

THE HIGHLAND COUNCIL
EDUCATION, CULTURE AND SPORT COMMITTEE

14 JANUARY 2010

Agenda Item	
Report No	

Significant Trading Operations

Report by Director of Education, Culture and Sport Service

Summary

This report reviews the Catering and Cleaning trading activities and considers whether or not both activities continue to satisfy the definition of significant trading operations as approved by the ECS Committee in March 2004. If neither activity satisfies this definition then Members are asked to agree that the maintenance of trading accounts for the Catering and Cleaning activities cease with effect from 1st April 2010.

This report contributes towards the following outcome in **Strengthening the Highlands:**

- We will continuously review our performance to improve the way in which Council services are designed and delivered. We will do this by measuring our progress, reporting on it publicly and listening to our customers and communities.

1. Background

- 1.1 The ECS Committee on the 17th September 2009 agreed that "...on the basis that the Catering activity is becoming inextricably linked with the delivery of the curriculum through statutory health promotion and nutrition requirements the statutory obligation to produce trading accounts on a commercial basis be reviewed in conjunction with the Depute Chief Executive & Director of Finance and Audit Scotland...". In the intervening period it was also felt appropriate to include the Building Cleaning activity as part of this review.
- 1.2 On this basis, this report examines both the Schools & Welfare Catering (hereafter referred to as Catering) and Building Cleaning (hereafter referred to as Cleaning) functions and considers whether or not both activities continue to satisfy the definition of significant trading operations as approved by the ECS Committee in March 2004.
- 1.3 The Catering function has been delivered by the in-house provider for approximately 20 years, with the exception of the Lochaber area where a private sector operator provided the service between 1997 and 2006. The private sector operator relinquished the contract voluntarily in 2006. The Cleaning function has been delivered by the in-house provider since 1991. Throughout the period in question both functions have been subjected to a compulsory competitive tendering process.
- 1.4 The budgeted income for the Catering function in 2009-10 is £9.360M. The corresponding figure for the Cleaning function is £5.381M.

- 1.5 It was agreed by the ECS Committee in September 2009 that a Catering and Cleaning Best Value Report would be produced annually and reported to Committee.

2. Requirements of the Local Government in Scotland Act 2003

2.1 The Local Government in Scotland Act 2003 sets out a statutory duty of Best Value and provides a strong link between the duty of best value, the delivery of services and the duty to publish performance reports and includes provision for the publication of trading accounts.

2.2 The test of what is a trading operation is based on whether or not an activity meets both the following criteria:

- The activity is provided in a “competitive environment”, and
- The activity is provided on a basis other than a straightforward recharge of cost

The definition of competitive environment is not explicit in that neither the legislation nor the related guidance provides full clarification. On this basis, any test of what is a trading operation is likely to be fairly subjective.

2.3 The Act requires trading accounts to be maintained for “significant trading operations” and that they should break even over a 3 year period. The test of significance is important as it determines which trading operations are required to maintain a statutory trading account. Critically each local authority is permitted to set its own parameters for significance.

3. Definition of Significant Trading Operation

3.1 The parameters for Highland Council as approved by the ECS Committee in March 2004 are as follows:

- A trading activity with an annual turnover of 1%, or greater, of the (Highland Council) Net Revenue Budget will be considered significant.
- A trading activity, the performance of which may materially impact on the Council’s reputation, will be considered significant.
- A trading activity, which exposes the Council to material financial loss, will be considered significant.
- A trading activity likely to be of interest to key stakeholders will be considered significant.

3.2 A trading activity should meet at least 2 of the final 3 bullet points before being considered significant.

4. Do the Catering and Cleaning functions comply with this definition?

4.1 Performance in the public sector is increasingly measured by outcome targets and the ability to measure improvement against these targets on an on-going basis. Improved efficiency and effectiveness can therefore be demonstrated by the measurement of performance against more challenging targets on an on-going basis. This approach therefore focuses on the outcomes achieved from the

effective deployment of all resources available to managers. This approach can be further extended by bench-marking the performance of the Highland Council Catering and Cleaning functions against similar activities in local authorities across Scotland.

- 4.2 Effective utilisation of resources and achieving value for money can therefore be demonstrated by creating the appropriate outcome targets and re-assessing those on an annual basis. This approach has the benefit of providing management with a clear direction that, if delivered, will result in improved services on a continuous basis over a period of time. Conversely the justification for maintaining an “artificial competitive entity”, that has to bear a share of support service costs that it cannot influence, has to be challenged within the above framework.
- 4.3 It is proposed therefore that the original basis for demonstrating Best Value, as defined in the 2003 Local Government in Scotland Act is revisited.
- 4.4 The Catering function has become inextricably linked with statutory and policy requirements to improve the health and well-being of pupils. In addition an awareness of diet and nutrition are regarded as an integral part of a Curriculum for Excellence under the Health and Well-being heading. The challenges presented by changes in legislation and government policy, including the Schools (Health Promotion and Nutrition) (Scotland) Act 2007 and the Concordat commitments to extend the provision of free school meals, have had a significant impact on the Catering function. For example the introduction of the Health Promotion and Nutrition legislation has resulted in a reduction of almost 1,000 school meals per day. In addition food costs have increased as a result of the requirement to meet specified statutory nutritional requirements. Also there is an increasing demand to utilise local suppliers and producers for the provision of foodstuffs which conflicts directly with the purely commercial benefits achieved from competitively awarded contracts for foodstuffs.
- 4.5 For the above reasons it is debatable whether or not the Catering function is actually operating in a true “competitive environment” per the definition of a trading activity outlined in paragraph 2.2 above. Increasingly the Catering function is more about delivering outcomes that focus on qualitative factors and less on strictly commercial factors based on quantitative factors, in particular achieving a break-even position over the average of 3 financial years. This latter factor is no longer the sole focus of the Catering function as factors that deliver improved outcomes for the health and well-being of our children are accorded a higher priority. As further evidence of this no private sector catering company provides school meals in any Scottish local authority, other than those inextricably linked with facilities management functions in PPP schools.
- 4.6 The current annual turnover of the Cleaning function is £5.381M which is 0.90% of the Highland Council Net Revenue Budget. On this basis alone the Cleaning function does not meet one of the parameters that determine a significant trading organisation. In addition it is important that the primary focus of the Cleaning function relates to qualitative factors that ensure that the school/working environment is maintained at the appropriate levels of hygiene and cleanliness.

- 4.7 In addition, both the Catering and Cleaning functions have contributed to the ECS budget savings targets and corporate improvement programme savings in recent financial years.
- 4.8 It is proposed therefore that the Catering and Cleaning functions are no longer regarded as trading activities and instead operate on a cost recovery basis. As a result there would no longer be a requirement to maintain trading accounts and to maintain an artificial Client/Contractor split, both structurally and from an accounting perspective.
- 4.9 This proposed change in accounting arrangements would continue to provide management with financial information in relation to detailed expenditure and income recharged. However, in future these accounting arrangements would be simplified as all relevant transactions would be contained within single sets of accounts. It is proposed therefore that Members agree that trading accounts should no longer be maintained for the Catering and Cleaning functions. If this proposal is agreed then there would be implications for the current structural arrangements that require the Catering and Cleaning manager to operate on a dual basis. In future there would be no requirement to operate separate Client and Contractor functions.

5. Demonstrating Best Value

- 5.1 If the proposal to remove the requirement to maintain trading accounts is approved then it is important that both the Catering and Cleaning functions can demonstrate that best value is being achieved for the Council on a sustainable basis. The framework for achieving this objective will be delivered via:
- A Service Level Agreement that will outline the standards of service that will be provided, including a very strong focus on customer satisfaction surveys.
 - User groups that will provide the appropriate forum for discussing service delivery issues and provide the appropriate feedback to inform improvement.
 - An improvement plan that will be informed by a self evaluation process that identifies strengths and weaknesses associated with service delivery based on the evidence provided by customer surveys, user group feedback and key performance indicators.
 - Key performance indicators that are informed by a combination of statutory performance indicators, legislative and government policy requirements, the respective industry standards and the policy requirements of the Highland Council.
 - Publication of key performance indicators that will be reported to the ECS Committee on annual basis, including comparative analysis with other local authorities and identifying internal performance trends in comparison with previous financial years.
- 5.2 The above performance framework will focus on a combination of qualitative and quantitative factors that will measure outcomes achieved on an annual basis. At that time proposed alterations to the key performance indicators will be submitted to Members for consideration.

6. Summary

- 6.1 On the basis of the above analysis, it can be demonstrated that the delivery of the Catering, in particular, and Cleaning functions has changed since significant trading operations were originally defined by the ECS Committee in March 2004, as outlined in paragraphs 3.1 and 3.2 above.
- 6.2 The evidence in support of this statement can be summarised thus:
- The Catering function is not operating in a “competitive environment” on the basis that it has to increasingly comply with the qualitative impact of statutory, national government and local government policy requirements.
 - Both functions operate more on a cost recovery basis than the strict commercial basis on which a true trading activity would operate. This is evidenced by the fact that both functions have made significant contributions towards ECS budget savings in recent years.
 - For the above reasons it is debatable whether or not the Catering and Cleaning functions are truly “trading activities” and as such no longer satisfy the criteria as significant trading operations.
 - The Cleaning function is not material in the financial sense in that its annual turnover is less than 1% of the Council’s Net Revenue Budget which is identified within the original definition as a prerequisite of a “significant trading operation” as defined in paragraph 3.1.
- 6.3 The financial performance of the Catering and Cleaning functions will continue to be monitored closely within the Service’s robust budget monitoring framework. The main difference in future, if this proposal is accepted, is that the financial management will be greatly simplified by removing the need to maintain separate Client and Contractor financial statements.
- 6.4 The critical factor in future is the move towards demonstrating that value for money is being achieved by focusing on the performance measurement framework outlined in section 5 above under-pinned by strong financial management.
- 6.5 Colleagues in the Finance Service been consulted in relation to this report and their views have been incorporated.
- 6.6 Whilst Audit Scotland will not comment specifically on the content of this report it is anticipated that they will be interested in the outcome of this decision and, if approved, will closely examine the proposed changes prior to implementation.

7. Recommendations

7.1 Members are requested to:-

- Note that the current Catering and Cleaning trading activities no longer comply with the definition of significant trading operations as outlined in section 3 of the report.
- Agree that with effect from 1st April 2010 the requirement to maintain statutory trading accounts for the Catering and Cleaning functions should cease and that instead the delivery of best value by the Catering and Cleaning activities could instead be demonstrated by the measures out-lined in section 5 of the report.

Signature:

Designation: Director of Education, Culture and Sport

Date: 23rd December 2009.

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