Better together
Building a successful joint venture company
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Executive summary

Local government is continuing to innovate and change as it looks for ways to protect front line services. The changes are picking up pace as more local government bodies innovate by introducing alternative delivery models to generate additional income and save costs.

While these new models are not a solution by themselves they do add to the wider solutions being explored by local government such as devolution, collaboration and integration.

In September 2014 we published our first report on alternative delivery models (ADMs), ‘Responding to the challenge’, which examined a variety of models that local councils were looking at to tackle the financial challenges. Our next report ‘Spreading their wings: Building a successful local authority trading company’, published in April 2015, built on this by exploring the use of trading companies. This is the next report in the series and focuses on joint ventures (JVs) for service delivery.

JVs have been in use for many years in local government and remain a common means of delivering services differently. They offer the opportunity to deliver services with partners who, more often than not, bring something new to the table. Many of the JVs used by local government have been public-private collaborations, providing either front or back office services. While some have been successful, it is true to say that they have a mixed reputation, particularly where they have focused on the contractual aspects of the relationship rather than the partnership element.

There are well-publicised cautionary tales of public-private JVs that have attracted attention and debate; some have ended earlier than planned or have not delivered the intended benefits. While this can detract from their potential as a viable model, many councils are continuing to use this type of JV because they recognise that experienced commercial partners bring cost effective solutions. We agree with this, but only if the JV moves away from the traditional model of inflexible and complex contracts and both the council and its partners are clear on the objectives. Moving to a more collaborative JV partnership model can, if managed well, provide councils with the commercial edge over any of the ADMs we have looked at, including local authority companies.

There is also an emerging breed of JV in which councils partner with other public sector bodies or commercial companies that are wholly-owned by the public sector: public-public JVs. They offer the opportunity to benefit from scale and experience while being more closely aligned to public sector values.

Overall, JVs remain a viable ADM for local authorities. We have set out below our insight, based on our research, that councils may wish to take into account when setting up their own JVs.

Our research indicates that the number of JVs will continue to rise, in particular public-public partnerships as proven models are replicated. JVs offer great opportunities for savings and income generation and can make more sense in some circumstances than a LATC if the council feels it cannot operate alone.

If procured with enough innovation, creativity and collaboration in mind, they may also be capable of delivering more than just profit, such as wider community benefits. This will be important as more councils seek to identify social as well as financial returns.

Treading the line between contract management and partnership working may be a challenge, but the selection of partner and building of trust will be key. Our research has found that in many cases councils believe that they work better in a commercial setting when working in partnership, rather than operating alone. As one observer noted: “it is better to have 50% of something rather than 100% of nothing”.

Local government is continuing to innovate and change as it looks for ways to protect front line services. The changes are picking up pace as more local government bodies innovate by introducing alternative delivery models to generate additional income and save costs.
We have researched a range of JVs for this report to provide inspiring ideas from those that have been a success and lessons learnt from those that have encountered challenges. The report also provides information about the key areas to consider when:

- deciding to set up a JV
- setting it up
- making it successful.

Key messages

Public-private JVs can bring significant benefit

JVs continue to be a viable option. Where they have been successful they have supported councils to improve service delivery, reduce costs, bring investment and expertise and generate income. In our experience a JV can be the right model when a council does not think it can achieve its particular objectives alone, for example when it needs particular expertise or investment such as improvements to IT systems.

Successes include: CATERed, which has reduced costs for Plymouth City Council, and London Borough of Barnet’s JV (Regional Enterprise), which generates profits for the council. Similarly, Nottinghamshire County Council has chosen a JV model for its highways as it allowed retention of control within the public sector and the future sustainability of the service. So there are some clear reasons to be optimistic about the future of JVs.

But not all public-private JVs have been successful

There is also reason to be cautious. Our research found a number of JVs between public and private bodies had mixed success in achieving outcomes for councils. In particular, JVs involving multiple back office services were prone to difficulties. Similarly, we have seen that JVs used in transformational programmes have not always delivered intended benefits. Success stories are more common in JVs that have a narrow remit – for example one service rather than a range of services – or focus on a front line service such as catering.

A key reason for failure is objectives lacking alignment, which is particularly prevalent in public to private JVs. This is primarily because the private sector partner’s primary focus is always profit, whereas the local authority often has a range of objectives. If councils are looking to set up a JV it should have a blended set of objectives covering income generation, service improvement, cost cutting, transfer of commercial skills and new investment. These need to be aligned to the objectives of its partner and included in the articles of association of the JV.

The cultural fit and responsiveness of the chosen partner are as important as any considerations about commerciality, as their omission can negate the opportunities that scale, expertise and investment bring.

Capita

The London Borough of Barnet has an outsourced contract with Capita for the delivery of some of its services but the two partners have also set up Regional Enterprise (Re), a JV for the development and regulatory services in the borough, to enable the council to benefit financially from the profits anticipated from the commercial opportunity that the partners have identified, as it has a 49% stake in the business and representation on the JV board.

We identified a number of JVs, set up to deliver services in a particular way, that hadn’t been responsive to the council’s changing agenda, objectives or circumstances. This had resulted in both sides reaching for the contract and the JV ultimately failing.

Usually, councils are the minority partner in these JVs. While this brings less risk it also brings less control and ability to influence the partnering company’s direction. An inflexible response from the majority shareholder can frustrate the council as it seeks to respond to financial pressures and lead to a significant deterioration in relationships between the partners.

There can be a blurring of the roles and responsibilities of the council in its different capacities as both traditional commissioner and strategic partner.
The correct governance architecture, beyond just the shareholding, is paramount. This should strike the right balance between taking sufficient control to ensure the council’s needs are met at a reasonable cost and allowing the partner the necessary freedom to act to achieve them, such as working in a partnership rather than solely enforcing a contractual model.

In setting up the JV, there needs to be an awareness that the JV will contract directly with the council to provide services. Our discussions indicated that contract development and negotiation were both complex and costly. When difficulties arose with performance, or changes were needed to the service, there was a tendency from both parties to ‘reach for the contract’. This inflexibility linked to the complexity of contracts often leads to disputes and misunderstandings and consequently makes the relationship more fragile and prone to break-up. The partnership element of the JV should have come into play significantly before this point.

“Don’t get confused with outsourcing – back office transactional services don’t lend themselves to joint ventures.”

Switzerland One

If the key driver is cost reduction then outsourcing or shared services may be a more appropriate model. Most transactional services lend themselves more easily to these models because they are easier to define and follow a simpler set of key performance indicators (KPIs) that can easily be measured. In contrast, JVs are more successful if cost savings are combined with a growth or income-generation objective.

Being a commercial partner to a public sector body is not always easy. The commercial partner will need to make a profit to satisfy shareholders and will want to maintain commercial confidentiality. As the council is both a partner and a purchaser of services this can create tensions.

In reality, there will always be an uneasy tension for councils in a JV that is pursuing a profit margin as well as providing services back to the council under contract. This issue needs to be managed from the beginning of the JV by aligning objectives and ensuring partnership working is supported by the appropriate governance. While there needs to be sufficient governance to protect the council and the public interest, this should be balanced with sufficient commerciality to drive improvement, additional income and cost reduction. For many public to private JVs this has been a difficult line to walk.

Civica

The three South Worcestershire districts’ outsourced contract with Civica has enabled benefits to be realised more quickly than any other model, according to their business case. It enables the three authorities to achieve bonuses when more contracts are signed, giving them some of the benefits of a JV through a contract with a private sector provider rather than a separate company model.
Public-public JVs are a new breed
Our research has demonstrated that public-public JVs can be more successful at working and staying together. In part this is as a result of combining common cultures, but in many instances councils already have good collaborative relationships. In our experience there is also less tension for councils as a partner in a profit-making public-public JV, as ultimately all profits are returned to the public purse.

The Coventry and Solihull Waste Disposal Company is a good example: it was established in 1992 and continues to operate with both councils achieving their respective objectives. Key success factors are the flexibility and joint working developed by the partners, alongside shared objectives that effectively combine service delivery and have a wider focus than simply profit making.

However, while two councils may collaborate well together they do not always have the commercial expertise of a private sector organisation and may not realise all the economic benefits that a more commercial operator would bring. In reality there is often a trade-off between collaboration and profit.

"Creating the right environment for maintaining the alignment of strategic objectives and exploring how the venture can maximise benefits to all parties was important."

Coventry Metropolitan Borough Council

This new breed of public-public JV, in which councils partner with wholly-owned companies of other councils, is becoming increasingly popular. For example, Cormac (a wholly-owned company of Cornwall Council) is about to embark on a JV with Nottinghamshire County Council to deliver its highways service. This will be the first JV for Cormac. Norse (the wholly-owned company of Norfolk County Council) also operates this model. This type of JV provides the opportunity for councils to partner with companies that bring both the scale economies and expertise, combined with the public sector ethos.

We are seeing that as these companies grow, they are seeking out opportunities to partner, and there are several discussions currently underway. However, these JVs are relatively new and it remains to be seen how successful they will become in the longer-term.
Key success factors

Taking the following into account will help to ensure the success of a JV:

**Deciding to set up a JV**
- **Be clear on your objectives.** The market will need clear information about the council’s requirements to enable it to respond in a meaningful way.
- **Be ambitious.** If you are setting up a JV then you need to have clear objectives around income growth, cost savings and value to the community such as job growth. If all you want to do is deliver savings then consider whether outsourcing would be better.
- **Be ready to work in partnership.** This is not simply a contract, it is a partnership and needs to be viewed as such by both sides if it is to be successful.
- **Carry out due diligence.** The council needs to properly understand the existing services, their associated financial costs and where the opportunities are for growth or cost savings.
- **Obtain professional advice and support.** For most councils this will be their first JV. There are issues that will need to be dealt with including state aid, management, people and pensions. Advice and support early on will avoid costly mistakes in later stages.

**Setting up the JV**
- **Ensure that the procurement process is effective.** Time needs to be taken during the procurement process to test the partnering arrangements and to ensure any evaluation criteria are aligned to the objectives set for the JV. Councils need to be confident that the procurement process is capable of delivering the right JV partner.
- **Revisit the objectives with your partner.** All parties need to be clear on what they want to achieve with a clear vision of the future and how they will grow and adapt together.
- **Share profits and risk.** It should not be possible for one party to benefit at the loss of the other partner. For example, excess profit clauses or the requirement to share the costs of redundancy or service reduction should be built into the agreement.
- **Anticipate future changes.** The environment in which the JV works will change. Mechanisms need to be put in place to address future tensions; not just formal dispute processes, but also regular meetings and guiding principles for how to expect to manage the relationship and allow it to evolve in time.
- **Build flexibility into contracts and articles of association and performance monitoring arrangements.** Councils seeking increased efficiencies put additional pressure on joint arrangements. This has been particularly evident with private sector partners where the contract has not allowed sufficient provision for such changes.

**Making the JV successful**
- **Create a culture of trust and strong working relationships.** There should be a ‘one team’ ethos between the council and the JV and an understanding of the importance of communication across all stakeholders. In our experience, silences are filled with questions and uncertainties misinterpreted as significant risks. Communicating clearly is key and having all stakeholders on board can be critical to success.
- **Focus on the key outcomes.** If the objectives are income generation, improved service performance and cost reduction, ensure that scrutiny is held at this level and does not fall into an assessment of inputs or performance indicators.
- **Allow the JV to operate independently.** The JV must be able to operate outside of the council, focusing on income growth alongside improved service delivery and cost reduction for the council. The temptation to make the JV another corporate directorate that acts in the same way as others needs to be resisted.
- **Ensure appropriate corporate structure and governance arrangements.** The JV’s corporate structures should allow it to operate in a commercial manner with non-partners and in a partnership manner with the council. From a council’s point of view it should have the necessary oversight and arrangements in place to identify risks in the JV and to ensure performance remains high, but without having to revert to the contract.
- **Take into consideration the local politics.** Political administrations change from time to time, so having all political parties in agreement that the JV is the right thing to do will provide stability for the future.
- **Get the right level of performance management.** Councils will need to think clearly about what they want to measure. The performance arrangements will inevitably drive the behaviour and priorities of the JV, so they need to be closely aligned with what it is hoping to achieve.
- **Planning the exit.** There are a number of reasons that a partner may choose to exit from a JV. Whatever the reasons, the closure process is complex and can damage services and relationships. Clarity is needed from the outset regarding how and under what circumstances the venture will come to end.
Deciding to set up a JV

What is a JV and why would you create one?
JVs comprise a range of different commercial structures that involve two or more partners. In local government they are usually formed either for a specific project, or for the ongoing delivery of council services; we focus on the latter in this report. Some of them also enable business and services to be added to the portfolio of the JV over time in accordance with pre-agreed mechanisms within the contract.

Our research has covered JVs delivering a range of council services, both back office and front line services, all at different stages in their lifecycle; from those starting up to those coming to an end as their objectives are met or they no longer meet the business needs in a changing environment. The most common services provided through a JV are set out below.

JVs can be beneficial. But there are many examples, often high profile, where they have not achieved their intended outcomes. This has caused other councils to be wary of choosing this option. It can be challenging to strike the right balance between contract management and partnership working to ensure that the council’s objectives are not compromised. Typically, councils have a minority shareholding in JVs which can make it more difficult to challenge the other partner.

“The joint venture route has to be the right business thing to do, rather than the best compromise between outsourcing and a LATC.”
Southwest One

Most common services provided through a JV

- IT
- Human resources
- Payroll
- Finance
- Road repairs and maintenance
- Revenues and benefits
- Property management
- Schools catering
Structures for the JV
There are several models available (shown in the table below), but the most common form of JV is a company where each party invests, i.e., takes shares in the company (limited by shares), or where each party guarantees the company’s liabilities up to a fixed amount (limited by guarantee).

Setting up a JV company provides both parties with some protection in the form of limited liability in the event that the JV fails. However, no corporate structure can protect from the reputational damage that may ensue if it does fail. Stakeholders invariably look to the council to provide the solutions in the event of any issues with the JV, rather than the other partner, because, often, it will still need to provide those services to the public or be reliant on the back office services being provided by the JV.

The ownership structure is an important determinant of the governance arrangements. For example, in some cases a 50:50 ‘deadlock’ JV may be deliberately structured to provide both parties with equal voting rights. In our experience, the collaborative relationship between the two partners is more important than the equity split; consensus between partners should be achieved through working together rather than a focus on the ownership proportion. It is a reality that greater voting rights can help to retain control, but if the partnership is working well this should not be necessary.

An effective governance framework provides protection and ensures there is accountability for both parties. This typically includes documents such as shareholder agreements and memoranda of understanding which set out expectations and responsibilities of both parties to the common

Types of JV model

**Contractual partnering**
Suitable where there are clearly defined tasks to be undertaken, likely to be relatively static and less flexible.

**Limited partnership**
Not a separate corporate entity and can be inflexible, however limited liability for partners and a flexible basis for profit distributions.

**Company limited by shares**
This is a flexible and familiar structure with a simple mechanism for the introduction for new equity/transfers. There is limited liability for shareholders with reward linked directly to risks taken, generally in direct proportion to the proportion of shares held. Governance and minority protection or reserved matters may need to be considered.

**Company limited by guarantee**
Flexible structure for a non-profit distributing venture. It is easier for members to join and leave, with rewards linked directly to risks taken. May prove more difficult to attract investment.

**Limited liability partnership**
Corporate body with limited liability with a flexible basis for profit distributions and return of capital. There is a lack of case law in the event of a dispute and there are potential limitations for local authorities to trade through a partnership.
goals. It is also usual to have certain ‘reserved matters’ that require the participants’ approval. These should be confined to strategic rather than operational decisions, for example relocation or local procurement requirements. Effective strategic collaboration can distinguish a JV from other models and deliver strong outcomes for each partner. Clear governance arrangements underpin the collaboration and are essential to the success of the JV.

The nature of a JV means that the various stakeholders have different roles, needs and levels of interest. Elected members may have an interest in securing the quality of services for the right price and require a level of information that informs their policy decisions. A private sector partner will by necessity focus on commercial considerations as they need to make a profit to remain in business. The council is both the commissioner of JV services and a partner in the JV which makes decisions. The governance arrangements need to: give assurance to the council that its objectives are being met; be flexible enough to ensure that the JV can deliver its business plan; and minimise conflicts of interest. Clarity over how the ‘client’ role and ‘partner’ role of the council are to be discharged is essential.

Southwest One

Southwest One is 85% owned by IBM and the council had concerns that it did not have enough influence and the JV did not have full accountability. To provide sufficient control for all the partners, it included ‘reserved matters’ within the constitution (see page 22) to give sufficient control of key strategic decisions. An example of this in force occurred around relocation, where the council did not want jobs to be moved out of Somerset, although this would have an adverse impact on growth and therefore was not consistent with the objectives of the JV.

The board’s remit is to manage the business and operate in the interests of the company. This responsibility may well conflict with elected members’ primary focus on what they consider is best for the council. The council should consider how it will appoint its representatives to the board to ensure that duties to the council and the company are discharged effectively. There are other mechanisms, such as a shareholder committee, that may be used to facilitate accountability. Training for board members before the company is set up is recommended.

CATERed

For CATERed it was important to ensure that all 67 of the schools involved had a voice without the governance arrangements becoming too complicated. This has been achieved by setting up a company which is owned by the schools on the basis of one school – one vote. The company, Plymouth Schools Shareholding Company Limited, is limited by guarantee. The company owns 49% of CATERed and the council owns 51%. CATERed is limited by shares. The CATERed board comprises eight teachers and two council officers.

This will ensure that conflict protocols and procedures are understood. Equally important is the council’s role as a client and how it intends to undertake and manage its actions with the company.

As the JV matures, it is good practice to revisit the governance requirements periodically. Do the structures in place continue to provide the right balance between control and freedom to operate, along with the right information to enable effective decision making? The governance arrangements will inevitably need to evolve over time to ensure that they continue to be relevant for the company and its owners.
Building a successful joint venture company

Common reasons for setting up a JV

- Quicker transformation of services
- Greater investment in infrastructure/assets than the council operating alone
- Generating savings and return of profits back to the council
- Greater income generation opportunity, bringing a greater commerciality to a service
- Developing expertise and skills of council staff
- The desire to work in partnership with a provider who brings expertise and scale economies

Objectives, outcomes and ambition

It is important to be clear about the objectives of the JV. Potential partners require clear information about the council’s requirements to enable them to submit the most appropriate bid.

We have set out below the most common reasons for setting up a service JV. All of the JVs we looked at were able to show delivery against these reasons, although, of these, the desire for ‘quicker transformation of services’ tended to be the most difficult to achieve.

Collaborating with a partner who has complementary abilities and resources, such as finance, distribution channels or technology, can make good sense. JVs offer the opportunity to share risk and reward. Trading separately, with shared commercial skills, the JV may be able to access opportunities which the council may not have been able to achieve alone. JVs are not suitable in all situations.

“Enable head teachers to focus on the core business of providing children with a high-quality education rather than wondering whether the peas have been delivered for lunch.”

CATERed

If the council wishes to retain control – and all the associated risk and reward – a trading company may be more appropriate. Similarly, if the objective is simply to cut costs then outsourcing may be the most appropriate model.

Be ambitious: before making any decision, the council must be clear about the intended purpose of the JV. It must be able to articulate its ambition for the JV and the service(s) the JV will be providing. For example, is the key objective revenue generation, promoting social value, improving service quality or reducing costs? It is not simply agreeing which services are to be provided. It is focusing on the objectives and outcomes that are expected from the JV. JVs are unlikely to be the best option if the objective is purely cost saving. Typically, successful JVs are created where the council has ambitions for wider gains such as income growth and/or value to the community.

Some JVs arise from a need to continue to provide public services, but in a way that more closely aligns with financial constraints and how budgets are devolved. The public-public JV of CATERed is an example of how changes in funding to schools produced a real need for the existing schools meal service to work with schools and help them decide how best to meet their obligations. The JV would not be sustainable without a critical mass of schools receiving its meals service. Equally, for each school, it was important that this change in funding did not place an additional burden on head teachers. The clarity of the shared objectives has helped ensure the JV is maturing well.
Be ready to work in partnership
In setting key outcomes and agreeing the services to transfer, thought needs to be given to how the services will relate to the rest of the council. For example, how will transformation programmes be co-ordinated across the JV and the council. Will the JV be treated as a separate company or is it expected to act as a directorate of the council? If it is the latter, in our experience, it is unlikely to be successful.

“Budgetary pressures mean that generating income is necessary and a JV model is a sustainable way of achieving this requirement. It is also important to keep some degree of influence over the service.”
Nottinghamshire County Council

It is a reality that in transferring services to the JV the council will and should lose some control over their day-to-day management. The JV needs to be able to change and explore different operating models without the risk of unnecessary direction from the council. Some councils are uncomfortable with the thought of losing control of services. If this is the case then JVs are unlikely to be the ideal solution. In making this decision councils will need to balance their desire for innovation and cost reduction against their wish to retain direct control.

It is also important to consider the ability and appetite of the council to collaborate rather than contract manage. JVs are a partnership and a willingness of both sides to work together and to change is a key ingredient of a successful JV. Lack of clarity on this issue has caused a number of JVs to flounder, so councils need to be clear about their own ability to work in partnership and to avoid reaching for the contract every time there is a problem.

As we outlined in our ‘Spreading their wings’ report, there are other options. All of the different potential options should be considered first, to ensure that this model is the best fit. For example, a LATC, outsourced contract or informal collaboration (which provides flexibility and the opportunity to respond in a more agile fashion to changes in the local landscape) may be more appropriate. The suggested approach for an options appraisal is set out in ‘Spreading their wings’.

The circumstances of the council and perhaps the partner organisation will change over time. Clarity is needed at the start with regard to how the partners will manage these changing circumstances, adjusting both the objectives of the JV and the associated contracts to meet the changed circumstances of the partners. A key question to ask is ‘Will the JV restrict the council’s ability to be flexible in the future and affect its ability to respond to changes in the local landscape?’.

These may include changes of political administration or new commercial opportunities elsewhere in the local economy. The council’s partner in the JV cannot be expected to take the risk of significant potential changes. The relationship and understanding the environment in which each operates and what they are each required to deliver, alongside appropriate contractual mechanisms which allow sufficient flexibility, are particularly important in managing and sharing the costs of these changed circumstances.

Carry out the due diligence
Once all of these areas have been considered, a business case needs to be developed for the JV. Due diligence is critical; there should be a clear understanding of the existing services, their associated financial costs and opportunities for growth or cost savings.

The business case should set out the benefits of the JV over its lifetime and give assurance to stakeholders that all key considerations have been taken into account, for example future income streams based on market assessment. This is often neglected, but it is important to understand how the market will respond and the procurement process that may best deliver the requirements. The business case should also be capable of demonstrating the wider benefits to be realised, rather than purely the financial.

It is important to obtain professional advice and support in the early planning stages to avoid costly mistakes further down the line.
Key considerations for the planning stage

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<thead>
<tr>
<th>Strategic direction</th>
<th>What are the JV's objectives and how will the company be managed?</th>
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<tbody>
<tr>
<td>Business activity</td>
<td>What will be the core levels of activity for council services and beyond? Is there a tension between delivering improved services to the council and concentration on securing new business streams? How will profits or losses be shared? Who will own any intellectual property created by the JV? How will disputes between the JV partners be handled?</td>
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<tr>
<td>Financial planning</td>
<td>How will the JV be financed at the start? Is existing baseline information accurate and correct and are any assumptions made realistic? Where are the milestones for further investment and what will happen if additional funding is needed in the future? Will finance be available to support business growth? Are all the elements that impact upon the venture's cost base identified and included in the costing analysis? Are the assumptions that underpin these costs reliable or appropriately reflected in scenario planning?</td>
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<tr>
<td>Employment matters</td>
<td>Who will work for the new venture and how will potential issues around staff transfer and pensions be resolved? Is a plan in place to deliver cultural alignment? What is the long-term development plan for staff?</td>
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<tr>
<td>Support services</td>
<td>How will support services be provided and at what cost?</td>
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<tr>
<td>Assets</td>
<td>What assets and other resources, including intellectual property, will each party contribute? Who owns the assets and what is their value? What happens to the assets on exit?</td>
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<tr>
<td>Governance</td>
<td>What arrangements are appropriate to give the parties sufficient assurance, providing a balance between control and freedom to operate? What controls are proposed at board and shareholder level? Which innovations in governance such as service user or staff forums have been considered?</td>
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<tr>
<td>Markets</td>
<td>How will the parties ensure they can continue to deliver the objectives against a changing financial backdrop, economic environment or changes in government policy? What factors are so critical they could render the JV unsustainable (eg is it heavily dependent on particular income streams) and are these critical factors featured in scenario planning? Are demand assumptions reliable or appropriately reflected in scenario planning?</td>
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<tr>
<td>Measuring outcomes</td>
<td>What performance management arrangements will be appropriate? Can they be measured in the immediate short-term or will some of the benefits take a longer time to realise? How is the JV appropriately incentivised to perform?</td>
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<tr>
<td>Exit strategy</td>
<td>What exit routes will be available if either party wants to realise its investment in the JV, or wind it up because it is no longer achieving, or has already achieved its intended purpose? What are the realities of the service transition and does any exit plan appropriately reflect the complexities of unravelling longer-term arrangements?</td>
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Legal powers and state aid
JVs are typically set up under the general power of competence contained in Section 1 of the Localism Act 2011. There are various structural options which provide both the council and the other party with some control. This may be the creation of a company limited by shares or guarantee, or a partnership. There may also be other associated legal issues to be considered such as what can be contracted out to any partner and which statutory duties the council may need to ensure are being appropriately discharged in accordance with its duties.

State aid legislation governs whether financial support from state resources can be granted to companies and JVs. These rules prohibit state aid, in whatever form, which could distort competition and affect trade by favouring certain undertakings or the production of certain goods. Examples of state aid are the giving of loans, grants, subsidies or provision of support services below market rates, or granting of business rate exemptions. Councils therefore need to pay close attention to what support they will provide to any JV in which they are taking part. Many JVs are set up at a market value or follow a procurement route to prevent issues with state aid arising. However, it is important to consider all aspects of the transaction and complete a state aid assessment to determine whether it may be an issue, or whether there is any leakage of state aid further down the transaction chain. There are often ways to resolve such issues if sufficient time is allowed to take legal advice at the outset.

Management
A JV requires a strong management team with commercial acumen. Often the partner is able to bring this skill so it is important to understand to what extent this will be required. Depending on the situation, external recruitment may be needed. This is particularly important if a key objective of the JV is to grow beyond contracting back to the council. It is also important to ensure that there is sufficient knowledge of contract management retained in the council to ensure that it is delivering the desired outcomes.

The degree of staffing and skills required to run the JV should be considered at the outset as specific skills – such as procurement and project management – are needed for it to be a success. Operating a JV necessitates input from the council throughout the whole lifecycle of a JV from the procurement stage to eventual exit. Many councils or their partners have reduced their capacity and capability in recent years and may realise that they don’t have the necessary in-house skills to procure and manage contracts. Identifying this before entering into any JV is essential, because it is difficult to bring in this expertise at a later stage. There are many instances where JVs have not delivered intended benefits because the council has not managed the contractual relationship effectively, that is, the operational perspective has not been considered. There should be no surprises for either party; the financial models, contractual mechanisms, governance arrangements and anything else must be clearly understood by all involved in delivery, both within the JV itself and in any council retained client-side function.
Case study 1

Entrust – Staffordshire County Council JV with Capita

Staffordshire County Council's education support services had an annual budget of around £60 million, but was caught in a 'perfect storm'. The value of work had reduced in the previous two years and there was concern over the job security of all the 4,500 employees. Schools were becoming more independent and education outcomes increasingly important. The council looked at options including a trading company, but felt that they wouldn't be commercial enough on their own. However, they did see a big commercial opportunity in education support services and identified a £19 billion market that they could access. Key factors were education outcomes, revenue generation and innovation of education to promote better outcomes.

Having identified a JV venture model as the preferred vehicle, they used external support to carry out soft market testing with a range of suppliers. The process also included discussions with private equity houses. With 20 different services to bring across, this was a big undertaking. Without a track record the business was not initially attractive to private equity houses.

Negotiations with the shortlisted potential partners followed and identified that Capita brought forward lots of good ideas, was prepared to invest to improve services and shared the same strong vision as the council. Discussions with the unions and pensions were important – particularly around risk sharing.

Crucial factors to success were: political support; keeping the workforce informed; and keeping the work in Staffordshire. The council wanted a minority shareholding to facilitate commerciality, but sufficient to ensure that the council's voice was heard. They therefore agreed a 49:51% split of equity.

Entrust started in 2012/13 and has grown considerably since then – supporting over 600 schools, up from the original 400 at creation of the JV – and is performing well. The route to growth is proving to be different to that initially envisaged. Instead of acquiring large services from other local authorities, the business is growing incrementally with new schools, clusters of schools and chains coming on all the time. The council is confidently anticipating further growth and while at some point in the future it might consider realising its investment, that day is a long way off and the council is giving no thought to exit at the present time.
People

Most JVs include the transfer or secondment of people from the council. As we highlighted in ‘Spreading their wings’, a change to a more commercial culture will be needed if the JV is to be successful. The JV will need to be focused on delivering to its ‘client’ (the council) and, in many cases, in generating new business. Both leadership abilities and the behaviours of the people in the JV will determine the success of the new business. In the midst of the transaction, it is easy for these ‘softer’ changes to be forgotten, but the JV will not be successful without them.

To achieve as smooth a transition as possible, communication with those involved throughout the process is extremely important. Even if those delivering the project think there is nothing to say it is better to report what they can. More often than not, silence is filled with rumour and speculation. It is vital to understand and respond to the key concerns that people and stakeholders raise. These will inevitably vary depending on the circumstances. In the case of one JV, rebranding was seen as crucial to differentiating the new company from the council. As a result, a key priority for people was a new uniform. In other cases, the priority has been to ensure that staff continue to be able to identify with the council and to maintain those close relationships rather than promote a separate identity.

“You’ve got to control the rumour.”

CATERed

There is no fixed model for how people are moved into the JV. For example, Southwest One chose to second people into the JV from the public sector partners rather than transferring people under TUPE. CATERed choose to transfer its people under TUPE. There are advantages and disadvantages to both choices.

Secondment creates less uncertainty for people as they still feel connected to the council and it removes the need to make changes to pension arrangements with the local government pension scheme (LGPS). On the downside it means that there is no opportunity to discuss with people changes to terms and conditions that could make the JV more successful and create opportunities for individuals. Secondments also make cultural change harder to implement. Without this increased commerciality or focus on improved service delivery it will be harder for the company to be successful.

CATERed opted to transfer its staff under TUPE. The 51% control of the JV by the council enabled the JV to remain a scheduled body within the LGPS. This meant that staff being transferred could continue to benefit from this scheme. The council was also able to transfer associated pension assets and liabilities to the company. Other upsides to TUPE include the ability to renegotiate terms and conditions with new staff, and to implement cultural change.

A clear decision is needed at the start of the process as to whether the JV will move away from council terms and conditions, including the LGPS over time for both the people currently providing the service and for new starters. Councils need to balance the potential cost savings, the release of monies to deliver better services and the terms and conditions offered to people working in the JV.
Pensions

Pensions are often seen as a significant issue for any transfer of council staff to a commercial entity due to the scale of the pensions strain, but the issues are not insurmountable.

The council should have a sufficient understanding of the partner’s transition plans so that any impact on pensions can be assessed. Unless these are clearly set out, there can be misunderstandings that can prevent the JV proceeding. For example, costs savings may be predicated on a reduction in staff through redundancy, but unless this has been communicated, it may not be included in any financial models and could adversely impact the success of the JV due to pensions liabilities not being taken into account.

Future pension schemes and the potential for liabilities can have a significant impact from a financial perspective, especially if there are significant number of staff in the LGPS.

Key pension considerations

- Who is responsible for the deficit funding and how will this affect employer contributions in the future? This can have a significant impact on a company’s viability or leave the council with unfunded costs. Where does the risk best lie?
- What is the cost of any pension bond and how is the cost of that likely to be managed?
- Who is responsible for any potential pension liabilities that would arise should the company fail?
- What form of pension scheme will be offered to any new starters?
- Will existing employees continue to be able to be members of the LGPS scheme, and will the JV be able to gain admitted body status to the scheme?
Setting up the JV

JVs typically require a process to identify and contract with a suitable partner. In our experience, many of the skills associated with partnership working are highly specialised. Most councils will have not been through the process before and quite naturally will not have either sought to develop or retain these procurement, marketing, legal or financial skill sets.

Engaging advisers with these skills from the outset is often the solution. While we accept that there is a cost to this, councils need to ensure that they have the right support to manage the procurement process effectively.

Selecting the right procurement process

An alternative model for delivering services is usually in response to challenging funding gaps and time is limited. Councils feel the pressure to move very quickly through the procurement stages so that benefits can be realised as soon as possible. As a result, OJEU notices are often produced to a very short timescale. The impact of this can be a lack of clarity on councils’ requirements and insufficient time and flexibility in the procurement process to explore fully the opportunities with partners. In some cases, this has led to the procurement process being stopped which can then cause further delays.

Procurement processes should not be viewed as a formality, but as something capable of delivering a real solution to the actual objective. It is important to be open to the different processes that could be followed. The new 2015 public procurement regulations have introduced new processes that may be of use to councils, including a new competitive procedure with negotiation and a new ‘innovation partnership’ process. They also removed the list of services that (subject to cross-border interest) did not have to be tendered. For many such services a new ‘light touch’ regime applies to all contracts above £589,148. Light touch services include health and social care, education and youth services, and cultural services. So there will inevitably be a competition, but the key is the manner in which tender exercises are managed to choose the best partner for a JV.

Councils need to consider the following areas before procurement:

- If needs are well understood, would a competitive process with negotiation be appropriate?
- If more innovation and solutions from the market place are required, would a competitive dialogue be a good idea?
- Where would an innovation partnership fit in? This is still an evolving process and may be more appropriate for development of new goods, though the legislation does state it can also be used for services. There is limited evidence as to the benefits the process can offer but it should not be discounted
- If selecting a public-public JV what are the implications of Teckal as set out in our ‘Spreading their wings’ report and joint control on the procurement?
- If health, social care, education or other specific services falling within the new light touch regime are part of the procurement, can advantage of the light touch flexibilities be taken?
- Could the JV be linked to the ultimate pursuit of a public service mission based on employee ownership or participatory principles? If so, there is also a procedure that can be followed to deliver this objective

Once a shortlist of potential partners is established, if the procurement process allows it, councils are able to enter into discussions with them in order to identify a preferred partner. The process can help to ensure the council gets the best deal, as interested parties may be encouraged by competition to enhance their offer – not merely in financial terms, but in the innovation and other value reflected in their bids. It can be an opportunity for both parties to get to know each other better.
**CATERed**

CATERed is a co-operative trading company which is 49% owned by 67 local schools and 51% by Plymouth City Council. It serves almost 2.5 million meals to Plymouth schoolchildren every year.

The council historically subsidised the school meals service which made a notional loss of around £1 million a year. The schools’ focus was perceived to be on the teaching curriculum rather than the financial viability of delivering the school meals. The catalyst for change occurred when central government delegated responsibility for the service to the schools. At this point the council discussed the likely impact of this change with the schools to help them develop the best way to meet their statutory responsibility. It was clear to all that schools could not afford to deliver the service in the same way and that individually they would be unable to maintain kitchens and the employ the people required.

As a first move, for the financial year 2013/14, all those schools and academies receiving services from the education catering service agreed to pool the entire delegated funds, to support each other, share risk and ensure continued provision of high-quality food at the same cost to all pupils, regardless of where they lived or attended school. Schools supported the pooling arrangement on the understanding it would ultimately lead to the setting up of a company which had a strong schools representation.

The council and schools later decided that a JV structure would suit the requirements of joint working; allowing the focus on good outcomes for children in addition to cost saving and income generation opportunities. The company was set up as a Teckal company in order to enable it to trade with the council unfettered by procurement rules.

The council believes that this collective approach will “enable head teachers to focus on the core business of providing children with a high-quality education rather than wondering whether the peas had been delivered for lunch”.

Approximately 250 staff were transferred from the council’s education catering service to the company, meaning their conditions of service, hourly rates, hours and length of service were unaffected. Decisions about the school meals service are taken by a co-operative joint partnership board of elected representatives from the schools and the council.

As well as delivering school meals, the company has freedom to secure additional business (within the Teckal thresholds) and procure its own back office support.

The council subsidy is reducing each year and the service will be self-financing by 2016/17. The business plan makes it clear that CATERed needs to feed 61% of pupils to enable it to make a small surplus that covers the kitchen maintenance and equipment costs. There are plans to expand the service to other schools in the region and more widely, but CATERed is very clear that the relationship with existing school clients must not be compromised.

CATERed obtained independent legal advice in setting up the company and now recognises the need for further advice on VAT and Corporation Tax.

The council took care to ensure that staff transferring were engaged and informed throughout the transition process. Regular communication was seen as key to resolving key questions such as job security and pensions before rumours started.

By owning 51% of CATERed, the council has been able to ensure that staff retained their LGPS pension. However, the rebranding has had a positive impact on front line staff as they now have a wider range of opportunities for business development.

The council believes that some aspects of the JV’s management will need further development. Performance management is one such area.

CATERed took a decision to procure as many back office services from the council as possible in order to be able to focus on the core business. However, CATERed is now looking more closely at these costs, working with the council to identify the true cost of service provision, rather than an apportionment. It may decide in future to test the market and the council will need to recognise that this source of income may not continue.

The council considers CATERed to be a success. There is a shared vision of delivering high-quality affordable school meals and the number of children taking school meals has increased significantly. This allows the council subsidy to reduce each year. New opportunities for expansion are carefully considered for strategic fit with the core business of school meal delivery.
Set the right procurement criteria
Councils will need to be aware of EU procurement requirements and the different requirements that may apply when the other party is in the private rather than the public sector.

Selection criteria used to shortlist potential partners are usually based on their financial standing, technical capabilities, competencies, experience, attributes and legal status. However, in a JV relationship it is also important that the other party will ‘fit’ well with the objectives and vision of the council. This means that other criteria may need to be identified and incorporated into the selection process.

The Public Services (Social Value) Act 2012 already affords councils greater freedom on responsible procurement and it is increasingly common for councils to pursue forms of commercialisation that also deliver both a financial and a social return. The intention here is to deliver multiple outcomes from the same spend. Non-financial outcomes could include:
- the stimulation of more affordable housing
- supporting local SME jobs and apprenticeships
- paying the Living Wage
- safeguarding vulnerable communities
- protecting the natural environment.

Correctly structuring the procurement process at the outset is extremely important in ensuring that the project is capable of delivering what the council needs.

It is important that councils do not simply ask the market to provide the answers without thinking carefully about their requirements first. Relying on their greater experience can of course be beneficial, but must be done with caution. Lack of preparation, with an expectation that the market will provide the solution, may result in suppliers providing the answer that suits them, not the council.

Councils may also wish to consider the reputation of potential partners and the threat (perceived or real) of potential conflicts of interest. Failures of other JVs often result in a level of suspicion being created before contracts even begin.

Review objectives
Keeping alignment of the objectives throughout the procurement process for both parties in the JV is essential. Throughout the procurement process the council and its partner should constantly revisit the questions “What is the JV here for? Will it work for both sides?”. This consideration is often more important when entering into a JV that includes both public and private sector partners.

Common council objectives include a change in service delivery, cost reduction via investment in new technology and improved business processes. Common objectives for commercial partners are profit, or to gain market share. Understanding the drivers and key deliverables of all parties and aligning them prior to entering into the venture is critical to its long-term success.

“In a JV relationship it is also important that the other party will ‘fit’ well with the objectives and vision of the council.”
Building a successful joint venture company

Make an investment decision
The JV needs to be attractive to other parties. There are a number of factors that will influence the risk assessment of potential private sector partners. These include:

- does the JV offer a good opportunity and align with the partner’s own strategic direction?
- what potential does the service offer for growth?
- what is the expected timeframe for returns and the level of return expected?
- is the investment required at an appropriate level?
- is there an alignment with the partner’s aspirations for its wider business and place in the market?
- is it clear and agreed if any partner intends to deliver social as well as financial returns?
- are the risks worth taking and will the board accept this?

Throughout the procurement process, it is important to be mindful that (for both the council and its commercial partner) this is an investment and critical business decision. The proposition should not be treated as an outsourcing exercise. The council should also be mindful of the fact that some investors or potential partners may not be familiar with public procurement processes and so their expectations should be managed throughout the process to prevent them potentially walking away because the process is simply too cumbersome or costly for them.

One of the key challenges for JVs is meeting the aspirations for business growth and development. This is particularly important in relation to the potential for securing finance for further growth, business development activity and pitching for new business. These are all skill sets which may need to be invested in and developed further if the company is to be a success.

Any tensions between delivering the existing day-to-day services and servicing the council while investing time in new business developments need to be understood. Teams may not have had to focus on these areas in their previous work and so there must be an acknowledgement that staff may also need to undertake their own personal development plans which are supported by the company.

All parties need to be clear at the outset about what they want to achieve and how they will grow and adapt together, anticipating that the future environment in which the JV works will change over time.

The partner should bring something new
While the process and meeting any procurement requirements is important, it is the organisational and governance characteristics of those preferred partners that can be critical in establishing a JV which both delivers its objectives and responds to a changing environment.

Is the council clear in what it is looking for in its partners? What does the council feel it lacks in order to be commercially viable? Our research has shown that councils are often looking for a partner who can help them to transform services. While price and cost reduction will inevitably be a consideration, the ‘added value’ or additional innovation that the other party brings to the venture, the opportunity to share knowledge and expertise, is also important in making a difference to the way services are delivered. It may also offer other opportunities to the council that may not otherwise have been available.

Where councils are realistic about their strengths and weaknesses, carrying out a SWOT analysis (strengths, weaknesses, opportunities and threats) and being clear about their own capabilities will help to identify the complementary attributes needed in a partner.
Share profits and risk
It should not be possible for one party to benefit at the loss of the other. For example, excess profit clauses or the requirement to share the costs of redundancy or service reduction should be built into the agreement. Transparency is important for trust to be built between partners and also to demonstrate to other stakeholders (such as local residents) that the JV is operating in the interests of all partners. The rationale behind all charges – such as management charges and advisory costs – should be clearly articulated so that they are understood and accepted. A partner who brings a significant degree of expertise, infrastructure and/or commercial skill will expect a greater share of the JV commensurate with the greater share of the risk they are taking on. This may signal to stakeholders that they are benefiting more from the JV unless the benefits they bring are clearly stated and acknowledged.

Build in flexibility
It is important that flexibility is built into the partnership arrangements at the procurement stage within the contract, articles of association and performance management mechanisms. This will allow for significant changes in external factors, for example, further Central Government funding reductions. The business case should consider the impact of these factors. How will the level of service provision be managed and the balance of risk and control varied?

Many JVs we have seen fail have done so because of the rigidity of contracts. The procurement process and contract should factor in the flexibility to be open and upfront about some of the more difficult areas of commercial negotiation that may be required.

Ensure you have considered the tax implications
Councils are, by their nature, tax efficient and so delivering services through a corporate structure means that tax implications need to be understood at the outset. It is important that specialist advice is sought early on, as it may affect the structure or governance arrangements of the JV. This will ensure that tax and VAT are managed appropriately and reduces the chances of anything significant arising that could impact on the positive outcomes of a JV.

If the JV is a partnership, the entity is ‘transparent’ for corporation tax purposes. That is, the direct tax treatment would revert back to the partners in this arrangement, with each partner accounting for its share of any profits in line with its share of the partnership. If the entity is a company limited by shares or guarantee, it will be subject to corporation tax which will require tax return filings for each accounting period.

The nature of the shareholdings could impact on the use of group or consortium relief to reduce tax liabilities. Depending on the size of the company and the numbers of staff transferred by TUPE into it, intercompany charges and transfer pricing may need to be taken into account when projecting corporation tax costs.

The JV may be required to register for VAT where it makes taxable supplies. Key considerations are the VAT treatment of the goods or services provided and the ability to recover the VAT incurred on expenditure used for making exempt supplies. The JV could be entered into a VAT grouping arrangement with other non-council shareholding entities which could simplify VAT administration and possibly reduce ‘sticking VAT’ costs whereby VAT cannot be recovered. In our experience, inappropriate VAT planning can leave JVs and councils with unexpected costs.

“The council wanted a minority shareholding to facilitate commerciality, but sufficient to ensure that the council’s voice was heard.”
Staffordshire County Council
Southwest One

Southwest One (SWO) is a JV set up in October 2007 between Somerset County Council, Taunton Deane Borough Council, Avon and Somerset Police and IBM. The company is governed by the terms of a Joint Venture Agreement (JVA), with IBM as the majority shareholder providing financing under the JVA. Each of the public authorities nominates a director at the board and maintains a shareholder veto on certain ‘reserved matters’.

SWO provides operational services – including ICT, finance and HR/payroll – to the public authorities – which, along with any associated financial liabilities, are subject to a Parent Company Guarantee (PCG) between IBM and each of the public authorities.

The driving force for the JV was the councils’ desire to do something fundamentally different with their back office services and, in transforming them, to focus on how services were delivered to the customer. The vision was to provide services to a wide range of authorities across the south west, growing the JV to achieve savings for all of them. The aims were to:

- modernise the way the partner organisations worked, to improve access and delivery to customer facing services
- improve and reduce the cost of corporate, transactional and support services with investment in new technology
- generate economic development by investing in Somerset.

The lessons learnt have been key in helping the partners renegotiate the contract. As a result some of the strategic functions originally placed with the provider have now been placed back with the other partners.

The overriding message from this experience is the need for councils to be agile and not expand without the right governance. Only enter into a JV if it makes the most commercial sense. Be clear that the structure will really deliver the benefits that you expect, and that a different model of service delivery, either through outsourcing or a local authority trading company, isn’t more appropriate.

The JV has experienced difficulties including significant contract disputes which resulted in an out-of-court settlement. This experience has resulted in the council reviewing the JV and learning some important lessons. The key challenges can be summarised as follows:

- The project was very ambitious. This generated a hugely complex contract over 3,000 pages long, making performance management against the contract a challenge.
- While the vision was to transform services for all, in practice each of the partners specified different requirements, which added to the complexity of what needed to be delivered. In hindsight more work should have been undertaken earlier to gain clarity on the core common elements for the partners and an understanding of where flexibility was needed for the individual circumstances. This would have reduced the number of competing client priorities.
- The arrangement effectively handed over the control of the transformation agenda to a private sector company. This resulted in difficulties in the way that the client side of the contract was managed. As so many functions went into the JV the council initially felt that only a small contract-management function was needed. However this created tensions when delivery was not as expected and further resources were then needed when problems arose, and at a time when council resources were becoming increasingly squeezed.
- The selected performance indicators were not the most appropriate and not enough thought was given to the behaviours that these indicators might promote. Greater focus needed to be given to mature, constructive relationships between the partners, rather than contractual mechanisms.
- The model used worked on a secondment model, with staff from the partners being seconded into the company with assured employment. This meant that there was no opportunity to normalise terms and conditions which has hampered the ability for SWO to find savings for its partners.
- The need to be able to flex the contract for changes in circumstances was not properly assessed, particularly those outside of the council’s control, such as changes to the economy and the financial circumstances of the partners.

The lessons learnt have been important in helping the partners renegotiate the contract. As a result, some of the strategic functions originally placed with the provider have now been placed back with the other partners.

The overriding message from this experience is the need for councils to be agile and ensure that the right governance supports future growth. The council's advice is only to enter into a JV if it makes the most commercial sense, to be clear that the structure will really deliver the expected benefits, and that a different model of service delivery – either through outsourcing or a local authority trading company – may be more appropriate.
Building a successful joint venture company

“Our report ‘Spreading their wings’ identified that back office support costs were a major issue for the companies.”

This is sometimes overlooked when JV business plans are being developed.

For employment taxes, the JV will need to: run a separate payroll (with separate PAYE and CIS references); agree any settlement agreements with HMRC separately from those of the council and other partners; set up independent salary sacrifice arrangements; and review any tax implications from changes in terms and conditions – particularly those arising from TUPE which will apply when staff are transferred from the council to the new company.

The longer-term plans for business development are also important considerations at the outset for tax planning purposes:

• Where is growth anticipated and in what markets?
• Will the proposed structure of the JV support these ambitions?

Dealing with support service costs

Our report ‘Spreading their wings’ identified that back office support costs were a major issue for the companies. The same issues apply to JVs. In the early stages of a JV’s lifecycle, it is common to procure support services from the council. This approach enables the company to focus on building its business and provides income for the council. However, as the company matures, it is important to have the freedom to procure these services from elsewhere, if this represents better value for money.

In some cases, for example CATERed, the company procured as much back office support from the council as possible in its early stages. This was a deliberate decision to allow those involved to focus on their key objective of providing quality school meals. As the company matured, it challenged the rationale for the charging mechanism and discussed with the council whether a charge based on actual usage was more appropriate. Agreement has now been reached taking account of the added value and knowledge transfer from the council alongside the costs for the transactional part of the service.

We have seen a trend of more JVs looking elsewhere to procure back office services because of cost and quality, or deciding to provide these services themselves. These JVs often develop their own infrastructure to do so. This presents a challenge for councils to consider whether the remaining council services can remain sustainable given this loss of income. Their overheads may remain unchanged regardless of whether the company purchases back office services and therefore this may not result in a saving to the council. This should be assessed and quantified as part of the business case development.
Making the JV successful

JVs tend to have a high profile and are more transparent than LATCs due to the contracting terms, invoices being available for scrutiny and the fact that they are subject to many Freedom of Information Act requests. It is therefore essential to continue to work at the partnership once set up until it ends, whether happily or not, and to be mindful that aspects of the transaction and relationship will undoubtedly enter the public domain.

Create a culture of trust
We have seen that unsuccessful JVs have lacked trust between the partners. This is often the result of misunderstandings. It is therefore critical to ensure that there is a culture of trust; something which is achieved through getting to know the other organisation and effective communication.

There should be a ‘one team’ ethos between the council and the JV and an understanding of the importance of communication across all stakeholders. In our experience, poor communication leads to uncertainty which is often misinterpreted as a significant risk. This can be addressed by ensuring that stakeholders are represented on the board.

Time needs to be taken throughout the life of the partnership to work together and share experiences and concerns. Developing an appropriate working style will take time and requires cultural change by both partners. Councils need to recognise that their own role as an active collaborative partner – distinct from an outsourced service arrangement – is fundamental to success.

Put the right leadership in place for the JV
It is important to put the correct leadership in place and create the right culture in order to make the most of the attributes of the partners and achieve their respective goals. In our experience, successful JVs have appointed individuals onto the board who have knowledge of the business and the associated market and an appreciation of the original motivations for starting the JV. Bringing in commercial expertise is important to help shift the culture towards greater commerciality and set the tone for future growth. Our research found that those who have recruited externally for individuals with specific skills perform better.

Focus on the key outcomes
Keeping alignment of the objectives for both parties in the JV is essential. If the objectives are income generation, improved service performance and cost reduction, it is important that scrutiny is held at this level and does not fall into an assessment of inputs or performance indicators. Our research found that those who periodically reviewed objectives throughout the lifecycle of the JV fared better than those who did not; all organisations change over time and so do their objectives. Understanding both parties’ goals helps partnership working and places less focus on the minutiae of the contract as a means of assessing to what extent the JV is on track.

Allow the JV to operate independently
The JV must be able to operate outside of the council, focusing on income growth alongside improved service delivery and cost reduction for the council. The temptation to make the JV another corporate directorate that acts in the same way as others needs to be resisted. This may be facilitated through physical separation; originally Entrust was based within Staffordshire County Council’s offices and now operates from its own premises which has helped to demonstrate it is a separate commercial entity.
In 2002, Liverpool City Council entered into an arrangement with Enterprise plc for the provision of highways maintenance and street lighting services. A subsidiary company of Enterprise plc, Enterprise Liverpool Limited, was created to carry out the contract. The new JV was then successful in securing contracts for street cleansing (2003), grounds maintenance (2006) and waste and recycling services (from 2008) through OJEU procurement.

At the start, a key driver was the opportunity to bring more commercial discipline to the service, with a strong focus on controlling costs. Through negotiation with the staff and their unions, the company’s management made changes to employment terms and conditions. In turn, this enabled the company to develop a service that was flexible and more responsive to any operational risks that threatened the services being delivered and that might otherwise result in financial penalties through the contracts’ performance management framework.

The JV structure was seen to provide the council with some advantages over other delivery vehicles, in the way that it provided an opportunity for influence and control:

- The council appointed two directors to the company board and holds a 19.9% shareholding with any profits distributed equally to each partner
- With this contribution to the board, the council had input into the appointment of staff, decisions around additional contracts and opportunities to vary the company’s policies, and certain matters required mutual agreement
- Major investment required the council’s approval
- The company’s business plan was the mechanism to tighten up performance every year. With the cash contribution effectively frozen, the onus was on the company to make the necessary savings to offset inflation, which also helped the council avoid inflationary cost pressures

In 2010 the political administration change in parliament and at the council, and austerity measures, were also being felt. There was increasing pressure to make financial savings from awarded contracts. This led to redundancies and failings in contract performance, and the basic services provided by the JV also began to be affected.

The various contracts secured by Enterprise Liverpool Ltd started to come to an end. The highways and street lighting contract and street cleansing contracts ended in 2013 and the council moved to a contract arrangement with another provider. In the same way that the additional services brought into the JV presented the company with opportunities to share its overhead costs over a wider service base, the contractual changes left the company with overheads to be allocated across a reduced number of services.

The Council has been exploring the best way to deliver these services as the contracts came to an end. It has opted to bring the remaining services of grounds maintenance and refuse collection into a new local authority trading company. The street cleaning contract has also since been transferred into the company, from the previous provider.

While the original joint venture was set up to save money and to enable the council to reduce its council tax charges, the change now is to provide a structure that gives sufficient flexibility to respond to business needs but still with a focus on efficiency and the need to drive through performance improvements.
Ensure appropriate corporate structure and governance arrangements

The JV’s corporate structures should allow it to operate in a commercial manner with non-partners and in a partnership manner with the council. From a council’s point of view it should have the necessary oversight and arrangements in place to identify risks in the JV and to ensure performance remains high, but without having to revert to the contract. If the governance is strong, the operations of the JV should be able to run smoothly without interference from the council. Some councils commented that operating a ‘tight and loose’ model, whereby the governance is tight but the operational side is loose, benefits the JV because the council can allow the day-to-day running to be the remit of the JV’s management.

Take into consideration the local politics

Changes in local political administration might be expected over the life of the JV which means that the appetite to retain it may change. Councils should therefore consider the impact of these changes on the proposed JV. For example, a venture that was heavily dependent on government grants may find that a change in funding priorities would have a detrimental impact on its viability. These aspects should be identified as part of the business case, but again underline how crucial it is to ensure that the objectives are the right ones for the project.

Get the right level of performance management

Councils will need to think clearly about the KPIs they want to measure and how these link to the objectives. The KPIs will inevitably drive the behaviour and priorities of the JV, so they need to be closely aligned with what it aims to achieve. As the market moves to more incentivised and outcomes-based contracts, this may require another cultural shift and realignment that will need to be carefully navigated.

“Having a mature relationship with all concerned is much more important than a highly complex contract arrangement.”
Southwest One

Our case studies identified a wide range of performance management regimes. Southwest One has a hugely complex contract which comprises over 3,000 pages. This makes performance management of the contract a real challenge. One of the main challenges faced by Southwest One was that the three public sector partners all wanted different service provision and KPIs adding significant complexity. It also meant that economies of scale were difficult to achieve.

In contrast, CATERed has a comparatively under-developed performance management framework. The main indicator used is the take-up of school meals. The council took external advice on KPIs when setting up the company. As a result, one of CATERed’s KPIs is a cost comparison not only with other local authorities’ school catering services but also with commercial entities in this sector providing the same service.

While measuring progress and achievement is important, care must be taken to ensure that KPIs are not used to the detriment of the JV, as a focus on contract management rather than partnership working can be disadvantageous overall. Councils must therefore strike the right balance between contract management through KPIs and working collaboratively to achieve objectives. A further risk of relying on KPIs is that the council becomes too closely involved in the operational aspects of the JV (rather than strategic) which can hamper its ability to thrive commercially.
Planning the exit

It is helpful to have some clarity from the outset regarding how and under what circumstances the venture will come to an end and that this exit strategy is documented, even if it is amended at a later date. The Articles of Association and Shareholder Agreement can include protection for all parties. For example, a ‘tag along provision’ is a right entitling certain (usually minority) shareholders to participate in a sale by the other (usually majority) shareholders at the same time and at the same price for each share. ‘Drag along’ provisions can equally enforce sales by the other party.

During the lifetime of the JV, it is important to try to resolve disputes without resorting to formal procedures or terminating contracts. Building rapport and regular communication, even when the project is running smoothly, can help to ensure that if problems do arise the goodwill has been established to keep the relationship as positive as possible. As a JV is a less ‘arm’s length’ relationship than traditional outsourcing, building trust and the ability to work together are key. Personalities and working relationships are important.

At some stage, however, the JV may need to end. Its objectives may have been met, or the council may decide to bring it back in house. For both scenarios, the exit strategy must be understood by all parties at the outset of the establishment of the JV, especially how the risks and rewards will crystallise at the end of the arrangement and be returned to each partner.

The initial contract with the JV may have been for a fixed period of time and these contracts may then be extended or re-tendered. If the council seeks an alternative provider, the JV is faced with a shrinking business, but may be left with limited scope to reduce its overheads or other costs while having to continue to meet other service obligations. If short-term thinking becomes the norm then this may hamper investment that might otherwise improve business practices and release efficiencies. It is therefore vital for the council and partner to agree how and under what circumstances the JV might be brought to a close, so that action may be taken swiftly if needed.

The exit strategy not only needs to be considered in relation to terminating the services agreement, but also in relation to the governance arrangements, sale/transfer of shares in the JV company and, ultimately, winding it up. The complexities arising on the transition of services, depending upon their nature and scale, cannot be underestimated. A properly managed exit could take some time to realise.

There should be consistency across the legal documentation as to how any exit or termination strategy is to be implemented. The services contract would usually contain ‘consequences of termination’ provisions and an exit management plan to ensure that there is a managed process for the transfer of the services/exit. This may address issues such as the approach to be taken on asset valuations and ownership.

The shareholders agreement would normally detail how the parties can exit from the JV and this would also accord with provisions and protections contained within the Articles of Association. For instance, the articles may include protections around reserved matters which cannot be agreed without both parties’ consent, rights of pre-emption so as to avoid dilution of existing shareholdings, or provisions which can force share sales or transfers in particular scenarios where one of the parties’ intends to sell their shares. It is imperative that all parties are clear on the potential exit strategies and how they may be implemented, so as to avoid disputes arising at a later stage, particularly at a time when good relations may be more strained.

A JV has reached its end when it can no longer provide the most effective vehicle for ongoing council services to be delivered, or where in contrast it has been successful in meeting its objectives and reached the outcome that it was set up to deliver. Whatever the result, the experience will inevitably impact upon future collaborations. The ending of a JV does not necessarily mean that it has been a failure; rather that it has served its purpose and the council is now able to deliver services better through another model, or bring it back in-house if that is the best option.
Case study 5

Coventry City Council and Solihull MBC Waste Partnership

The Coventry and Solihull Waste Disposal Company Limited (CSWDC) is an independent waste management company whose main business is extracting energy (heat and electrical power) from municipal and commercial solid waste through an energy-from-waste facility based in Coventry. CSWDC manages household waste disposal for the councils and also provides heat to Coventry’s district heating network through a council partnership with Cofely to heat council buildings and the cathedral.

CSWDC has been operating successfully since 1975, but was established in 1992 as a local authority waste disposal company (LAWDC) because Coventry and Solihull were obliged to arrange for the discharge of their waste disposal functions through a contractor or a LAWDC.

Coventry holds two thirds of the share capital and Solihull has the remaining third; voting rights are shared equally. Both councils have maintained a strong, positive relationship over the duration of the venture. Warwickshire County Council recently gained a minor limited rights shareholding at nil value. The company is managed operationally by a managing director, financial director, a small management team and technical staff. They report to the board. Both councils have non-executive directors on the board and there is also an independent non-executive director. The shareholder panel has the right to make certain decisions which are incorporated in the Articles of Association and Shareholder agreement – the panel includes elected member representatives from each of the councils.

Key success factors

- Clarity on the purpose of the company and keeping strategic objectives aligned – the councils each had a shared objective to collaborate
- Throughout the duration of the partnership time has been invested in familiarisation with the other partner
- Strong governance through the board – ensuring effective challenge and performance of the company and its business plans to ensure they remain robust. This has also included ensuring that non-executive director appointments are made on the basis of strong credentials and experience
- Maintaining strategic awareness of the company’s activities and its operation, in the interests of both the company and the shareholders
- Having no day-to-day input from the councils to allow it to operate with sufficient commercial freedom as an independent entity
- Using professional advice whenever needed by company executives. The councils themselves have also sought advice where necessary to support their role as shareholders
- Keeping the governance as simple as possible
- Having a gateway process in place to ensure decisions are made as robustly as possible and against agreed performance criteria
- Ensuring the company continues to generate value for the shareholders

Advice for others considering entering a JV

- Don’t rush when developing the model – take a measured pace to ensure nothing is missed, get the right advice early enough and learn from others
- Keep everything as simple as possible to make it easier to manage – a clear purpose is easier to achieve
- Some service areas are easier to put into a JV than others – waste is relatively straightforward, but is also highly specialised, so ensure that there is the right expertise to operate the venture and as part of the board
- Create the right environment for maintaining the alignment of strategic objectives and exploring how the venture can maximise benefits to all parties
- Question whether a formal structure such as a JV is necessary – an informal financing arrangement may be preferable, particularly for shorter-term projects, and enable the council to be more agile in response to opportunities for investment
- Put in place strong governance arrangements which people understand and believe in, with a framework including a clear shareholder agreement in place, which is refreshed regularly to maintain relevance
- Consideration of whether critical size is an issue in sectors that are dominated by larger entities, often multinationals

Challenges experienced include:

- Implications of managing the pension liability and associated contribution rates within a smaller entity, for staff who are part of the LGPS
- Cost of existing terms and conditions and losing competitive edge in the marketplace
- The complexities of tax planning which has usually required specialised advice
- Breakdown in relationships throughout the lifetime of the partnership and the rebuilding of them
Case study 6

Nottinghamshire County Council JV with CORMAC

The council was looking for an alternative way of delivering its highways services. An options appraisal was conducted and the authority selected a joint venture model as the best fit to its ethos and goals. This would enable the council to benefit from the skills and scale economies of a partner. A partner with shared values was also important, keeping the beneficial elements of a public sector ethos but adding a much stronger commercial drive. Budgetary pressures meant that maintaining a viable operation was becoming more challenging. Generating more external work was not only desirable, but necessary, with surpluses returning back to the council.

For CORMAC, this was the first JV model they had entered into with a local authority to deliver its services. They were looking to build on their original model and were keen to explore the possibilities. CORMAC was keen to expand into other parts of the country and the Midlands was seen as a good opportunity. The joint venture model was an attractive option for both partners: NCC would pass over some control but gain expertise and scale from an organisation that shared similar values; CORMAC would expand its business and would share in the benefits.

The contracts were signed on 20 May and the new company ‘Via’ has a go live date of 1 July 16. The budget of £42m (including capital and revenue) will be transferred, covering highways operations, highways management and design and fleet management and maintenance. Initially the JV will largely be handling passported work, and it will very much be business as usual to start with but after settling down the plan is to start looking for more external business in both the design and delivery areas. CORMAC has tried and tested processes, including a time recording system that will allow them to record productivity, helping to control costs and making the operation more commercial.

The main barrier to change is culture, but the council and CORMAC have worked to ensure that this is not an issue by having a good communications plan including staff engagement and briefings. Both parties recognise how important it is to bring staff along, for them to be involved in the journey and feel that they have some control and input into the change process.

Staff are supportive of the change, they understand the alternatives and welcome this as an opportunity to develop and grow, as CORMAC has done over the past few years.

Potential issues around the Local Government Pension Scheme and working capital have been addressed. The agreement will operate on a positive cash basis – the council will pay monthly in advance to an agreed profile. Via will have a positive cash flow. Sub-contractors will be paid promptly. Client management, as in all such arrangements, is key to ensure that the work is undertaken to time, cost and quality standards, and invoiced appropriately. Elected members will still play a major part in monitoring performance and determining key priorities, in terms of capital investment.

Support services have also been considered. A new company, CORSERV, has been set up, owned by Cornwall Council. This is the holding company for Via. CORSERV will provide a range of services to Via, including Finance, HR, Health and Safety and commercial support. Payroll and IT will continue to be provided by Nottinghamshire CC. CORSERV will also provide support services to other companies owned by Cornwall Council.

Nottinghamshire County Council will own 49% of Via and CORSERV 51%. The board will comprise two directors from CORSERV and two from Nottinghamshire. The chair is from CORSERV and will have the casting vote. Via will be run from Nottinghamshire by the new Managing Director, Doug Coutts, who has extensive commercial highways experience and there is the benefit of a successful and strong management and staff team from the current operation.
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We regularly produce sector-related thought leadership reports, typically based on national studies, and client briefings on key issues. We also run seminars and events to share our thinking on local government and, more importantly, understand the challenges and issues facing our clients.
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