Dear Chairs,

Motability

Thank you for your letter dated 7 March.

In the course of the session you expressed interest in knowing how separate Motability the charity was from Motability Operations Group plc, and more generally about the governance of the Motability Scheme. The opportunity to provide a full answer on this important topic did not arise during the evidence session, so I am delighted to provide one now. This is set out in section A of the enclosed submission.

Our response on the specific matters on which you have requested information is also better understood in a wider context, not only of governance, but also in terms of the economic and legal factors. This is explained in section B, paragraph 3.2 of the enclosed submission.

Should you have any further questions please do not hesitate to let me know.

Director

16 March 2018
Motability inquiry
Submission to the Work and Pensions and Treasury Committees

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Appendix 16
A. Governance

1. Summary

1.1 Two separate organisations are involved in the delivery of the Motability Scheme ("the Scheme"): 

1.1.1 Motability, an independent charity ("Motability") whose primary charitable purpose is to "facilitate the relief and assistance of disabled persons (…"the beneficiaries") in connection with the provision to the beneficiaries of personal or other transportation" (the "Primary Purpose"); 

1.1.2 Motability Operations Group plc, a commercial organisation ("Motability Operations") which delivers the Scheme on the ground. 

1.2 The relationship between Motability and Motability Operations is governed by a contract ("the Scheme Agreement").¹ 

1.3 Motability Operations is not a subsidiary of Motability but is owned by its bank shareholders. 

1.4 Each organisation plays a different role in servicing the needs of disabled people: 

1.4.1 Motability is responsible for the strategic direction and oversight of the Scheme, to ensure that the Scheme delivers a high level of service and value for its beneficiaries, disabled people, in a sustainable manner; 

1.4.2 Motability Operations assumes the commercial risk of operating the Scheme, in which capacity it enters into leasing contracts with customers, finances the purchase of cars and manages other commercial matters such as insurance, maintenance and the sale of used cars. 

1.5 The Scheme is the principal, but not the only, means by which Motability fulfils its Primary Purpose. 

1.6 After-tax profits of Motability Operations are either reinvested to improve customer service, or retained as capital reserves to safeguard the sustainability of the Scheme. Any amounts not required for these purposes are transferred to Motability or to the Motability Tenth Anniversary Trust ("MTAT"), an independent charity. MTAT invests these funds to provide Motability with income which is put to charitable purposes by Motability. 

¹ A copy was provided to Committee members on 1 March 2018.
2. **Motability**

2.1 Motability is an independent charity, which was co-founded in 1977 with all-party support by the late Lord Goodman and its current Chairman Lord Sterling. Since 1988 it has been incorporated by Royal Charter. The concept of an independent voluntary organisation outside, but having an excellent working relationship with, Government has always been fundamental. It resulted from the Government’s withdrawal from the old vehicle scheme (involving loan of the ‘trike’). Following exploration of various alternatives, it was realised that a scheme enabling disabled drivers and passengers to use the mobility allowance to lease a vehicle could best be arranged outside Government. As the then Secretary of State for Social Security, the Rt Hon David Ennals MP, said in his statement to the House of Commons on 6 December 1977:

“No Government can be expected to meet all the mobility needs of the disabled. It is reasonable for the disabled, like other people, to contribute to the cost of their own mobility. […] a group of prominent people […] chaired by Lord Goodman, has now set up a voluntary organisation for the United Kingdom, working in collaboration with the Government, to ensure that disabled people, both drivers and passengers, who want to use their mobility allowance to obtain a vehicle will get maximum value for money in doing so. […]

"Motability will be an independent organisation. […]

"Motability will decide itself how to fulfil its aims, and what its priorities should be, with the advice of the disabled and their spokesmen."\(^2\)

2.2 Motability is governed by unpaid charity trustees, known as the Governors. The Governors are drawn from the membership of Motability. Governors set, and then monitor and keep under regular review the strategic direction of the Scheme and oversee Motability Operations’ delivery of the Scheme. Governors are appointed on the basis of their familiarity with issues facing disabled people and their commercial and financial experience. In its 2007 Report, the National Audit Office ("NAO") confirmed that Governors had been recruited who had experience in finance, leasing, insurance and disability.

2.3 This remains the case today. When the Charity Commission concluded their review of Motability last year, it said that:

"The personal contribution to the charity made by Lord Sterling and his drive, determination and vision since its inception, strongly supported by the charity’s Governors and Director has undoubtedly led to the charity’s success."

"The governors understand the external environment in which the charity operates and ensure the charity stays relevant and has a long-term future."

"The CVs of the Governors (…) indicate that the individuals are well qualified to serve and cover the expected areas."

\(^2\) Quoted at greater length in Appendix D to the Report on Motability by the Comptroller and Auditor-General (HC 552 Session 1995-96, 18 July 1996)

\(^3\) "Motability: Review of progress against past NAO and PAC recommendations", June 2007, paragraphs 38 et seq.
2.4 There are currently nine Governors. Following the sad passing of three disabled Governors during the last two years, Motability is actively looking to recruit three new Governors with the assistance of a leading recruitment agency.4

2.5 The strategic direction of the Scheme, as set by the Governors, has always reflected three fundamental principles (the "Guiding Principles"): customer service, value for money for Scheme customers and the long term financial sustainability of the Scheme.

2.6 Detailed oversight of delivery of the Scheme by Motability Operations is undertaken in a number of ways:

2.6.1 A detailed written contract, the Scheme Agreement, governs Motability Operations' operation of the Scheme and sets demanding Key Performance Indicators (KPIs) related to customer service, value for money, affordability and sustainability, and Service Targets, reflecting the Guiding Principles, against which Motability Operations is held to account (see section 5 below).

2.6.2 A committee of four Governors called the Scheme Oversight Committee (the "SOC"), chaired by Motability’s Vice-Chairman Sir Gerald Acher, meets quarterly, supported by three members of Motability’s staff: the Director, Finance Director and Scheme Oversight Manager. Each quarter, the SOC reviews Motability Operations' performance against the KPIs and appropriate actions are taken in the event of any shortfalls in performance. The CEO and Finance Director of Motability Operations attend SOC meetings in order to account for Motability Operations' performance.

2.6.3 Motability's Director (or Scheme Oversight Manager) attends bi-monthly meetings of the Motability Operations Customer Management Committee, which focuses on customer service levels, and ensures that Motability can maintain a close eye on matters affecting its beneficiaries. In practice there is daily communication about specific customer cases which raise policy issues or where additional financial or technical help may need to be given to disabled customers by Motability. Bigger policy issues are discussed by Governors.

2.6.4 On a monthly basis Motability receives Motability Operations data on KPI performance and the full pack of information that goes to Motability Operations' Board of Directors, including Motability Operations' internal Company Performance Report and minutes of Motability Operations' internal governance meetings (excluding Board and Board Committees). This provides Motability with the same management information as Motability Operations' non-executive directors.

2.7 The Charity Commission considered Motability’s oversight of Motability Operations as part of its review last year, and said the following:

"We are satisfied with what we have found from our review of both Motability (and its relationship with Motability Operations plc) and … have not identified any significant regulatory issues. Indeed, from our limited work, the charity appears well-run, provides a unique and valued service to its beneficiaries and has a history of impressive achievements."

4 Odgers Berndtson.
2.8 At the end of 2017 the Governors commissioned a governance review to see whether there were areas of Motability’s governance that could be further improved. The review is ongoing.

3. Independence of charities

3.1 During the debate following the Urgent Question on Motability on 8 February 2018 the Secretary of State for Work and Pensions, the Rt Hon Esther McVey MP ("the Secretary of State") said:

“… in 2013, I ensured that they paid £175 million more to disabled people and will continue with that direct action from my new elevated position”.  

3.2 Referring to this statement in the evidence session on 5 March 2018, Neil Coyle MP put the following to the Minister for Disabled People, Sarah Newton MP ("the Minister"):

“… the Secretary of State said very clearly on 8 February that in 2013 she compelled Motability to provide better support”.  

The Minister answered:

“Yes, and the letters will show that”.

3.3 These statements were made in relation to the transitional support package provided by Motability to customers no longer eligible for the Scheme as a result of the Government’s reforms to the benefits system. The Secretary of State’s statements create a misleading impression about her involvement, but more importantly, in the context of governance, they reflect a misunderstanding of her role and powers in relation to the decisions taken by a charity.

3.4 When Government announced its proposed reforms, Motability was deeply concerned about the effect they would have on Scheme customers. At their Board meeting on 18 June 2012, predating the Secretary of State’s appointment as a minister by over two months, the Governors decided to provide transitional support. On 20 November 2012, the Chairman of Motability wrote to the then Secretary of State, the Rt Hon Ian Duncan-Smith to say:

“Motability has a proud history of service to disabled customers and we will ensure that we provide the right transitional support to them if they are no longer eligible to use the Motability Scheme following reassessment for PIP”.

3.5 Over the course of the following two years, Motability was open and transparent with the DWP and Ministers about the plans it was developing with Motability Operations to assist affected customers. Motability carried out a wide-ranging analysis of how customers would be affected and what could be done to mitigate the effects of the Government reforms. This included taking financial and legal advice and engaging with customers and disability organisations.

3.6 More importantly, the Secretary of State’s and Minister’s comments do not appear to recognise the legal independence of charities. As a charity, Motability is required

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5 Hansard, Volume 635, Motability, 8 February 2018.
6 Oral evidence: Motability, HC 847, question 110.
by law to be independent of the state. The Charity Commission’s guidance on the subject makes clear that:

“...for a body to be a charity, it must be independent. By this we mean that it must exist in order to carry out its charitable purposes, and not for the purpose of implementing the policies of a governmental authority, or of carrying out the directions of a governmental authority.”

3.7 The Governors of Motability have always taken their duties to be independent very seriously, and will continue to do so.

3.8 In the evidence session, the Minister promised to provide the whole sequence of relevant correspondence. This will show that the requirement of Motability to act independently from Government was raised in correspondence between Motability and the Secretary of State in 2013. The same correspondence will show that the level of support for affected customers proposed by Motability was the result of its own detailed and independent analysis with Motability Operations.

3.9 The proposed package remained under constant review by Motability, in particular as it assessed the financial performance of Motability Operations in the period up to August 2013. A strong financial performance during that period enabled Motability to increase the amount offered in the package. In short, factors such as customer needs, affordability and the long term health of the Scheme were central to Motability’s decision-making when reaching a figure to be provided to customers leaving the Scheme as a result of Government reforms. The Secretary of State’s interventions had little or no impact on Motability’s decision-making process although, as always, Motability continued to engage in the very helpful and constructive discussions it has enjoyed with DWP officials throughout the past 40 years.

4. Motability Operations

4.1 At its inception the Scheme was totally financed by the major clearing banks. The six major clearing banks in existence in 1978 (now four) established Motability Finance Limited (now Motability Operations) as a non-profit distributing private company, and were its shareholders. This is the origin of the separation between Motability (which did not have access to the funding), and Motability Operations.

4.2 Over time the nature of Motability’s oversight of Motability Operations has evolved to reflect the changing nature of Motability Operations’ business. As noted by NAO in their June 2007 Report, the division of roles between Motability and Motability Operations has evolved and since 2003 Motability Operations has been responsible for operating the financial and customer management aspects of the Scheme, while Motability has focused on setting the policy, direction and oversight of the Scheme. The division of roles is reflected in the Scheme Agreement, and has been reinforced by a series of fundamental changes in the risk profile of the Scheme that have occurred since 1999 and onwards:

4.2.1 The first step, from 1999, involved Motability Operations taking on the risk (from car manufacturers and dealers) of purchasing and subsequently disposing of lease vehicles. The decision to purchase cars without a

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7 Independence of charities from the state (RR7), 1 October 2009.
8 Ibid, paragraph 7.
guaranteed buy-back at a pre-agreed price from manufacturers or dealers exposed Motability Operations to the risk of shortfalls in cash flow (in the event of unexpected falls in used car prices). In its June 2007 Report, NAO recognised that this "massively increased the direct risk to the Scheme of reductions in residual values".9

4.2.2 At the same time Motability Operations took responsibility for spending on maintenance and servicing during the lease contract (previously managed by dealers for a fixed fee).

4.2.3 These new arrangements ensured that a full range of cars suitable for customers’ disability needs could be provided through the Scheme, and that customers would receive a consistently high level of service from any participating dealer across the United Kingdom. These changes also enabled the Scheme to provide a more flexible service, ensuring for example that a customer only needed to hand their old car back once their new car was available.

4.2.4 Since 2008 (in part thanks to its reserves) Motability Operations has been progressively diversifying its funding sources by accessing the debt capital markets, responding to NAO’s recommendation to review the scope for increasing the level of competition for financing.10 Motability Operations’ direct accessing of the capital markets has gathered pace since 2007. In that context, the level of capital reserves is a factor in lowering Motability Operations’ borrowing costs, as well as supporting the sustainability of the Scheme.

4.2.5 Since 2013 Motability Operations has assumed further risk, again with the aim of offering the best level of service and value for money to customers. It has insourced 80% of the motor insurance risk11, reducing the Scheme’s motor insurance costs, with the savings passed through to customers.

4.3 The risk factors identified above, and how they affect the level of reserves, are the subject of regular review by Governors (see section 6 below).

5. Scheme Agreement

5.1 As noted above, the Scheme is itself the principal means by which Motability aims to fulfil its Primary Purpose of helping disabled people.

5.2 The Scheme Agreement sets out the obligations of the parties with regard to the Scheme. The current Scheme Agreement is dated 25 September 2003, and was amended by a letter dated 30 June 2008.12 Prior to this the relationship between Motability and Motability Operations was regulated by earlier agreements and memoranda of understanding.

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9 Ibid, paragraph 9.
10 NAO 1996 Report, paragraphs 3.60 et seq.
11 Using a separate subsidiary incorporated for the purpose, MO Reinsurance Limited.
12 Copies have been provided to the Select Committees.
The Scheme Agreement sets Key Performance Indicators ("KPIs") and Service Targets ("Service Targets") for Motability Operations, and establishes the contractual framework by which Motability exercises its governance control over Motability Operations' delivery of the Scheme. Motability publishes the KPIs and reports on the performance of Motability Operations against them in its Annual Reports. In particular, the Scheme Agreement:

5.3.1 contractually obliges Motability Operations to remain a not for profit organisation providing services to Scheme customers, and not to pay any dividend or other distribution to its shareholders (other than in respect of certain preference shares issued to named banks);¹³

5.3.2 contractually requires Motability Operations to procure that the Scheme Financing is provided at a competitive cost;

5.3.3 requires Motability Operations to provide the detailed information needed by Motability to exercise its oversight function, and to submit to an independent audit if requested;

5.3.4 imposes contractual obligations on Motability Operations to prioritise the unique levels of service required by disabled people, which go far beyond the requirements of discrimination legislation;

5.3.5 provides for Motability to set the Scheme Policies, in consultation with Motability Operations, on a wide range of parameters which are of critical importance to the provision of the unique levels of service required by disabled people, including dealer accreditation, pricing, breakdown assistance, vehicle adaptations, early termination of leasing contracts and insurance;

5.3.6 limits Motability Operations' accumulation and retention of reserves by reference to the Motability Operations Capital Management Policy.¹⁴ This is enshrined in Motability Operations' governance framework, and establishes the Economic Capital ('EC') methodology (adopted with input from NAO) to determine the level of risk capital (mainly in the form of reserves) required in light of the risks facing the business, and explicitly sets a conservative approach to reserves management (see section 6 below). The Motability Operations Capital Management Policy has been formulated with the benefit of independent advice;¹⁵

5.3.7 requires Motability Operations' Remuneration Committee to place a significant weighting on performance against the attainment of the contractual service targets when assessing bonuses and or salary increases, and gives Motability a right for a Governor to be in attendance at meetings of the Remuneration Committee. A Governor did attend between 2008 and 2013 but attendance subsequently ceased in light of legal advice to avoid any perceived conflict of interest or participation in decision-making due to company law rules on shadow and de facto directors;

¹³ The banks are, separately, paid fees for services which are benchmarked and competitively tendered.
¹⁵ Principally from KPMG.
5.3.8 requires Motability Operations to take remedial action in the event of non-performance and entitles Motability to terminate in the event of a material breach.

6. **Scheme Profits and Reserves**

6.1 The operation of the Scheme has the capacity to generate profits. Indeed, the Scheme is designed to do so in order to underpin its long term sustainability. As NAO stated in their 1996 Report:

"It is normal business practice to build in a contingency margin into the prices paid by customers to create a contingency reserve to provide against the risks of running a commercial operation. Setting the appropriate level for this contingency reserve is a matter of business judgment".\(^\text{16}\)

6.2 From Motability’s perspective, these profits can be deployed to support its charitable Primary Purpose, supporting the mobility of disabled people and their families, in several ways:

6.2.1 being reinvested in Motability Operations, in the form of capital reserves (held in the form of vehicles), thus underpinning the stability and longevity of the Scheme;

6.2.2 being invested, again within Motability Operations, on initiatives and programmes in the Scheme to improve customer service and assist customers;

6.2.3 being transferred to Motability or MTAT for the benefit of disabled people in the form of grants and other forms of support.

6.3 For many years, Governors have, in consultation with Motability Operations, had the responsibility of considering the allocation of profits. Given that any application of profits is (whether directly or indirectly) in pursuit of Motability’s charitable Primary Purpose, this has always involved a weighing-up exercise, taking into account the whole range of relevant factors including external risks, the centrality of the Scheme to delivery of Motability’s Primary Purpose, the particular needs of disabled customers at the time, and changes in Government policy.

6.4 Governors recognise that since Motability Operations cannot raise capital for its business in other ways (such as a rights issue), retained post-tax profits are the only source of new capital. As noted above, Motability and Motability Operations have therefore agreed a Capital Management Policy which is designed to support the long term sustainability of the Scheme and enable it to withstand the whole range of economic shocks to which the Scheme may be exposed. Since 2003 the level of capital reserves has been built up to reach the level of adequacy determined by management, in its judgment, to meet the requirements of the model.

6.5 Provided that the level of capital reserves is sufficient to protect the sustainability of the Scheme, an amount of post-tax profit can be applied, within Motability Operations, to improve customer service or value. In practice this may often be the best way of meeting Motability’s Primary Purpose of helping disabled people and

their families. Examples of the types of support funded in this way are price reductions, subsidising the 27,000 Wheelchair Accessible Vehicles (WAVs) on the Scheme, providing free vehicle adaptations. Other examples are given in Motability Operations’ submission to the Chairs (see Appendix D, Customer Investments and Charitable Donations). The impact of these investments (and size compared to sums transferred to Motability or MTAT) can be seen in chart 1.3 of Motability Operations’ submission.

6.6 Where profits exceed the levels required to protect the affordability and viability of the Scheme, and have not been used to enhance customer support within Motability Operations (as described in section 6.5), they are, as noted by the NAO in their 1996 Review, available to be transferred to Motability or MTAT for the benefit of disabled people. As chart 1.3 of Motability Operations’ submission shows, the level of charitable donations has been significant over the last seven years, reflecting buoyancy in the used car market and the successful management of the Scheme by Motability Operations. Since 2007 £265 million has been donated to Motability and £80 million to MTAT.

6.7 Up to now the Governors have not felt it appropriate to adopt a rigid framework which would limit their consideration of the options or fetter the flexibility of their decision-making. However, it is evident that efficient management in Motability Operations and the cyclical strength of the used car market has resulted in a sustained and indeed increasing level of profits over recent years. There have of course been discussions between Motability and Motability Operations, and among Governors, about the application of future profits, especially if their level permits investment in support of disabled people and their families (whether in the form of customer support as part of the Scheme, or in the form of grants by Motability or MTAT). There are certainly many opportunities to provide such support which the Governors keep actively under review, and Governors will continue to make decisions with the interests of disabled people and their families uppermost in the minds.

6.8 One of those opportunities was the provision of PIP transitional support provided by Motability to the circa 75,000 disabled people to date who have lost out as a result of Government changes to the benefit system – with tens of thousands more expected to lose out as DWP reassessments continue until 2020/21. Going forward, other opportunities have already been identified by Governors. They recognise, for example, that up to 250,000 disabled people with mental illness or learning difficulties will join the Scheme in the coming years, requiring an exceptional level of care and service. None of this support would be possible without the profitability of Motability Operations, which has resulted from management of the new business model outlined above (see section 4.2 above) and relatively benign economic conditions.

7. **MTAT**

7.1 MTAT is an independent charity, incorporated as a guarantee company. Its principal charitable object is "... the relief and assistance of disabled persons (... the "beneficiaries") in connection with the provision to the beneficiaries of personal or other transportation by assisting, promoting and supporting Motability ...".

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17 NAO 1996 Report, paragraphs 3.51 et seq and Appendix B.
7.2 MTAT was established in 1989 to support Motability by making grants to Scheme customers and investing in projects to support mobility needs. At that time, it was often necessary to make grants to customers who could not afford the advance payments required for even the smallest of cars. Over the last two decades MTAT has supported Motability’s provision of charitable grants with circa £50 million of funding.

7.3 MTAT’s board is currently made up of six trustees. Its Articles provide for a maximum of eight trustees, of whom:

7.3.1 up to two may be appointed by the Secretary of State for Work and Pensions;
7.3.2 up to two may be appointed by Motability Operations;
7.3.3 up to three may be appointed by Motability;
7.3.4 one is a Chairman appointed by the others.

7.4 MTAT’s principal charitable purpose means that its interests and Motability’s are, to a large extent, aligned.

7.5 Income from MTAT has been used to maintain support to a category of beneficiaries following the DWP withdrawing support for the Specialised Vehicles Fund from December 2015. As the Charity Commission noted in its 2017 review, it is an appropriate use of charitable funds to meet the cost of public services previously provided by the State where doing so is within the charity’s objects and is in the interests of the charity’s beneficiaries.
B. Competition and tendering

1. Economic background

1.1 Competition is undoubtedly a means of driving value and competitive pressure can help to ensure that services are priced competitively. However, this is only true where there is genuine potential for competition in the given market, and where competition ensures that all the customers in that market can be served. The particular features of Motability Operations' market mean that these conditions do not apply, and therefore the Governors have, following NAO’s 1996 Report, established other means of ensuring that best value is delivered.

1.2 Motability Operations' estimate of the proportion of Scheme customers who would be unable to obtain a new vehicle on the open market is 80%. Without the existence of the Scheme, these customers would be unable to access the credit required to buy a new car, or in some cases to access affordable insurance cover. By contrast, the Scheme is open to recipients of the relevant mobility allowances across all of the United Kingdom. The reason for this is that Motability Operations' not for profit status enables it to reinvest profits in the Scheme for the benefit of customers (principally through improved customer service, a wider and more comprehensive range of services, and value for money). Crucial added benefits are that Motability Operations is able to provide the unique level of service required by disabled people and their families, and can also subsidise certain customers, for example customers requiring wheelchair accessible vehicles (WAVs) or adaptations, in a way that profit-distributing companies would find difficult, if not impossible.

1.3 Although Scheme customers are free to select the products of commercial leasing companies, these companies have not specifically targeted such customers or developed products tailored to their unique needs. This no doubt reflects the difficulties they would face in offering such products at a price that was competitive compared to Motability Operations', principally on account of having to distribute part of any return generated to shareholders or investors, but also because of the cost of developing tailored services. Even if they could offer a competitive solution, this would involve cherry picking the most profitable customers, leaving other customers (potentially a majority, especially in disadvantaged areas) unprovided for.

1.4 NAO recognised this in their 1996 Report:

"due to its unique characteristics it is not possible to compare the Motability contract hire scheme directly with the market".\(^{18}\)

1.5 Rather than introducing competition at the level of Scheme provision, NAO considered that a good proxy for competition could be achieved by:

1.5.1 Motability Operations using its scale and purchasing power to maximise competition among suppliers;

\(^{18}\) NAO 1996 Report, paragraph 16.
As highlighted by NAO, various tools other than tendering could be used to assess competitiveness:

1.6.1 using price comparisons and benchmarking;
1.6.2 setting customer service targets;
1.6.3 specifying performance measures;
1.6.4 setting out the roles and responsibilities of Motability Operations and Motability in a revised agreement;
1.6.5 providing key performance information to disabled people using the Scheme.

In its Review of Progress in 2007, NAO found that, with one exception, all its recommendations – such as the use of KPIs and benchmarking, improved scrutiny by Motability and the use by Motability Operations of its purchasing power – had been met. The exception related to the introduction of more competition for financing and administration services. On financing, NAO recognised that competition and transparency would follow from the plans to have recourse to additional means of financing, including the use of bonds. On administration services, NAO recognised the difficulty of making comparisons, again accepting that the arrangements with Motability Operations were unique. It noted, however, that savings had been achieved through benchmarking and, more widely, that Motability Operations’ purchasing power had been used to “deliver better value for customers while maintaining and improving standards of customer service”. In addition, Motability commissioned EY in 2014 to carry out a full independent review of Scheme overhead costs which concluded that the Scheme had reduced its overhead costs by customer by 28% in real terms over the previous decade.

Neither in 1996 nor in 2007 did NAO recommend that the arrangements with Motability Operations be opened up to a tendering process.

Legal background

Motability is not a "body governed by public law" for the purposes of the Public Contracts Regulations 2015. It is not “financed, for the most part, by the State”. As the Government has made clear on more than one occasion, neither Motability nor Motability Operations are publicly funded. Specifically:

"The Department makes no financial contributions to the Motability charity or Motability Operations […]" (Baroness Buscombe, Parliamentary Under-Secretary of State for Work and Pensions (Lords))

"The Department works closely with Motability and facilitates the transfer of benefit to Motability on behalf of those claimants who have chosen to join the Motability Scheme.”

19 Ibid, paragraph 18.
20 Public Contracts Regulations 2015, regulation 2(1).
21 Baroness Buscombe, exchange between Lord Rooker and Baroness Buscombe on 21 February 2018.
As these statements correctly indicate, the monies received from the Department are not public funds. They are the freely committed monies belonging to benefit recipients. These monies do, of course, ultimately derive from the tax payer, but at the point at which they are transferred to Motability Operations in settlement of Scheme customers' liability under leasing contracts, they are the property, and at the free disposition of the customers. This was recognised by the Secretary of State, David Ennals MP, in 1977 when he announced the founding of a voluntary organisation independent of the State (see 2.1 above).

Motability is therefore not a "contracting authority" under the Public Contracts Regulations 2015, and is consequently under no legal obligation to put the Scheme Agreement out to tender. Given that no such obligation arises (although tendering is one of a range of options open to Governors), it is for Governors to decide how to achieve the best outcome for their beneficiaries, disabled people, in terms of value for money and service levels.

3. Approach adopted by Motability

3.1 From experience, the Governors have concluded that a competitive tendering process for the operation of the Scheme would not result in improved service, value for money or sustainability for the benefit of disabled people (the Guiding Principles). Governors would be concerned that opening the Scheme Agreement to a tender process involving a number of commercial organisations seeking to make a profit would be likely to result in a fragmentation or dilution of purchasing power; lower standards of customer service generally and, in particular, for those customers needing a higher level of support (cherry-picking); as well as increased prices to customers as profits were drawn off for shareholders rather than being reinvested in the Scheme or donated to Motability or MTAT for the benefit of disabled people.

3.2 Reflecting this approach, and in response to the specific points made in the letter from the Select Committees dated 7 March 2018:

3.2.1 Motability did not 'award' the Scheme Agreement in 2003 but updated the agreement that was already in place. There are therefore no papers or minutes in relation to ‘awarding’ the contract.

3.2.2 As discussed, the 2003 Scheme Agreement was an update to existing agreements and was not the result of a tendering process.

3.2.3 The Scheme Agreement (see 1.3 above) is an arm's-length contract between two separate entities who were independently professionally advised when the updated terms were negotiated in 2002-2003. This is reflected in demanding KPIs and Service Targets and a high degree of oversight (see 5 above) over Motability Operations' delivery of customer service, value and sustainability. These reflect Motability's independent

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22 Hansard – Motability: answer to Written question – 10579.
assessment of what is required to provide the unique level of service required by disabled people and their families.

3.3 Applying the KPIs and Service Targets in the Scheme Agreement and the tools recommended by the NAO, the Scheme is independently recognised as offering a leasing package that is over 45% cheaper than comparable market offerings.23 The ways that competitive forces are channelled by the Scheme to the advantage of Scheme customers are set out in more detail in the Appendix. Even excluding the benefit of VAT and IPT concessions, the Scheme is still around 25% cheaper than comparable offers in the wider market, reflecting its purchasing power and its efficiencies.

3.4 In addition to value for money, the quality of service provided by the Scheme must also meet the unique needs of disabled people and their families. In the latest private survey (January 2017) of customer service by the Institute of Customer Service (an independent, not-for-profit professional organisation which works with its members to raise the standards of customer service in the UK) Motability Operations scored 94.8% overall customer satisfaction. The highest scoring companies in the most recent ICS national survey (January 2018) were Amazon at 86.6% and First Direct at 86.1%; John Lewis scored 85%.

3.5 Governors do not consider that a tender process would deliver better value for money or customer service at the present time, especially if competing providers have to distribute profits to their shareholders.

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23 CAP Derwent, January 2018.
Appendix

Channelling of competitive forces through the Scheme to the advantage of Scheme customers

Cost components of a typical lease

- Depreciation (44% of lease cost): The Scheme price list is updated quarterly following discussions with manufacturers. The aim is to ensure a stable and consistent price proposition over time so that a customer can renew for a similar vehicle at the end of their lease without a significant change in the price they need to pay for their lease. Through the quarterly pricing process, Motability Operations generates a highly competitive environment between manufacturers to deliver the best possible value for customers, while maintaining a diversified fleet vehicle mix.

After the end of the lease, the vehicle is sold by Motability Operations into the used car trade, typically to franchised and non-franchised car dealers as well as to specialist used car superstores. The resale process is as important to the value and sustainability of the Scheme as the initial acquisition of the vehicle. Motability Operations sells through two main channels: a business to business channel direct over the web and through a network of third party physical auction sites. Over the past decade, Motability Operations has succeeded in growing the percentage of cars sold online to 80%, achieving higher returns than would have been achieved through auctions. In light of structural changes in the new car market including the proportion of UK retail sales now made on three year personal contract purchase (PCP) agreements, the used car disposal operations will continue to innovate and develop new strategies in the coming years to stay ahead of other businesses competing to sell their own used cars.

- Insurance (27% of lease costs): Since October 2013, the Scheme has gradually introduced a new motor insurance risk model whereby the Scheme takes on 80% of the insurance risk, with appropriate reinsurance placements to limit this risk and with RSA in Liverpool (who carry the remaining 20% of the risk) continuing to provide the customer-facing service. The solution protects affordability and minimises price volatility over the long term, while reducing costs to the benefit of customers. Appropriate incentives are in place with RSA to ensure a high standard of customer service and to reduce claims leakage costs.

- Maintenance (10% of lease cost): Maintenance costs are controlled through an industry standard electronic system between Motability Operations and dealerships which facilitates submission by the dealer of cost estimates and authorisation requests, online authorisations by Motability Operations and electronic invoicing from dealerships to Motability Operations.

- Funding (10% of lease cost): The Scheme is funded by a combination of Sterling and Euro bond issues and bank debt, all of which is arranged by Motability Operations through competitive processes. The shareholding banks have no advantage in these competitive processes.

- Customer Support (6% of lease cost): Scheme prices includes an amount to fund key elements of the customer offer, including Good Condition Bonus, subsidised prices for 27,000 Wheelchair Accessible Vehicles on the Scheme and for vehicle adaptations, and the provision of continuous mobility e.g. hire cars for customers whose cars are off the road for a period of time.

- Administration Costs (4% of lease cost): In relation to administration costs, in 2014 the Governors commissioned a full, independent review of the Scheme overhead costs from 2002 to 2013. EY (Ernst & Young) produced this review which covered by Motability and Motability Operations. The review concluded that over the period noted, the Scheme improved its customer service levels to 98%, and the number of cars available at nil Advance Payment rose from 62 to 490. At the same time as making these improvements, the Scheme reduced its overhead costs per customer by 28% in real terms.