the opportunities for social purpose and the re-investment of services as offered by the employee mutual would be missed.
 - In addition, SICTU have presented anecdotal evidence that the schools would not welcome this option. They are very happy with the current service and a number have come to SICTU following poor experience with private sector providers.

OPTION 3 - PUBLIC SERVICE MUTUALISATION

32. The strategic case for mutualisation is as set out in paragraphs 3 to 24, summarised as:
- The ability to capitalise on growth opportunities and meet the changing customer base
 - Mitigate future financial risks and bring wider resource benefits to the Council
 - Provide the opportunity for local economic benefits and job creation
 - Capitalise on the entrepreneurial vision of the staff
 - Improve the ability to be flexible in meeting customer needs
 - A social purpose entity with re-investment into the community
 - Support current policy on opportunities for employee led mutualisation

PREFERRED OPTION

33. Based upon the strategic case for mutualisation and consideration of the options the preferred option is public service mutualisation.

THE BUSINESS PLAN

34. It was agreed by the Children's Programme Board that the preferred option was public service mutualisation, subject to further work on a detailed Business Plan. The Business Plan was subsequently developed, working closely with nominated representatives from the Legal, Finance and HR teams.
35. The Business Plan was presented to the Children's Programme Board on 26 September 2013. It set out the work that had been undertaken in developing the plan including detailed unit costing and pricing of services, the proposed base budget, and growth, pricing and expenditure plans. This work culminated in a three year Profit and Loss Forecast and cash flow forecast. The Business Plan also set out transfer proposals, including proposals for assets, liabilities and staffing.
36. The key assumptions built in to the Business Plan included:
- All staff would transfer to the mutual under TUPE arrangements with existing terms and conditions;
 - Income growth is forecast for each of the first three years 2014/15 to 2016/17;
 - Prices will be revised on an annual basis in line with CPI;
 - Supplies and services expenditure have been adjusted for inflation using CPI;
 - Following transfer the mutual plans to introduce a Performance Related Pay scheme that is linked to the financial performance of the company, with spot salaries and non-consolidated bonus payments. Therefore, the Business Plan does not include any salary cost increases, as they will only be paid from surplus if appropriate;
 - Subject to an actuary report, it is planned that the mutual will apply to be an admitted body under the LGPS, if this is not possible a comparable alternative will be introduced for pension arrangements;
 - It is planned that any financial surplus will be utilised as follows:
 - Pay back SBC loans and build up appropriate level of working capital / contingency fund to ensure continued financial stability
 - Contribute to the operation of an appropriate performance related pay scheme
 - Re-invest in the service, developing new and innovative service offers for the benefit of schools and pupils
 - Invest in social purpose projects both in schools and the communities within which they work
 - Assets (mainly IT hardware) will be purchased by the mutual at current market value through the provision of a loan from the Council;
 - Minimal start-up costs will be incurred by the mutual through the provision of a loan from the Council;

- Although the cash flow forecasting is positive it has been agreed that it would be prudent for the mutual to have some contingent working capital, therefore the Council will also provide a loan for this purpose;
 - All loans will be fully repayable by the mutual and will charge an appropriate interest rate.
37. In summary, the detailed work on the Business Plan, including the three year Profit & Loss Forecasts and cash flow plans, demonstrate that the mutual is a viable proposition generating healthy surpluses which will be re-invested for social purpose and securing the continued provision of the service for schools.
38. It is important to note that the financial growth as set out in the Business Plan is on the basis that SICTU is a public service mutual that has the scope to secure significant growth outside of the Borough, the flexibility to be fleet of foot in responding to customers, and develops a cost base that is in a position to continue to remain competitive within the marketplace.

IMPLEMENTATION

39. Subject to final approval, it is planned to 'go-live' with the mutual on 1 April 2014. A draft Implementation Plan is currently being prepared which includes the following key tasks:
- Create the legal structure for the entity and establish its governance arrangements. External legal advice is required for this and the costs will be met by the mutual itself, through the start-up costs loan;
 - Prepare and agree the Transfer Agreement between the Council and the Mutual. The Transfer Agreement will deal with all aspects of transfer including assets, liabilities and contract novation's;
 - Put in place the loan agreements for the purchase of assets, start-up costs and working capital;
 - Undertake staff consultation and arrange for TUPE transfer of staff;
 - Consult with customers on the plans for mutualisation;
 - Ensure operational readiness for the 'go-live' date including accommodation, IT hardware set-up and business administration systems (e.g. invoicing, bookkeeping, payroll, etc).

FINANCIAL IMPLICATIONS

40. The financial implications of the proposal relate to the loans to be provided to the mutual, which will be charged at an appropriate level of interest and are fully repayable by the mutual. The Business Plan demonstrates that the mutual will be in a position to repay these loans within its first three years of operation.

LEGAL IMPLICATIONS

41. The relevant legal issues and implications are that the mutual will need to be established as a legal entity and that the Council will enter into a Transfer Agreement with the mutual to enable the legal transfer of assets and liabilities.

RISK ASSESSMENT

42. This employee mutualisation is categorised as low to medium risk. Existing management systems and daily routine activities are sufficient to control and reduce risk.

SUSTAINABLE COMMUNITY STRATEGY IMPLICATIONS

43. The mutualisation of SICTU will contribute to key themes of the Sustainable Community Strategy, including:
44. Children and Young People - by helping provide real opportunities to achieve their full potential and contribute to a fast moving, changing and interdependent world and access to excellent public services when they need them, which strive to meet the individual needs of children and young people and their families.
45. Economic Regeneration and Transport – and the ambition for a strong local economy with better jobs and improved employability
46. The social purpose approach of the mutual will also contribute to the Supporting Theme of Stronger Communities and the ambition for strong community involvement.

EQUALITIES IMPACT ASSESSMENT

47. This report is not subject to an Equality Impact Assessment because

CONSULTATION INCLUDING WARD/COUNCILLORS

48. Consultation with key stakeholders, particularly with Head Teachers, will be undertaken prior to mutualisation.

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Education related? Yes

Background Papers: None

Ward(s) and Ward Councillors: Not applicable

Property: SICTU is currently located in the Education Centre which Cabinet have previously agreed will be subject to change of purpose / disposal.