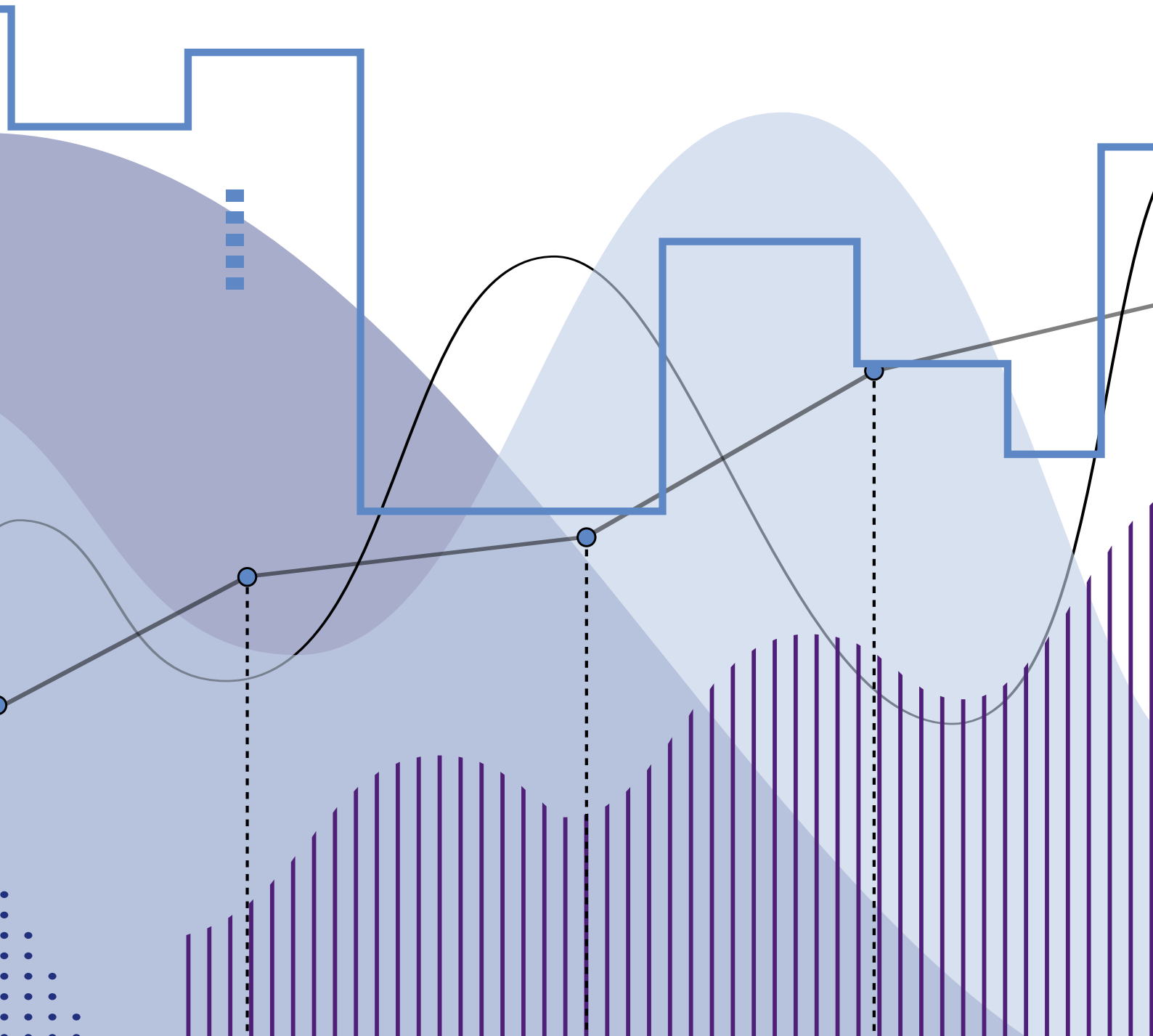


# Shared services toolkit

Delivering services differently



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*“Over the last two years we have undertaken a series of discussions and wide reaching surveys to gain a deeper understanding of how the public sector approach service delivery, particularly in respect of shared services. This has been a fascinating insight into how the public sector delivers services day to day and we hope this toolkit acts as both a guide and a useful checklist to achieve successful and collaborative shared service delivery.”*

Lucy Doran

## Introduction

Over the last two years, we have been running a series of events and publications to better understand how public sector service delivery is changing to adapt to an ever changing landscape. Some of these challenges have been foreseeable such as reductions in budgets and spending, changes in legislation and an increased focus on factors such as social value and net zero, however, other events have been unforeseeable – namely the huge impact that the covid pandemic has had on businesses and the financial uncertainty caused by the war in Ukraine, political changes in the UK and soaring inflation.

For those of us who advise on and set up public sector service delivery structures, there has been a noticeable shift in the last two years in how the public sector approach service delivery, particularly in respect of shared services. This was reinforced by the results of our “Delivering public sector services differently” survey, published in November 2021.

There has been increasing interest in models which involve organisations across the wider public sector rather than just two or more organisations in the same sector. An example of this has been in the affordable housing and accommodation sphere, registered providers, NHS Trusts and local authorities have all had to look at new and innovative ways to solve their individual requirements and often, teaming up can be a viable solution.

Despite an increase in interest in shared services models generally, there were some very candid responses from those who were involved in existing shared service arrangements which goes to demonstrate that there are still challenges and obstacles that need to be overcome. In our experience (and reinforced by the survey comments), the more time and resources that can be deployed upfront in aligning the parties on core objectives and aspirations, the greater the odds that the shared service arrangement will be successful.

The aim of this toolkit is to explore the shared services models available and their legal basis and look at some of the key questions that need to be asked early on to ensure that the parties are compatible and share the same objectives. We understand from the Cabinet Office that the forthcoming Procurement Act has been drafted with the intention of reflecting the law presently in force under the Public Contracts Regulations 2015. All forms of shared services mentioned in this toolkit have been included in the Procurement Act. Any changes as a result of the new Act would be due to the use of UK statutory language and interpretive difference to EU statutory language. We have included what we know so far from the Procurement Act and will update the toolkit once the Act comes into force.

We hope that this toolkit is helpful and aids the conversation around shared services and the wider public sector service delivery piece. As always, we welcome any comments and suggestions and look forward to your involvement in future events and publications on this public sector service delivery series.



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# Shared services – the legal basis

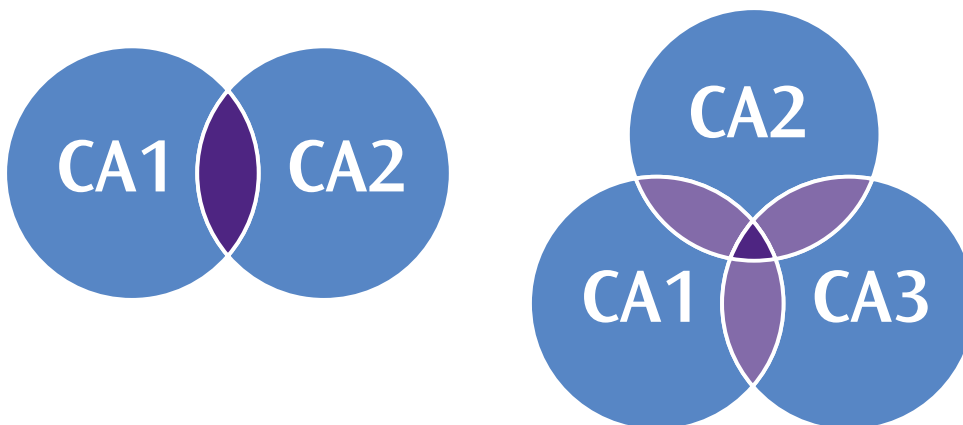
## Current position (pre- Procurement Act)

A “shared service arrangement” is a term which is loosely used to describe a situation where two or more public sector bodies work together to deliver services. Such an arrangement can fall outside of the current procurement rules as long as certain conditions are met. There are two types of shared services model that we consider in this report:

- Services to two or more parties delivered purely through a contractual arrangement (contractual shared service); or
- Two or more parties establish a legal vehicle which then delivers services to those parties and sometimes vice versa (corporate shared service or joint Teckal).

Both models permit the same services to be delivered to third parties which allows for a modest additional income stream for the parties involved.

## Contractual Shared Service



A contractual shared service arrangement falls outside of the procurement rules where the following conditions are met:

- The contract establishes or implements a co-operation between the participating public bodies with the aim of ensuring that public services they have to perform are provided with a view to achieving objectives they have in common;
- The implementation of that co-operation is governed solely by considerations relating to the public interest; and
- The participating public bodies perform on the open market less than 20% of the activities concerned by the co-operation.

As can be seen, this type of model needs to be a genuine sharing of services and not an outsourcing of one or more services to another public body. Previous guidance from the European Commission also indicated that such models should not be used to create a profit and charges should be on a cost recovery basis only. Post-Brexit, it is not known whether the UK Courts would uphold this guidance so until we get a clearer understanding in respect of the Procurement Act and any Regulations issued in respect of these exemptions, we would continue to work on a cost recovery only basis.

## The Procurement Act

The Procurement Act uses simplified language to refer to this procurement exemption, now termed “horizontal arrangements” (in Schedule Part 1 for Counterparty Exempted Contracts). These are described as arrangements between contracting authorities with the aim of achieving common objectives within their public functions and solely in the public interest. No more than 20% of the activities covered can be carried out other than for the purposes of the authorities’ public functions. These conditions accord with existing rules save for awaited clarification on previously understood rules on no profit arising in the arrangement and no full outsourcing to another local authority.

### Contractual Shared Service:

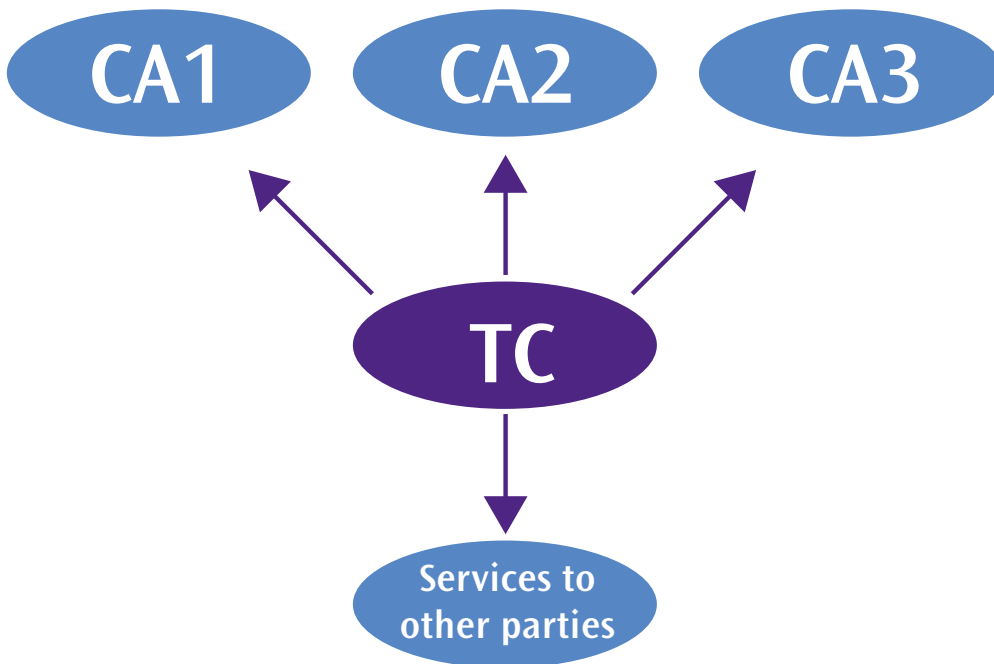
#### Documentation checklist:

- Shared service agreement

#### Analysis checklist:

- Implementation plan/financial model takes into account limits on (i) open market trading and (ii) pricing/charging
- All participating parties will contribute towards delivery of the shared service (more than just financially)
- A “host” authority is identified for staff, contracts, etc. The host understands their duties and how their costs are identified and shared
- All parties understand the structure of the shared service agreement and governance thereunder
- All parties have modelled the cost/benefits of the proposed model as opposed to existing delivery. Savings/benefits are not be assumed
- Each party’s decision making body has approved the entry into the relevant documents on an informed basis

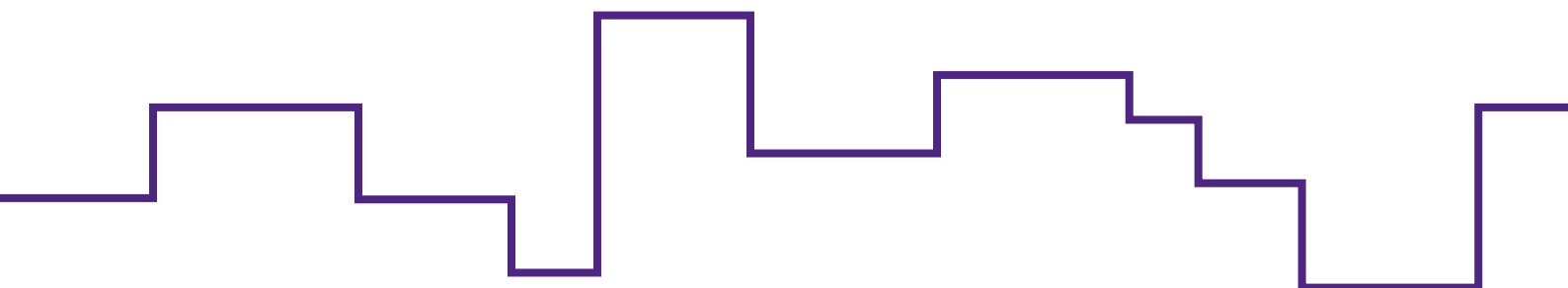
### Corporate Shared Service Joint (Teckal)



An alternative model that can be used for shared services is where two or more public bodies establish a legal corporate vehicle (usually a company) and then this vehicle delivers services back to the original public bodies. This type of arrangement is often referred to as “joint Teckal” named after the European case that originally set out the conditions for the exemption. For the arrangements to sit outside of the procurement rules, the following conditions must be met:

- the contracting authorities exercise a requisite level of joint “control” over the Teckal entity as follows:
  - The decision making body of the Teckal entity must be composed of representatives of all the participating contracting authorities;
  - The contracting authorities jointly exert decisive influence over the strategic objectives and significant decisions of the Teckal entity; and
  - The Teckal entity does not pursue any interests which are contrary to those of the participating contracting authorities.
- More than 80% of the activities of the Teckal entity must be for the contracting authorities; and
- There is no direct private capital participation in the Teckal entity.

The rules do not specify the amount of services that each participating contracting authority must receive from the Teckal entity nor is there any restriction on making a profit so in this respect it can be viewed as more flexible than the contractual model although the administrative time and costs in running a separate legal vehicle must be considered.



## The Procurement Act

As per the co-operation provisions outlined above, the Procurement Act seems to largely update terminology to UK law concepts (eg. references to the Companies Act 2006 rather than EU law concepts of related companies). This broadly provides for the same coverage of exempted contracts as currently in place regarding the joint 'Teckal' model – which will be known as “vertical arrangements”.

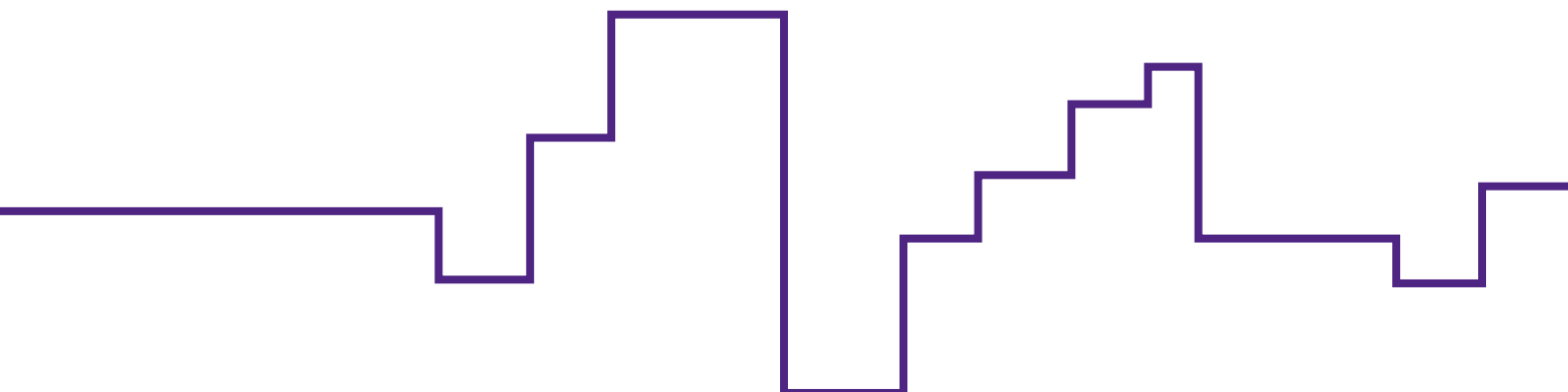
### Joint Teckal entity:

#### Documentation checklist:

- Company Articles of Association/LLP Agreement
- Shareholders Agreement / Member Agreement
- Services Agreement (potentially services both ways)
- Working Capital Facility Agreement may be required
- Admissions Agreement (where LGPS employees transfer)
- Consider a Business Plan
- Consider company policies
- Consider governance handbook

#### Analysis checklist:

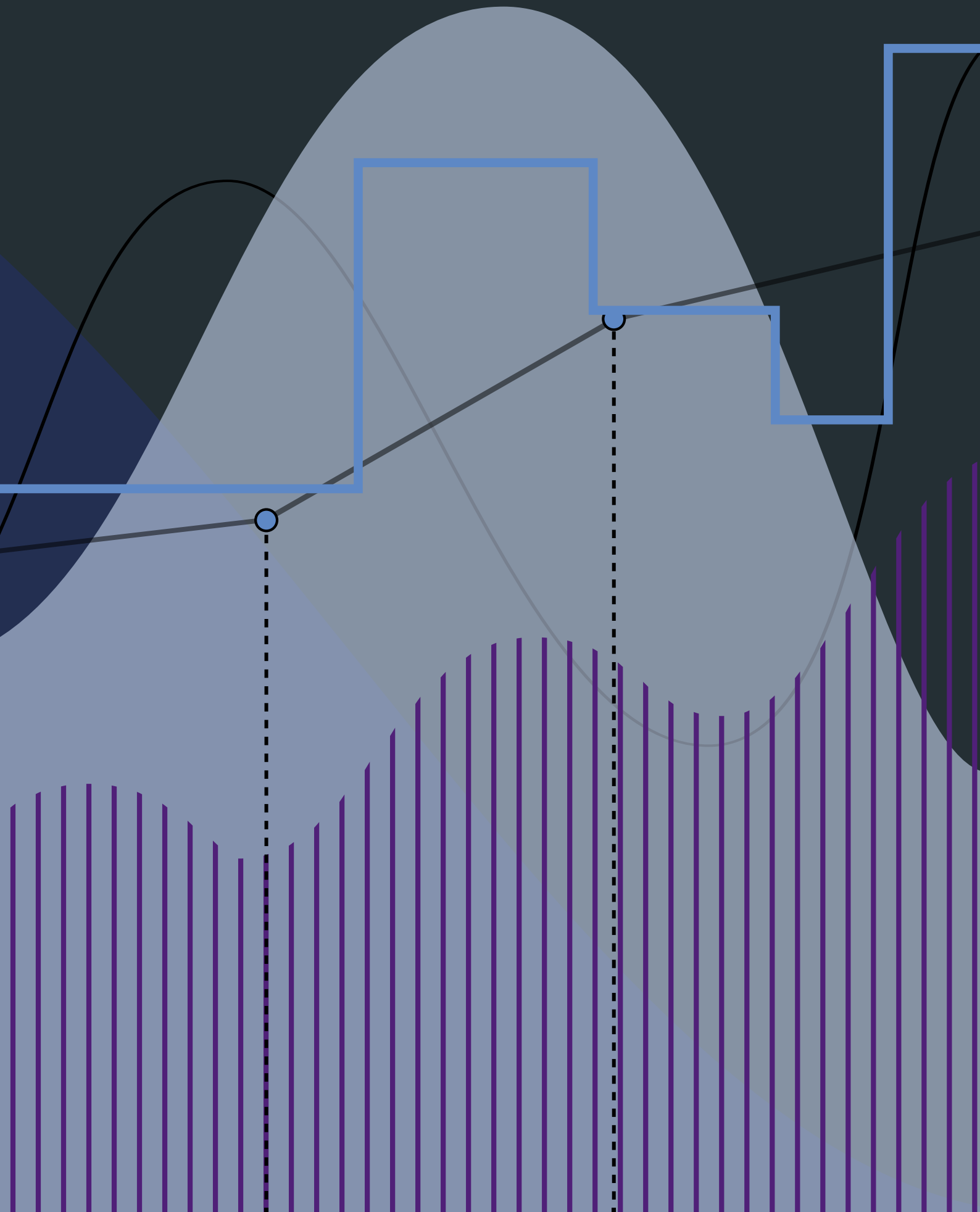
- Business plan takes into account 20% open market trading limit
- Hold TUPE consultation (if staff transferring) and understand pensions liabilities and requirements
- Consider if shareholders need to provide back office services to the Teckal company
- Consider if any assets/contracts should be novated
- All parties understand the Business Plan, including the risks involved, financial requirements and governance (eg. shareholder nominated directors and reserved matters approvals)
- All parties appreciate the different bureaucratic requirements of administering a company
- Scope for exit and addition of new parties
- Each party's decision making body has approved the entry into the relevant documents (including potential consideration of a business plan) on an informed basis



# Comparison of Contractual Shared Service v Joint Teckal

Consideration	Contractual Shared Service	Corporate Shared Service Joint Teckal
<b>Nature of services delivered</b>	Needs to be driven by shared public services and public interest considerations. This may limit commercial activities.	Can be wider and there is no requirement to show a link to shared objectives and public interest considerations.
<b>Volume and split of services</b>	There needs to be a genuine cooperation and sharing of services not just an outsourcing of services from one contracting authority to another.	As long as joint control can be demonstrated, the volume of services to each contracting authority can vary.
<b>Set up costs</b>	Cost of agreeing contractual terms and services agreement with other partners	Cost of agreeing governance agreement and services agreement with other partners. Additional cost of setting up and administering a separate legal entity.
<b>Cost recovery/Profit</b>	Only recovery of costs permitted from other authorities who are party to the arrangements. There is a 20% limit on services to other parties.	No procurement restriction on making a profit. There is a 20% limit on services to other parties.
<b>Control</b>	Control can be agreed and established through the contractual terms (e.g. memorandum of understanding or inter-authority agreement).	Control can be agreed and established through the governance arrangements.
<b>Risk</b>	Risk will need to be shared and borne by each contracting authority in accordance with the terms of the contractual arrangements.	Risk can be ring-fenced to an extent through the separate legal entity.
<b>Employment of Staff</b>	Can allocate staff to the service and second staff. As there is no entity created, staff would need to be employed by one of the contracting authorities.	The entity can employ staff directly and staff can be transferred and seconded to the entity.
<b>Property and contracts</b>	There could be a "host contracting authority" which will enter into contracts and provide facilities or this role could rotate between authorities. Any liability will need to be addressed in the contractual documents.	The legal entity can enter into contracts in its own right.





# Employment considerations

Employment considerations will depend on the model for shared services being used.

If a new entity is being created to provide the services and employ the staff then TUPE will apply. It will also apply in a situation where one public sector body is taking on responsibility for the provision of the services on behalf of the others.

## TUPE

The Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE) apply where there is either a “transfer of an undertaking” or a “service provision change”. Where services currently provided by one of the bodies are transferred either to a host body or to the new entity, there is likely to be a service provision change if the fundamental nature of the services remains the same.

### Effect of TUPE

The employees who are assigned to the transferring services will transfer to the new service provider unless they object. The new employer will inherit the contracts of employment of the employees who transfer, along with all pre-existing employment rights and liabilities.

### Information and consultation

The outgoing employers will be under an obligation to provide information to the new employer about the employees transferring under TUPE. The new employer must notify the outgoing employers of any “measures” that it envisages (for example any redundancy or planned changes to terms and conditions). The employers must inform and/or consult the employees about the fact and implications of the transfer and any measures.

### Changes prior to or following the transfer

Where TUPE applies, the relevant employers are prevented from dismissing employees or from implementing changes to terms and conditions which are because of the transfer. Such dismissals are automatically unfair and any such changes to terms are unenforceable.

An employer can make changes which are for a reason connected to the transfer, provided that the reason for the dismissals or changes is an “economic, technical or organisational reason which entails changes in the workforce” (ETO reason). It is essential that any employer looking to implement changes before, on or after a TUPE transfer has a robust business case to explain and justify the proposals and that those proposals satisfy the test for an ETO reason.

### Redundancies and restructures

There may be a need to streamline operations. As discussed above, it’s possible to dismiss employees who are affected by TUPE by relying on an ETO reason where any redundancies or restructures are likely to take place.

Any restructure, including one which involves a redundancy situation, must be implemented fairly. The separate bodies will also need to comply with their own redundancy policies including any redundancy entitlements. The process will require

cooperation between the bodies to identify which employees should be aligned or ringfenced to any roles in the new structure whether that is with a host body or the new entity.

### Harmonisation and equal pay

The new employer will inherit employees on different sets of terms and conditions of employment. TUPE generally provides a defence to any equal pay or discrimination claims which arise out of comparisons between different sets of terms and conditions in the hands of a new employer.

Harmonisation of terms and conditions is not a valid ETO under TUPE. However, there may be situations where harmonisation can be lawfully achieved.

## Alternative employment models

### Secondment

Secondment is a possible alternative to TUPE. It is not without legal risk, and ideally any secondment should be implemented by way of a secondment agreement and the employee objecting to any TUPE transfer.

### Joint employment

Another alternative is joint employment. Joint employment is an arrangement where an employee is employed by more than one employer. The joint employers are jointly and severally liable for all employment liabilities to that individual employee, and the employee in return can work for each or all joint employers. Again it comes with benefits and potential downsides.

## Employment / Personnel matters:

### Documentation checklist:

- Services Agreement (TUPE and pensions drafting – inc. potentially risk share)
- TUPE consultation documents
- TUPE List
- Admission Agreement (LGPS)
- SLA – for parent services
- Joint employment contracts
- Secondment Agreements

### Analysis checklist:

- Consider if TUPE will apply early – consider those who might have TUPE rights
- Factor TUPE into financial modelling
- TUPE consultation included in project plan
- Identify equal pay issues and harmonisation methods (if applicable)
- Consider statutory restrictions on outsourcing certain positions
- Consider cultural alignment between separate teams that may be merging or forming

## Vires considerations – local authorities

There are a number of models available under the Local Government Act 1972, including the delegation of functions, the establishment of joint committees, and the sharing of staff. Sharing services can help achieve economies of scale, but local authorities generally remain individually responsible for ensuring that their functions are carried out properly. In this report we have focussed on the contractual shared service arrangement and the corporate or joint Teckal shared service arrangement.

Local authorities are statutory bodies created by Acts of Parliament. Therefore, unlike individuals or commercial businesses, local authorities may only act in ways which Parliament permits. Behaving in a way which is not authorised by legislation can lead to decisions and actions of local authorities being vulnerable to legal challenge by the individual or business affected by the decision, by solicitors or by any aggrieved party who has a right to do so if a decision is outside the authority's powers.

The use of alternative delivery vehicles can sometimes be controversial, with some elected members, citizens, trade unions and other interest groups viewing the arrangements as akin to privatisation and private sector businesses concerned that a company will enjoy an unfair competitive advantage.

Challenges to proposals could take the form of judicial review actions claiming that the authority which established the vehicle has acted ultra vires. If arrangements are found to be ultra vires, the court can rule that they have no legal effect, damages may be payable to parties who have suffered a loss and the authority will be liable for the challenger's legal costs. Similar outcomes may arise through challenges under procurement or Public Subsidy law.

Local authority elected members and officers should also be aware that the responsibility for the proper and lawful performance of services remains with the authority whatever external delivery structure is established, meaning that it is the reputation of the local authority that is in jeopardy in the event of a failure. Careful consideration at the planning stage together with a sensible governance structure that balances supervision with commercial freedom is vital to reduce this risk.

Over the years, this led to much confusion about what local authorities could, or could not, do to transform their services. In recent times, there have therefore been moves to give local authorities much more general powers to use as they choose.

### The general power of competence

This culminated in the Localism Act 2011, which gives local authorities a 'general power of competence', which was intended to give local authorities similar broad powers as individuals and to allow them to carry out any lawful activity.

Much has been written about the general power of competence and the opportunities it brings. There are three important provisos:

First, if a local authority is using the general power to do something for commercial purposes, it must do so through a company.

Secondly, a local authority cannot carry out an activity commercially using the general power if the activity is something that the authority is required to provide as part of its statutory duties. This prevents local authorities switching required statutory activities to commercial ones. Neither may local authorities charge for services using the general power if separate statutory provision has been made for how charges should be structured: the general power does not allow for those charging schemes to be rewritten.

Thirdly, despite the breadth of the general power, local authorities cannot use the power to circumvent any prohibitions on how they carry out their activity which were introduced prior to the Localism Act 2011 coming into force, i.e. the general power of competence did not repeal previous statutory restrictions on what local authorities could do.

Local authority trading companies (LATCs): A company set up by one or more local authorities to carry out activities on their behalf. LATCs may be established as companies limited by guarantee or companies limited by shares, with the latter more usual where profit generation or incoming new shareholders are expected, or where it is desired to leave flexibility for either in due course.

The LATC model can accommodate numerous variants such as a community interest company, an employee mutual, a community benefit society, a charitable incorporated organisation, a charity and a joint venture with a private sector interest or contractor (to name just a few options). The suitability of the particular form of corporate vehicle will depend on a number of factors including policy and commercial objectives and who will be investing in the LATC.

It should be noted that section 2 of the 2011 Act limits the exercise of the general power of competence where it “overlaps” with a power which predates it (identified as the third of our provisos above). This includes the Council’s power to trade under section 95 of the Local Government Act 2003 (the 2003 Act). It would be prudent therefore for a local authority establishing a joint Teckal vehicle (which might at some point be engaged in trading) to comply with the requirements and limitations to which section 95 is subject. These are set out in Regulation 2 of the Local Government (Best Value Authorities) (Power to Trade) (England) Order 2009 (the 2009 Order) which requires a business case to be prepared and approved by the Council before a company starts trading. The 2009 Order also provides that the Council must recover the costs of accommodation, goods, services, staff or any other thing that it supplies to a company to facilitate its power to trade.

### Vires matters:

#### Documentation checklist:

- Options appraisal
- Internal reports and legal implications – supporting the vires justification
- Business case – consider if business case required for sign off
- Legal sign off / vires audit

#### Analysis checklist:

- Identify parameters/restrictions of options early
- Identify the purpose for which you are acting
- Supportive audit trail from options through decision making

## Vires considerations – housing associations

From our experience shared services in housing associations are less common than in local authorities, perhaps due to local authorities having been under a degree of pressure to cut costs since 2010 which mandated different ways of working across the public sector. Housing associations, more likely in the not-for-profit space, are adept at collaborative working (more so than in the for-profit sector) with quite a few examples of shared services in the repairs and maintenance space often due to VAT efficiencies.

Whilst housing associations tend to have fewer statutory restrictions on how they structure their trading activities per se, the lion's share of not-for-profit housing associations are subject to charity law, either as incorporated charities or exempt charities (community benefit societies). As a result vires needs to be carefully navigated when setting up a separate vehicle, especially with regards to financing.

If the shared service will be incorporated through a joint-vental profit-making subsidiary then the parent housing associations need to consider on what basis the subsidiary is being financed. For example, if the parents provide loans to the subsidiary as working capital, and the subsidiary shall use the funds to build a profit-making business providing R&M services, the parent will likely need to demonstrate that the loan is a genuine financial investment.

Housing associations will also have funders to consider. Loan agreements often include various covenants around granting loans and setting up subsidiaries. Whilst not a statutory or vires point – housing associations may need to apply for consent from their lenders or operate within covenants (for example in relation to limited on-lending).

## Vires considerations – NHS Trusts

Many of the factors addressed above will apply to NHS Trusts. One element which is unique to the NHS is that NHS England has issued guidance on forming or changing a subsidiary. This will obviously impact on any Teckal entities that need to be set up.

The guidance (last updated in October 2022) states that all subsidiary transactions (regardless of their size, legal structure or purpose) are 'reportable' to NHS England and will require a trust-approved business case to be reviewed by NHS England.

The Addendum to the guidance sets out the powers of NHS foundation Trusts and NHS trusts. NHS foundation trusts have power to set up subsidiary companies for the purposes of, or in connection with, the exercise of their functions and they may also form them for income generating purposes.

NHS trusts have more limited powers to participate in a subsidiary company and must demonstrate that participation is for income generating purposes only and this is by performing non-NHS services. Proposals for income-generating NHS trust subsidiaries must have Secretary of State consent pursuant to directions to NHS trusts dated September 2002.

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