CABINET

Proposed Company Restructuring of Oldham Care and Support and Oldham Care and Support at Home

Portfolio Holder: Councillor Harrison, Cabinet Member for Adult Social Care and Public Health

Officer Contact: Paul Cassidy, Director of Children’s and Adult Services

Report Author: Maggie Kufeldt, Assistant Executive Director Adult Services and Commissioning, Ext.4208

29th September 2014

Reason for Decision

To enable the restructuring of the wholly owned social care company group namely, Oldham Care and Support, in order to reflect our co-operative ambitions and to improve the efficiency of the company group.

Executive Summary

The report seeks approval of the restructure of Oldham Care and Support, by creating a holding company that will sit above Oldham Care and Support and Oldham Care and Support at Home.

It is recommended that the holding company is a Teckal exempt Community Interest Company, reflective of the Council’s co-operative ambitions.

The restructuring of the company provides an opportunity to make the company more efficient, in support of the adult transformation programme.

It is anticipated that the proposed restructure will have a 2-3 year life span, dependent on the growth of Oldham Care and Support at Home.

The effectiveness of the company structure will be monitored through the monthly client meetings and quarterly performance management meetings.
Recommendations

Cabinet are requested to approve:

1. The Restructuring of Oldham Care and Support such that a new structure and holding company can be put in place, with Oldham Care and Support and Oldham Care and Support at Home being subsidiaries of the holding company;

2. Option 3, the preferred option to establish a Teckal exempt, Community Interest Company holding company (see S2.5 and S2.6 for detailed explanations);

3. That the Borough Solicitor, or their nominated officer/representative is instructed/authorised to work with the Executive Director Commissioning and/or their nominated representatives to: achieve the establishment of the new company structure, and to sign and affix the common seal of the Council to any documentation required to legally effect the Restructure Proposals, furthermore:

4. Be given the authority from Cabinet to complete all new registrations and technical administration to comply with statute, company and the common law.
Proposed Company Restructuring of Oldham Care and Support and Oldham Care and Support at Home

1. **Background**

1.1 In October 2013, the Council established two trading companies and transferred staff and services to one of those companies. The companies are registered with Companies House and operate as Oldham Care and Support Ltd (OCS) and Oldham Care and Support at Home Ltd (OCSH). Oldham Care and Support at Home is a 'start up' company which was established with the primary aim of entering the home care and PA market by being in a position to compete in the open market.

2. **Current Position**

2.1 Oldham Care and Support has engaged the services of Price Waterhouse Cooper (PWC) to provide advice on a more efficient trading model. At the same time, the Council has engaged Eversheds to provide legal advice on the same, along with advice in relation to the implications that an altered company structure may have on OCS’s teckal status, and the benefits and implications of any of the companies becoming Community Interest Companies (CIC).

2.2 Teckal is the name given to companies that are set up that are generally owned by the public sector and pass two tests when examined. The name teckal derives from the first case tested through the courts. The two tests are called the control test and also the activity test. These can be explained in more detail if needed, however in simple terms: any Teckal company must not infringe or exceed 80% of its activities beyond the remit of its parent public sector parent and sponsor. If it does then it stands the risk of challenge under the procurement regulations.

2.3 The advice received in relation to a more efficient company structure, maintenance of teckal status and the implications of establishing the companies as CIC’s are dealt with in sections 2.4 2.5 and 2.6 below.

2.4 **More efficient company structure**

2.4.1 So that costs can be reduced, for example in relation to VAT, PWC has suggested that a holding Company should be established. This would enable VAT to be recovered in respect of taxable supplies by the Companies to the Council. The central support team, Managing Director and Finance Director will be employed by the holding company.

2.4.2 As the holding company would be providing social care services directly, it would not require Care Quality Commission (“CQC”) registration. It will have oversight of the other two companies and provide advice and support to a limited range of responsibilities and will act as a holding company for OCS and OCSH.

2.4.3 Under this model, the Council would contract with the holding company for the provision of adult care services, which are classified as “welfare services” for the purpose of VAT. In turn, there would be a contract between OCS and the holding
company for the delivery of those services. The proposed arrangement will help the
Council and the Company financially by prudent tax management and also comply
with the intention of the new procurement requirements. Whilst from a procurement
perspective, it would be cleaner for services to be provided directly between OCS and
the Council, the legal advice raises no undue concerns if the contractual arrangements
for the services are between the holding company and the Council.

2.4.4 Advice secured from working with PWC identifies that this model has the potential to
reduce costs when compared with the existing company structure and similar
arrangements have been implemented successfully on behalf of a number of other
authorities within the last six to twelve months.

2.5 Teckal Status

2.5.1 To maintain the Teckal status for OCS, OCS would need to satisfy both the control
test and the activity test by reference to the holding company. Provided the Teckal
exemption is satisfied as between the holding company and the Council, then the
holding company itself is likely to be a contracting authority for the purposes of the EU
procurement rules. The holding company, as a contracting authority, can award a
public contract to an entity which sits below it (here OCS), provided the Teckal
exemption is also satisfied as between the holding company and OCS.

2.5.2 Effectively the control is by the Council and the holding company, which reflects
additional clarification set out in the new EU Directive on public procurement. This is
not yet implemented into UK law (expected implementation date December 2014) but
assuming the UK implements the EU Directive, a structure such as this, put in place
shortly before UK law comes into force may carry limited risk of successful
procurement challenge. This very much depends on what each company is intending
to carry out in practice, the control the Council has with the holding company (and that
which the holding company has with OCS) and who is tasking whom and performing
what activities going forward.

2.5.3 The relationship between the Council and OCSH, the trading entity, must be carefully
structured to make sure that there is no breach of state aid law by subsidising the
costs of that company in a way that will give it a competitive advantage in the market
place. Care has been taken to ensure the companies pay the Council for the services
it provides to ensure they operate at arms-length on a commercial basis. It is
anticipated that the cost of support services will be less as the companies become
more established and in particular through the high level management and
administrative support which would be provided by the holding company.

2.5.4 If other entities are to be set up under the umbrella of the holding company in due
course similar issues will arise. Examples of unlawful state aid can include providing
in kind support such as use of premises and equipment.

2.5.5 Additionally it is important to consider the totality of the Group’s activities, including
OCS and OCSH and the holding company and the interplay between them, to ensure
that these do not inadvertently impact on the reliance, in part or whole, of the Teckal
exemption at various layers within the Group structure.

2.5.6 Since there is a clear separation of activity between OCS and OCSH and provided
OCS continues to comply with the control and activity tests, providing services just to
the Council who are its sole members (or indeed other public sector bodies who may
join and receive services) legal advisors are satisfied the structure is such that there is
no need to follow a procurement process for the Council to receive services from OCS. Any change to that arrangement needs to be carefully considered because increased flexibility is likely to risk losing the Teckal status of OCS.

2.5.7 To address the points above, it would be proposed that OCS will continue to deliver only the contract with the Council. OCSH would compete for services in its own right, and not via the holding company. This would satisfy the activity test, as the holding company would only subcontract to OCS. The holding company would sell support services to OCSH but this would be less than 5% of its overall budget.

2.6 Community Interest Companies (CIC)

2.6.1 Setting up a community interest company, which can be limited by either shares or guarantee, as a wholly owned company owned by the Council is not automatically inconsistent with the Teckal exemption. Consequently, and subject to both the considerations below and the ongoing development of the objectives and structure of the Group, any combination of the holding company, OCS and OCSH could be registered as a CIC.

2.6.2 Below are some of the key characteristics of a Community Interest Company:

- Community Interest Companies (CICs) can be either companies limited by shares or guarantee.

- CICs are designed for social enterprises where it is intended that their assets are to be used for the public good.

- They are intended to operate as a company with some special features to ensure that they are working for the benefit of the community and to ensure that assets cannot be transferred or distributed (the “asset lock”), except in limited circumstances.

- It is necessary to pass a “Community Interest Test” in order to become a CIC.

2.6.3 Such organisations are expected to pursue social objectives, including regenerating disadvantaged areas, community enterprise and empowering local communities. From the perspective of maintaining the Teckal exemption it will be essential that in establishing its social purpose that the Council’s ability to have decisive influence over the strategic objectives and key decisions of the relevant entity are not compromised or otherwise fettered.

2.6.4 CICs will not benefit from the tax advantages available to charities. There are specific reporting requirements and provisions to be incorporated in the constitution, as well as extra fees payable to any regulator. It is therefore very unlikely that a holding company created through restructuring would apply for a charitable foundation.

2.6.5 There are limitations on the distribution of profits and interest on equity. The CIC sets the returns on shares, debt and debentures which are capped by regulations.

3 Options to Consider
3.1 Cabinet are asked to consider the following options given the main advantages and disadvantages presented in the tables and summaries.

3.2 Cabinet are requested to note that strategically there are few benefits from any of the options. That is, any of the company structures could achieve the adult social care remit provided to Oldham Care and Support from the Council.

3.3 The main drivers are to take advantage of the most appropriate tax efficient company structure for both the Council and OCS.

3.3.1 **Option 1: Retain current structure (The "as-is," no change)**

**Advantages**
- No cost of change
- Communications and Financial Arrangements remain as-is;
- Inspection and all returns to statutory bodies remain the same

**Disadvantages**
- Does not improve efficiency of the group

3.3.2 **Option 2: Implement a holding company (TOPCO) over Oldham Care and Support and Oldham Care and Support at Home—no Community Interest Company**

**Advantages**
- Improves the efficiency of the group

**Disadvantages**
- Potential challenges to teckal status
- Cost of change is required
- Additional audit requirements
- Need to be clear which company is responsible for what
- Efficiencies gained may be reduced if there is a change in law

3.3.3 **Option 3: Implement holding company (TOPCO) as a Community Interest Company**

**Advantages**
- Reflective of our co-operative ambitions
- Ethically bound
- Improves the efficiency of the group

**Disadvantages**
- Potential challenges to teckal status
- Cost of change is required
- Additional audit requirements
- Need to be clear which company is responsible for what
- Efficiencies gained may be reduced if there is a change in law
3.4 Preferred Option

3.4.1 The preferred option is **Option 3 – implement holding company (TOPCO)** established as a Community Interest Company or CIC.

3.4.2 The major benefits for restructuring are mainly operational and financial. This would be time limited to approximately two to three years after which it is expected that the law may change. The financial efficiencies achieved will support the delivery of the Adult Social Care Transformation programme, and will be part of the overall cost reduction envelope. A mutual organisation is not an option, as any restructured upper tiered company should not look to have a charitable foundation. Other potential benefits of this new structure include developing the strategic capacity and capability of OCS, and enhancing governance by putting the organisation(s) in a better position to sustain growth when developing new services/bidding for new work. Adopting a new structure should provide the strategic oversight required to deliver competitive growth, with added value in terms of job creation/economic benefits for Oldham.

3.4.3 It is important to note that if the preferred option is agreed, that these arrangements will be reviewed in 18-24 months-time, as the current contracting arrangements with OCS come to an end, and their services can be market tested. We have developed a set of commissioning intentions for OCS’s future service delivery, which sets out how the council wishes to shape its service delivery going forward.

3.5 Key Considerations

**Construct of the TOPCO**
- Three company model all 100% owned by OMBC
- All three companies are limited by shares. TOPCO is also a community interest company (limited by shares)
- TOPCO and OCS are teckal compliant
- TOPCO isn’t CQC registered by OCS and OCSH are
- Single board that governs the group of companies, single MD/FD – each company has its own management board which is chaired by one of the shareholders board members. Committee structure (under the main board) also includes council officers where relevant to provide increased oversight

**Financial Considerations**
- All finance and payroll systems remain on Agresso to give oversight, continued use of OMBC back account structure and audit functions
- Any restructuring must take into account the cost of change and any additional recruitment and operational costs that the companies would bear.

**Operation of contracts**
- OCS and top-co don’t compete for contracts (retains teckal compliance). OCSH competes as OCSH (not via top-co)
- Top – co holds SLA between OMBC for adult services and subcontracts with OCS for the delivery of those services. Commissioning meetings are with top-co/OCS Shared MD and SMT as they are now.

**Human Resources**
- OCS retains OMBC terms and conditions. OCSH and top-co have terms and conditions aligned to the market which are no more favourable than those in OCS and
the Council continuity of governance in relation to the companies is important, as the ultimate employer for all equal pay considerations.

Commissioning Considerations
- The Commissioning Intentions document produced by the Council is amended to indicate the likely longevity of any restructure, and clarify how social reform and demographics and finance will all play a part in decision making moving forward.

Risks
- We need to consider registration with CQC and also any additional audit requirements.
- One major risk to restructuring is when Oldham Care and Support at Home gets too big for the parent and a challenge is received over Teckal compliance of the upper tier.
- The effectiveness of the company structure will be reviewed at the annual review meeting, and any contractual risks will be monitored on an ongoing basis through the monthly client meetings.

3.6 Governance Structure

In exploring potential models to address the issues raised, it is felt that the structure presented below, provides the most effective governance arrangements for the group.

4 Consultation

4.1 Commercial Services, Corporate Governance, Finance, Property, PWC, Eversheds, Legal Services, OCS

5 Financial Implications

5.1 Capital costs

There are no capital costs relevant to the options outlined above.
5.2 **Revenue costs**

5.2.1 **Cost of change**

There are no direct costs to the Council of the change. The costs of change will be incurred by OCS.

5.2.2 **Savings and VAT**

As the holding company is not CQC registered the provision of services to the Council is subject to VAT. The Council will be charged a management fee plus VAT for the service but is able to recover all VAT costs and therefore is in no worse position. However, due to the VAT-able nature of the services the holding company is also able to recover VAT on its costs including recharges from the Council, unlike the current position for OCS. The proposed structure works as all three companies will be a group for the purposes of VAT. This means the holding company is able to then recharge costs and sub-contract the services to the other two companies but these transactions between the companies are disregarded for VAT purposes and therefore there is limited irrecoverable VAT. To note, as stated in the rest of the report, there are other reasons than those of a financial nature for setting up the holding company.

5.2.3 **Transfer pricing**

All transactions between group companies and the Council should be levied on an arm’s length basis to comply with UK transfer pricing legislation. This leads to a risk that in executing this revised structure, the Council could increase its potential corporation tax liability which could offset the benefits of reduced VAT charges.

While advice from PWC in relation to corporation tax is encouraging, Council officers have agreed with OCS that additional corporation tax advice will be sought around process and procedures to ensure Corporation tax liabilities are minimised.

5.2.3 **Processes and procedures**

There is some level of complexity with running three companies therefore it is essential that the processes and procedures are set up appropriately to mitigate any risk of challenge (for VAT purposes as well as legal, governance, state aid, procurement and corporation tax purposes). PwC as part of their commission will provide appropriate training in relation to required processes and procedures.

This will provide some assurance that the processes are set up appropriately for VAT purposes but it is important to ensure that the correct controls are in place to mitigate against the broader risks identified. In line with this, the tasks required for the transition including the setting up of a new bank account, system set up within Agresso system and discussions with Unity around the transactional processing is advised once approval for the chosen option has been confirmed.

Natalie Coates – Senior Finance Manager

6 **Legal Services Comments**
6.1 External legal advice and support from Eversheds LLP is in place to support the delivery of the Restructure. This will ensure all necessary steps are taken/documents are in place to protect the Council’s position. Eversheds are advising on procurement law, governance and state aid. They have not been asked to advise on other areas including tax law but are able to assist further as necessary. Copies of Eversheds’ advice on establishing Social Care Companies and Adult Social Care Company Structure are attached as a background paper to this report.

6.2 The report contains information as is detailed in Paragraph 3 of the revised Part 1 of Schedule 1A of the Local Government Act 1972 however this exemption is not absolute and will not survive once contractual arrangements are entered into or until such time that the public interest test weighs in favour of disclosure.

6.3 Any contracts for the supply of works, goods or services made in the name of the Council following the Restructure would need to comply with the Council's Contract Procedure Rules and all relevant EU regulations. Any land transactions would need to comply with the Council’s Land and Property Protocols.

6.4 The Council has power to take the decision/approve the recommendations detailed in the Report relying on a range of powers including the general power of competence in section 1 of the Localism act 2011 and the incidental power in section 111 of the Local Government Act 1972 combined with other statutory provisions relating to powers and duties for the provision of adult social care. (Rebecca Coldicott)

7 Co-operative Agenda

7.1 The creation of the holding company as a Community Interest Company is reflective of our co-operative ambitions and in the pursuit of social objectives.

8 Human Resources Comments

8.1 People Services have been consulted on the proposals. The setting up of a holding company will require a first or second generation TUPE dependant on the staff identified. This will be undertaken in line with the appropriate policies and procedures (Emma Gilmartin)

9 Risk Assessments

9.1 A SWOT analysis has been undertaken on the initial proposals to assess the risks to the Council. This showed that the primary advantage to the Council in setting up a TOPCO at the present time relates to potential financial efficiencies that the new group structure could achieve.

9.2 Cabinet are also requested to note that the Council has not sought approval from HMRC for this Restructure based on advice from financial advisors, namely, PriceWaterhouseCoopers.

9.3 The proposal does carry some risk of challenge from HMRC which could mean that net tax savings are not wholly achieved. Further and ongoing work will be commissioned directly by Oldham Care and Support to review processes and
procedures and to consider a broader approach to the mitigation of VAT and Corporation Tax liabilities as part of the day to day running of the company(ies).

10 Information Technology Implications
10.1 None

11 Property Implications
11.1 None

12 Procurement Implications
12.1 The EU directives codify the 1999 Teckal case and latterly by the 2009 Hamburg Waste case law and confirm that in respect of the Teckal exemption, an authority may contract with another public body, quasi-public body or other supplier, such as a shared services company subject to compliance with several conditions.

12.2 The new EU directives (not yet enacted) go further than current case law in allowing the Teckal entity the ability to derive up to 20% of its turnover from activities with entities other than the controlling authority. The current directives limit this to 10%. The new EU Directives are expected to be formalised in the UK by the end of 2014. Special care will be needed to monitor activities so the thresholds described here are no breached, or mitigation is put into place such that if they are breached, the Council as parent of Oldham Care and Support are made aware. This will be done though the governance arrangements being designed by Commercial Services.

12.3 The new EU directives state that:
- The separate body must be controlled in a similar way to the contracting authority’s control over its internal departments;
- the separate body must carry out 80% of its activities with its controlling public body;
- there is no direct (with very limited exceptions unlikely to be relevant often in the UK) private capital participation

Karen Lowes – Head of Sourcing

13 Environmental and Health & Safety Implications

None

14 Equality, community cohesion and crime implications

None

15 Equality Impact Assessment Completed?

No. The proposals within this report will not change the scope or nature of services being delivered to disadvantaged groups.
16 Key Decision

Yes

16.1 Key Decision Reference

ASCPH-03-14

17 Background Papers

17.1 The following is a list of background papers on which this report is based in accordance with the requirements of Section 100(1) of the Local Government Act 1972. It does not include documents which would disclose exempt or confidential information as defined by the Act:

- Eversheds Advice to OMBC on establishing Social Care Companies
- PWC Advice to OMBC on Vat Implications

Ends