



Appendix 1

Environmental Services Re- provision Project

Commissioning Options Review

Report for Northampton Borough Council

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Report for Julie Seddon, Northampton Borough Council

Approved by



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Disclaimer

Eunomia Research & Consulting has taken due care in the preparation of this report to ensure that all facts and analysis presented are as accurate as possible within the scope of the project. However no guarantee is provided in respect of the information presented, and Eunomia Research & Consulting is not responsible for decisions or actions taken on the basis of the content of this report.

Executive Summary

Eunomia Research & Consulting (Eunomia) has been commissioned by Northampton Borough Council (the council) to support the following areas of the Environmental Services Re-provision Project. This is a project set up to identify the most suitable commissioning option for the future delivery of the council's environmental services and to subsequently implement the preferred commissioning option by June 2018 through:

- 1) providing project management functions;
- 2) supporting market research and community engagement activities;
- 3) undertaking a review of agreed commissioning options; and
- 4) advising the political and officer leadership group on the selection of the preferred commissioning option.

This report summarises the outcome of stages 3 and 4 above.

The importance of the engagement with senior officers and the political administration cannot be understated within the context of a commissioning options review project. Eunomia is a market leader in the review of commissioning options and the impartial and objective support is based on the use of models and tools developed over many years that have undergone continuous refinement and testing. However, the decision on commissioning options cannot become entirely focused on the modelling detail. Engagement with senior officers and the political administration is crucial to the success of such a project, so that the emerging evidence from the modelling can be tested and discussed at the right level. This also helps to ensure that the qualitative assessment and the operational and political issues with each option can be explored together.

Ultimately, the implementation of any new commissioning options will entail a major operational and cultural change for the council and decisions on the service commissioning route for universal front-line services as the environmental services are complex. The commissioning options modelling cannot identify a fundamentally 'best' option and is intended instead to serve as a decision-support framework to help members and senior officers arrive at the right and balanced decision for the council.

The council and Eunomia agreed that the following commissioning options would be considered and appraised as part of this project:

- Contracting out – going back to the market to conduct a new procurement exercise.
- Insourcing – bringing the services in-house to be delivered through a Direct Services Organisation (DSO) or similar.
- Local Authority Company (LAC) – delivering the services using a local authority owned company, either starting a new company or using an existing company founded by another authority.

Eunomia assessed the three commissioning options against two primary criteria:

- cost; and quality and risk.

Cost Modelling

Eunomia created detailed financial models so that each commissioning option could be compared based on variations in key cost components.

Financial pressure on the council, which is only likely to increase over the next few years, sets a key part of the context for decisions on future commissioning of environmental services. The main factors driving the results of the financial modelling relate to differences in assumptions on unit labour costs and corporate overheads and profit.

The key assumptions that drive the cost modelling are described below:

- Workforce pensions: the outsourced option pension costs are assumed to remain 'as is', whereas the in-house option is based on 100% enrolment in the LGPS. The LAC option is somewhere in between, albeit considerably closer to 'as is' than LGPS. In reality, enrolment rates may be different to those assumed. Pension policy for the LAC could also be set by the council and could be more or less generous than assumed. These assumptions drive a considerable proportion of the cost difference between the options.
- Corporate overhead and profit: assumptions here are estimates based on the kinds of target margin that the market aims to achieve, but are clearly somewhat speculative. In practice, the procurement process generates a wide range of results, with many recent contracts operating at lower margins.
- Productivity: all options are assumed to achieve the same underlying service delivery productivity. For labour intensive services such as these, variations in productivity can make a significant difference to service cost. Many believe that the private sector generally delivers greater productivity and that competitive procurement processes drive efficiency. There is no evidence from the market as a whole that one option generally delivers better value for money, so the 'no productivity difference' assumption avoids distortion of the financial model.

The results of the cost modelling show that:

- the LAC option delivers the lowest modelled cost solution for running the environmental services;
- the Contracting Out option delivers a modelled cost that is approximately £400k higher per year than the LAC; and
- the In-sourcing option delivers a modelled cost solution which is marginally higher than the Contracting Out option.

Another key conclusion of this step of the review is that all three commissioning options are likely to deliver a more expensive service than the current contract cost. Eunomia's approach to the development of the cost model was to build a bottom-up model of the service to reflect the current commission and this stage of the analysis concluded that the contractor is likely to be delivering the service at a significant loss, which is a confirmation of what the council already understands to be the case. Future commissions assume to cover the cost of the service (i.e. the loss is not carried forward into a future contract), and thus the service cost increases compared to the current contract.

Quality and Risk Assessment

The methodology used for the qualitative assessment of the commissioning options review is based on a risk assessment of criteria developed with officers and the Cabinet Advisory Group.

The quality and risk assessment concludes that:

- the Contracting Out option performs best in the risk assessment by some margin;
- the LAC option performs reasonably well in the risk assessment; and
- the In-sourcing option performs worse than the other options in the risk assessment.

The rationale for the scoring achieved by the options is as follows:

- **Financial and Overspend:** For the contracted out option, the contractor bears overspend risks. Management in the in-house option may not be subject to the same commercial pressures to manage budgets and deliver profits, and in any event the council bears the overspend cost risk. For the LAC option, whilst the council still bears the overspend risk, the LAC management and commercial mind-set may be more likely to keep costs in check.
- **Flexibility and Service Change:** Service change in the contracted out option would involve contract negotiations, whereas in the other options, change would be easier to implement, although considerable flexibility can be built into contracts.
- **Performance:** The contracted out option may be more likely suffer poor performance since the council has less direct control over the delivery of the services and the contractor is motivated by profit as well as customer service.
- **Expertise acquisition:** The contracted out option would involve selecting a contractor with the relevant experience. For the in-house option it would be necessary to recruit highly experienced management which presents a risk; a LAC may be a somewhat more attractive proposition for experienced candidates.
- **Market conditions:** There is a risk of attracting few bidders and having low levels of competition in the contracted out option, but the LAC and in-house options be exposed to the labour market for key talented senior managers and be impacted by reduced buying power in the procurement of key service assets.
- **Best Value:** For the contracted out option, it is assumed that the competitive tender process would result in a contract price that demonstrably provides Best Value to the council through market testing, while the LAC and in-house options do not undergo a procurement process and are therefore less certain to represent best value.
- **Political Stakeholders:** based on soundings taken, it is assumed that the political stakeholders are neutral on all commissioning options and do not rule out any option.
- **Operational Risks:** The contractor largely bears operational risks in this option, but for the LAC and in-house options, operational risks are ultimately the responsibility of the council.

Emerging Commissioning Option

The two criteria of cost and quality and risk are subsequently combined into a single 'score' using the weighting agreed with senior officers and the Cabinet Advisory Group:

- cost – 40%; and
- quality and risk – 60%.

The application of the weighting determines the overall ranking presented in Table E - 1.

Table E - 1: Overall Results – Comparison of Options

Criterion	Cost	Quality and Risk	Total	Rank
LA Company	40	54	94	2
Contracted Out	39	60	99	1
In-house	38	51	89	3
Notes:	<i>We applied a normalisation to the scores achieved by each option on the basis of a deviation from the lowest scoring option, so that the lowest modelled cost option achieves 40 points and the lowest risk scoring option achieves 60 points. The other options score points in proportion to the lowest scoring option.</i>			

Eunomia carried out a sensitivity test of the weighting agreed by considering a scenario where a 50/50 weighting is applied to cost and quality/risk and a scenario where the cost criteria is weighted more than the quality and risk criteria. The sensitivity test concluded that the ranking shown in Table E -1 is unchanged.

The commissioning options review concludes that the Contracting Out option delivers the 'best' result overall and could be selected by the council as the preferred commissioning solution. It must be stressed however that, taking into account the cost modelling results, the LAC option would also represent a viable solution for the council.

The selection of the Contracting Out option would also deliver the 'best' balance of benefits and risks to the council:

- A well understood solution with predictable implementation costs and timetable;
- The ability to transfer most of the financial risks to the selected contractor; and

The opportunity to attract competition during the procurement process to secure best value and to deliver an innovative contract.