

Report for: Service Delivery & Continuous Improvement PDG

Date of Meeting: 24 June 2024

Subject: Extending the Fleet Contract with Specialist Fleet Services

Cabinet Member: Cllr Josh Wright, Cabinet Member for Environment and Services

Responsible Officer: Darren Beer, Operations Manager – Street Scene and Open Spaces
Matthew Page, Head of People, Performance and Waste

Exempt: Appendixes A-D
These are Exempt from publication under paragraph 3, Part 1 of Schedule 12A to the Local Government Act 1972 (as amended) as it contains information relating to the financial or business affairs of any particular person (including the authority holding that information)

Wards Affected: All

Enclosures: Appendix A: Contract Extension Summary
Appendix B: Lease vs Purchase Capital Costs
Appendix C: Internal Borrowing vs SFS Lease Comparison
Appendix D: PWLB vs SFS Lease Comparison

Section 1 – Summary and Recommendation(s)

The Service Delivery and Continuous Improvement PDG are asked to consider the report and recommend to Cabinet to approve the decision to extend its current contract regarding its fleet provision with SFS (Specialist Fleet Services Limited), which will future proof and further cement the successful partnership. An effective fleet will help deliver quality, efficient and sustainable services to the residents of Mid Devon. It will help the Council continue to transition towards net zero, supporting Mid Devon to use low and zero emission vehicles. If approved, the contract would terminate in June 2033 and will continue to be reviewed regularly.

Recommendation that Cabinet be asked:

- 1. To approve the decision to extend the contract with SFS (Specialist Fleet Services Limited) for a further seven year period to cover 2026-2033 at the earliest possible opportunity.**
- 2. To include lease borrowing in the Capital Programme.**
- 3. To authorise the negotiation of the removal of the indexation rate from the master contract for all new vehicles as soon as possible and replace it with a fixed rate for the term of the individual contract.**

Section 2 – Report

1.0 Introduction – the request to extend the SFS Contract

- 1.1 This report requests for members to give permission for a potential extension to the existing fleet contract with SFS. It includes both the vehicles for the General Fund and the Housing Revenue Account (HRA). The report also considers the performance of the contract and areas where operational efficiencies could be achieved and further improved.
- 1.2 The specification for the original contract was published in 2018 with six suppliers submitting a completed questionnaire. Of these six suppliers only two submitted formal tenders. The Council awarded the fleet supply and maintenance contract to SFS on 03 June 2019 for an initial seven year term to 02 June 2026 with an option to extend for a further seven years as a secondary term. **Appendix A** contains the contract hire information from the original schedule and includes financial information for the primary, transitional period and secondary term to compare.
- 1.3 The indicative pricing given is correct at the time the information was provided in May 2024 and the new approach, if approved, would be implemented as of the 01 April 2025. It will give the Council the ability to more accurately budget based upon knowing what the future costs will be.

2.0 The Reasons to Extend the Contract with SFS

- 2.1 There are a number of reasons why the Council wishes to extend its contract with SFS. SFS are a wholly owned subsidiary of Paragon Bank PLC with 30 years' experience of fleet and workshop. This gives the Council greater stability and confidence regarding the service provision we are receiving. SFS currently work with 30 different local authorities across the UK including Exeter, Teignbridge (over 20 years) and North Devon (since 2021), and so are familiar with our local area.

- 2.2 SFS are able to offer the wide range of operational vehicles that the Council requires where many of their competitors are limited in the types of vehicles they are able to supply. SFS have significant buying power with manufacturers and influence over the supply chain which results in improved operational performance for the Council and the services we deliver.
- 2.3 This also helps the Council when in an emergency situation such as the COVID-19 pandemic. For example, SFS were able to use their purchasing leverage and position in the market to ensure the Council received the vehicles at the time we required in a competitive market (and where other industry orders for vehicles were being cancelled). It also helps the Council achieve better value for money in terms of us being able to obtain what we need at the time we need it.
- 2.4 The Council requires a particular range of regular and specialist fleet to deliver its services to the public (e.g. road sweeper, recycling and waste vehicles as well as Grounds Maintenance tractors). So having one provider who can deliver this particular range of vehicles helps the Council achieve better efficiencies but also get the knowledge and advice we require to continue our transition to an electric based fleet.
- 2.5 The Council requires specialist provision and SFS are in a position to deliver all of our requirements (rather than the Council requiring or having multiple different contracts). In addition, SFS have a significant local presence which benefits the Council. In recent years they have expanded their support network in the South West and this has in turn further improved the level of service required by the Council.
- 2.6 The Council has a statutory duty to provide a range of services that require access to a variety of different vehicles. Through their experience SFS are proficient in ensuring the fleet is roadworthy and the Council have sufficient availability of vehicles to deliver the service. The effective operations of these statutory functions depend on having reliable vehicles that are readily available and operate safely. This is crucial.

2.7 **Summary of considerations**

| | Pros | Cons |
|-----------------|---|--|
| Extend with SFS | <ul style="list-style-type: none"> • Expertise in managing fleets • Buying power and influence over supply chain • Dedicated workshops and back-up options • Fleet management software and administration • Contract is performing well • Other local authorities moving to SFS and staying with them | <ul style="list-style-type: none"> • Risk of complacency with contract extended to 2033 |

| | | |
|-----------------------------|--|---|
| | <ul style="list-style-type: none"> • SFS own the risk – inflation and supply chain | |
| Manage own fleet | <ul style="list-style-type: none"> • Not tied to lease contract terms for replacements • Able to use a range of local repairs workshops (subject to procurement process) | <ul style="list-style-type: none"> • Limited discounts through frameworks • Maintenance contract with primary and secondary support through procurement • The Council owns all the risk – inflation and supply chain |
| Use of alternative supplier | <ul style="list-style-type: none"> • Able to compare performance to SFS • Expertise in managing fleets • Fleet management software and administration | <ul style="list-style-type: none"> • Limited alternative suppliers in the region • A new contract to establish and embed |

3.0 Span of the Existing SFS Contract

3.1 The Council currently operates 104 vehicles and has an additional 4 spare vehicles for use when a vehicle is unavailable due to routine maintenance, breakdown or damage. SFS is responsible for sourcing additional spare vehicles to cover the managed fleet as required. There are currently 41 vehicles on lease contracts with SFS and 43 further vehicles due to move onto lease contracts by the end of 2025-26.

3.2 Summary of vehicles by size and service area:

| | Plant | Under 3.5 Tonne | Under 12 Tonnes | Over 12 Tonnes |
|----------------------------------|-------|-----------------|-----------------|----------------|
| Housing | 1 | 34 | 8 | 0 |
| Waste, Recycling and Trade Waste | 4 | 2 | 3 | 18 |
| Grounds Maintenance | 5 | 1 | 6 | 0 |
| Street Cleansing | 0 | 1 | 6 | 1 |
| Property Services | 0 | 7 | 0 | 0 |
| Others | 0 | 7 | 0 | 0 |

3.3 The lease contract term for each vehicle ranges from five to ten years depending on the vehicle size and fuel type.

3.4 The maintenance programme for all leased vehicles runs until 2026. The maintenance contracts are aligned to the master contract and can only be extended by exercising the option to move into the secondary term. There are no options available with SFS for maintenance outside the master contract term. Therefore, there is a current disconnect between the vehicle lease length and the length of the associated maintenance plan (which the proposed contract extension will resolve).

4.0 Performance of the SFS Contract

- 4.1 The contract specifies response times and vehicle availability rates, which is closely monitored by the Fleet Manager and the SFS Contract Manager. SFS understand our needs and are currently in negotiations to provide an in-house workshop facility in close proximity to the Mid Devon depots and the operation of the services. A well-managed fleet naturally underpins a continually improving service to the residents of Mid Devon.
- 4.2 Overall performance and ongoing operational concerns are discussed at quarterly management meetings with the Operation Managers (services that run fleet vehicles), Waste and Transport Manager, Fleet Manager and Council Accountant. These are complimented by fortnightly operational meetings with the Fleet manager and Waste and Transport Manager which discuss day to day issues including repairs, breakdowns and other concerns.
- 4.3 SFS provides in house maintenance provision for the smaller vehicles along with sub-contractors for the larger fleet vehicles.
- 4.4 Communication between the Council and SFS is much improved and at a good standard with all parties having worked hard to resolve early concerns. This has led to improvements regarding SFS proactively responding to queries and issues which in turn has led to better provision of services. The Fleet Manager is a regular visible presence at all Council sites to ensure Council procedures are followed to reduce legal risks and damage costs.
- 4.5 Further work is being carried out to ensure best practice is implemented regarding use of our fleet. This will include the development of a new Transport Policy by the Fleet Manager, which will work with relevant Operational Service Leads and the Climate Change Specialist to ensure operational and strategic objectives of the Council are addressed.

5.0 Legal Considerations

- 5.1 Procurement law prohibits “substantial” modifications to contracts following their award. Modifications will generally be deemed substantial if they:
- a) render a contract materially different in character from the one initially concluded;
 - b) introduce conditions that would have allowed or attracted additional bidders to the procurement exercise;
 - c) change the economic balance of the contract in favour of the contractor in a manner that was not provided for in the initial contract;
 - d) extend the scope of the contract considerably; or
 - e) involve the replacement of the original contractor.
- 5.2 There are some “safe harbour” provisions in procurement law, which specify conditions that, if met, would mean a modification would not be deemed substantive and would therefore, not be permissible. If a “substantial” modification is made to a public contract during its term, it is considered a new

contract, which should be subject to a fresh procurement. Making a “substantial” change is tantamount to making a direct award in breach of the procurement rules, and runs the risk of by an aggrieved party challenging the decision to modify the contract and the court making an ineffectiveness order.

6.0 **Lease vs Purchase**

- 6.1 The Council ordered a range of new vehicles for lease during 2022; the capital costs provided by SFS for these vehicles have been compared with the purchase costs provided by the manufacturer taking advantage of the framework discount they offer. The results are in **Appendix B**.
- 6.2 SFS have the buying power to purchase vehicles at lower costs than the Council. The average saving on the electric vehicles are £1,285 per vehicle; the Council has 54 vehicles of this type/ size. The average saving on diesel vehicles is £3,078.
- 6.3 **Appendix C** compares the SFS lease contract cost with the Council’s internal borrowing rate (2023). Internal borrowing spreads the interest over the life of the loan. These figures show that overall, there are savings to be made across the fleet with the SFS lease contract. Please note that diesel vehicles are shown to be slightly more cost effective using internal borrowing but these are due to be phased out with electric or ZEV vehicles.
- 6.4 **Appendix D** compares the SFS lease contract cost with the PWLB (Public Works Loan Board) borrowing rate (2023). PWLB borrowing is an annuity loan. The interest payable on this type of loan reduces each year achieving greater saving in the final years of the loan. This is similar to 4.3, and considers the whole fleet. Mid Devon are unable to procure the larger fleet vehicles at preferential rates.
- 6.5 Purchasing electric vehicles over eight years would save an average of £260 per vehicle per annum. However, purchasing vehicles would require procurement of a new maintenance contract; this would require multiple providers to ensure effective and reliable service delivery. The Council would need to purchase a Fleet Management software system at a cost of approx. £12k-£14k per annum and resource for employee time to maintain the fleet records. SFS currently provide the Fleet Management software and maintain the fleet records. Designated Council employees have access to the database.
- 6.6 A move away from leasing vehicles would require the Council to resource additional spare vehicles to provide resilience to cover servicing or breakdowns. The Council would become liable for the maintenance of the spare recycling vehicles currently held.
- 6.7 The transition back to a fully owned fleet would take more than four years to complete. Managing leased and owned vehicles with primary and secondary maintenance contracts would increase the complexity of fleet management.

6.8 The leasing company takes on the risk of the residual value of the vehicles at the end of the term. Purchasing vehicles requires the Council to retain the residual value risk.

6.9 SFS and manufacturers recommend leasing vehicles for up to seven years. If vehicles are expected to have a longer lifespan then a purchasing model is more cost effective.

7.0 **Annual Indexation Applied to Contract Rates**

7.1 The current contract has enabled the Council to budget for the lease and planned maintenance costs until June 2026 by applying the agreed maximum indexation rate of 3% per year.

7.2 The current contract provides for an annual increase on all pricing, which occurs on the 1st April and is capped at 3%. At the point of transition from the primary to the secondary term (should the Council opt to extend), SFS will take a view as to where inflation will sit during the secondary term, recognising that pricing will increase each year but will remain capped at 3%.

7.3 Subject to procurement regulations the inflationary mechanism currently specified could be adjusted in one of two ways:

- a) Abolish the inflationary increases and move to a fixed rate-pricing model. The cost of the vehicle would remain the same throughout the term of the lease agreement. SFS assumes all inflationary risk and will price with inflation built in; or
- b) Remove the inflationary cap. The inflationary risk sits entirely with the Council. This does not provide financial certainty for the future and the Council carries the risk of fluctuations in the consumer price index (CPI).

Due to the above, we recommend option A as the best solution to reduce financial risk for the Council.

7.4 Financial risk and uncertainty does not allow the Council to plan for future liabilities in the short or medium term.

7.5 Removing annual indexation will spread the cost of the contract evenly over the term of the individual vehicle contract with negligible overall financial pressure. SFS are open to reviewing the existing lease contracts with a view to moving these onto fixed pricing.

7.6 Savings of between 1.5% and 1.9% could be achieved by paying annually in advance for the contract.

7.7 This negotiated amendment to the contract extension would not breach any procurement regulations, as it would have a negligible impact on the value of the contract.

8.0 Contract Secondary Term

- 8.1 The contract states that all maintenance on Council owned or leased vehicles will cease 02 June 2026. Therefore, the Council will be liable for any maintenance costs on leased vehicles until their respective lease end dates if the contract is not extended. This comes at a time where these costs will be significantly higher due to the age of the vehicles. The Council currently has 32 vehicles that will remain on lease beyond the contract end date, 22 of these vehicles have a lease end date in 2030.
- 8.2 In the event that the Council chooses to exercise the contract extension, SFS will recalculate the contract maintenance rates on leased vehicles in June 2026 to reflect the level of support that the vehicles require to complete their anticipated lifespan. The latter years of a vehicle's operation require more maintenance and therefore costs.
- 8.3 Early agreement to the secondary term will smooth the impact of higher maintenance costs for all new leased vehicles with the maintenance being spread over all lease years rather than only the period until June 2026.
- 8.4 Contracted maintenance will subsequently cease in June 2033 and therefore, consideration should be given to new lease terms towards the end of the contract to minimise the number of vehicles that will be on lease with no maintenance contract in place. There should also be a mid-secondary term review of the fleet contract to help inform future decision making.
- 8.5 SFS are able to negotiate extended warranties with manufacturers, which are able to be taken into consideration within the contract hire pricing. Extended warranties will only be obtained by SFS to cover vehicles up to the maintenance contract termination date. An early decision to extend the contract will allow more vehicles to have extended warranties for maintenance reducing the overall cost to the Council.

9.0 Contract Termination

- 9.1 The contract will terminate with SFS in either June 2026 or June 2033. The Council will have vehicles on lease that extend beyond the termination date.
- 9.2 The Council will be required to procure a new contract that may or may not result in SFS continuing its service. Planning for a contract handover and working with different suppliers will take careful management.
- 9.3 A managed handover at the termination date is essential for service continuity. The Fleet Manager will engage with all stakeholders to ensure good communication throughout the process.

10.0 Summary

- 10.1 The fleet contract is past the mid-term point of the primary contract period. Good contract management requires the Council to review the contract

performance and assess whether the contract is delivering against the aims set out at the procurement stage.

- 10.2 The contract in its current form carries the financial risk of future spikes in cost due to:
- a) CPI increases
 - b) A revaluation of all maintenance terms in June 2026
 - c) At the end of 2023, 54 vehicles were on lease terms extending beyond June 2026
- 10.3 An addendum will be sought to the current contract to remove the annual indexation and adopt a fixed rate model reducing the financial risk associated with CPI increases and giving financial certainty to both parties. Furthermore, the maximum lease term for any vehicle should not exceed seven years; this will reduce the financial impact of higher maintenance charges on older vehicles. The potential higher interest charges will be offset by higher residual values.
- 10.4 An early decision to exercise the additional seven year option will reduce the financial impact of a spike in maintenance charges in June 2026. All future individual agreement terms should be carefully considered as the contract expiry date approaches to further mitigate the risk.
- 10.5 In summary, the contract is performing well and SFS are delivering the standard of service set out in the contract. The Council is in a good position to effectively manage the contract and ensure that continual improvement is delivered along with service efficiencies to provide value for money, which will meet all stakeholders' expectations.

Financial Implications

The current contract provides for lease and maintenance contracts until June 2026, thereafter lease only for the remainder of the individual vehicle contract term. This exposes the authority to an increased financial risk in terms of the significantly increased costs associated with maintaining an aging fleet.

Legal Implications

The Council is in a legal contract with SFS until 02 June 2026 for the supply and maintenance of the whole fleet. Any termination of the contract before that date requires 6 months' notice. The Council's legal team reviewed the contract terms and conditions prior to signing the contract. The procurement process ensured compliance with the Procurement Regulations. There is an option available to extend the contract by a further seven years.

Risk Assessment

This report is a risk assessment of the contract and the associated financial risk.

Impact on Climate Change

All new vehicles must be Zero Emissions Vehicles (ZEV) or Ultra Low Emissions Vehicles (ULEV) if the C is to meet its climate emergency obligations by 2030, with the understanding that there may be constraints on viable solutions due to cost, infrastructure and vehicle capability.

Equalities Impact Assessment

There are no equality issues identified in this report.

Relationship to Corporate Plan

To ensure compliance with procurement regulations and to deliver our Corporate Plan priorities within existing financial resources.

Section 3 – Statutory Officer sign-off/mandatory checks

Statutory Officer: Andrew Jarrett

Agreed by or on behalf of the Section 151

Date: 14 June 2024

Statutory Officer: Maria de Leiburne

Agreed on behalf of the Monitoring Officer

Date: 14 June 2024

Chief Officer: Stephen Walford

Agreed by or on behalf of the Chief Executive/Corporate Director

Date: 14 June 2024

Performance and risk: Steve Carr

Agreed on behalf of the Corporate Performance & Improvement Manager

Date: 05 June 2024

Cabinet member notified: Yes

Section 4 - Contact Details and Background Papers

Contact: Darren Beer, Operations Manager – Street Scene and Open Spaces

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