

WEST DUNBARTONSHIRE COUNCIL

Report by the Chief Executive

Council: 11 December 2007

Subject: Schools' PPP Project: Submission of Final Business Case and Authority to Proceed to Financial Close

1. Purpose

1.1 The purposes of this report are:

- to inform Council of the scope, nature, commercial terms and financial consequences of the proposed Schools' PPP Project;
- to seek approval from Council for officers to proceed to Financial Close of the project.

2. Background

2.1 In June 2004, the Council obtained confirmation of a provisional award of funding under the then Scottish Executive's Public Private Partnership (PPP) programme. This funding, in the form of a Revenue Support Grant (RSG) of £7.15 million per annum was awarded on the basis that the Council would take forward a project to construct the following new schools on four campuses:

- Vale of Leven Academy;
- Clydebank High School;
- a new Clydebank Denominational Secondary School formed by the amalgamation of St Andrew's High School and St Columba's High School on the St Columba's site (to be named St Peter the Apostle High School) and St Eunan's Primary School;
- Dumbarton Academy and a new primary school formed by the amalgamation of Aitkenbar, Braehead and Dalreoch primary schools.

2.2 The project has developed since June 2004, with the following as key milestones/developments:

- 12 December 2005: Revised Outline Business Case (ROBC) submitted;
- 15 December 2005 – 9 February 2006: European Journal contract notice (OJEU) posted; expressions of interest from 5 consortia/contractors;
- 26 January 2006: Audit Scotland assessed the project as being value for money for the Council;
- 29 March 2006: Initial Accounting Opinion indicated that the project would be off Balance Sheet;
- 7 July 2006: Invitation to Negotiate (ITN) issued to 3 bidders: Amey/Carillion (trading as West Dunbartonshire Schools Partnership); BAM and Transform Schools (Balfour Beatty);

- 26 October 2006: ITN return date;
- October – December 2006: evaluation of ITN submissions;
- 12 January 2007: all 3 bidders asked to submit a Best and Final Offer (BaFO);
- 23 February 2007: BaFO submissions received;
- February – April 2007: evaluation of BaFO submissions;
- 11 April 2007: BAM PPP named as Preferred Bidder;
- April 2007 – present: negotiations between Council and BAM on range of educational, technical, legal, commercial and financial aspects of the project;
- 8 August 2007: Project Board approved the appointment of the in-house teams to deliver Mandatory Variant 3 (Building Cleaning and Grounds Maintenance);
- 8 August 2007: Detailed Planning Permission granted for the Vale of Leven Academy, Clydebank High School and St Peter the Apostle High School/St Eunan’s Primary School and EECC campuses;
- September 2007: de-briefing of two unsuccessful bidders;
- 22 October 2007: Council’s Planning Committee unanimously rejected the application for Detailed Planning Permission for the Dumbarton Academy campus;
- 28 November 2007: Provisional Accounting Opinion indicated that the project would be off Balance Sheet;
- 28 November 2007: Council approved the removal of the Dumbarton campus from the PPP project and instructed officers to proceed towards Financial Close on the basis of a 3 campus project.

3. Main Issues

Project Scope

3.1 The final scope of the project in terms of schools and facilities (“the Project”) is as follows:

- i. **The Clydebank Non-denominational CLC**, incorporating a secondary school built for 1,500 pupils located on the existing Clydebank High School site. The Clydebank non-denominational CLC will incorporate sporting and social facilities, and be available for community use out of school hours. The facilities provided will include synthetic floodlit all-weather football and hockey pitches, an outdoor basketball court, a fitness suite, and flexible social space, incorporating theatre provision.
- ii. **The Clydebank Denominational CLC**, incorporating a secondary school (St Peter the Apostle High School) built for 1,500 pupils located on the existing St Columba’s High School site, together with a co-located but physically separate St Eunan’s Primary School and Early Education and Childcare Centre. The CLC will also incorporate sporting and social facilities, and be available for community use out of school hours. The facilities provided will

include a floodlit synthetic running track, synthetic floodlit all-weather football and hockey pitches, a fitness suite, a dance studio, and flexible social space with theatre provision.

- iii. **The Vale of Leven Academy CLC**, incorporating a secondary school built for 1,100 pupils located on the existing Vale of Leven Academy site. The existing Language and Communication Base facility in the current Vale of Leven Academy will be relocated to custom built facilities within the new CLC. Among the sporting and social facilities, capable of out of school hours community use, will be synthetic, floodlit, all-weather football and hockey pitches, a fitness suite and flexible social space incorporating theatre provision.

3.1.1 Under the terms of the Project Agreement, West Dunbartonshire Schools Limited, the Special Purpose Company (SPV) established by BAM for the purposes of contract, through its Facilities Management sub-contractor, (HBG FM), will have responsibility for the following services:

- Reactive and Planned Maintenance
- 30 Year Life Cycle Maintenance
- Janitorial Services
- Pest Control
- Waste Management
- Energy Management
- Insurance
- Porterage and Churn
- Deep Clean
- Elements of Grounds Maintenance Related to Warranted Pitches
- Litter
- Security
- Disaster / Emergency Management
- Help Desk

3.1.2 Following the assessment of the Mandatory Variant bids against the Scottish Government Value for Money criteria, it was clear that the Council's in-house team, would retain responsibility for building cleaning and grounds maintenance services. This position has previously been reported to the Project Board. However, the decision to retain the services In-house requires to be ratified at this meeting as part of the overall project scope. A copy of the Project Board report on this matter forms Appendix 3.

3.2 Consultation and School Views

3.2.1 Throughout the development of the project, a very high emphasis has been placed on the importance of extensive and effective consultation with all relevant stakeholders. Examples of this consultation include:

- informal consultation with all school communities in 2004/05;
- extended period of statutory consultation with all school communities affected in spring 2005;
- consultation between parents, staff and pupils of all schools involved and the 3 short-listed bidders at ITN and BaFO stages;
- public display of the bidders' school models in both Clydebank and Dumbarton, with the opportunity for members of the public to complete and submit comment sheets;
- direct contact between Preferred Bidder (PB) and all school communities on a wide range of educational and design issues throughout PB stage;
- establishment and involvement of subject specialist group from schools involved to act as advisers to project on subject specific issues;
- consultation with local branch of Scottish Autistic Society on design of Vale of Leven Academy Language and Communication Base;
- Extended consultation sessions with all interest groups (55 in all) in schools from primary 4 through to school boards and Catholic Church representatives;
- ongoing consultation with Head Teachers of all schools;
- ongoing consultation with Trade Unions on employment, TUPE and other issues;
- consultation with community groups (eg Kilbowie Residents Association);
- ongoing consultation with SportScotland on sports provision;
- ongoing consultation with the Scottish Environment Protection Agency (SEPA) on a range of environmental issues;
- PPP project has been a standing item on agenda for Education Directorate meetings throughout the project.

3.2.2 Responses by school communities and stakeholders towards the school designs have been overwhelmingly positive.

3.3 Affordability, Unitary Charge, Financial Contributions and Retained Costs

3.3.1 As noted in Paragraph 2.1 above, the funding provided to the Council by the Scottish Executive in terms of the Conditional Award is up to £7.15m per annum in Revenue Support Grant, and is predicated on the Council delivering a project with a Capital Value of approximately £100 Million or over.

3.3.2 Using a Swap rate of 4.89% (the most recent available), the estimated Unitary Charge payable to the SPV in 2012/13 is £10.419m. When one adds the sums payable to the in-house team for Cleaning and Grounds Maintenance (£3871k), sums payable for Utilities (£454k) and other retained costs, this results in an “Affordability Gap” of zero.

3.3.3 It should be noted that the Council will require to make contributions from the following sources:

Firstly, the administrative and operational savings arising from the merger of schools, the removal of excess capacity (essentially unused or under-utilised space), the application of the existing schools’ operational budgets and savings in the maintenance budgets etc..

Secondly, the Council will be applying the insurances from the fire at Vale of Leven Academy and the proceeds of sales of surplus property at St Andrews, St Eunan's and Braidfield High School. These will be placed in a sinking fund which, together with the interest generated, will be applied over the concession period to meet an element of the unitary charge.

Thirdly, a net contribution by the Council of a sum (generally referred to as the “affordability gap”) which is necessary to meet the Unitary Charge commitments over and above the two above funding sources (this would only be required if Swap rates rise before Financial Close or if other unexpected costs arise before Close is reached).

3.3.4 At the special meeting on 11 April 2007, when the Council approved the appointment of BAM PPP as the preferred bidder for the project, it was noted that the first full year Unitary Charge (UC), utilising the best available information, was likely to be in the region of £14.689 million. At that time, after the application of the sinking fund monies and the administrative and operational savings, the Council’s net contribution (generally referred to as the “affordability gap”) for the first year was likely to be £79,000 with the contribution to be met by the Council compounding by the same figure each year throughout the concession period.

3.3.5 It was subsequently reported to members at Project Board and thereafter the Schools Procurement Committee on 27th August 2007, that this net contribution figure had risen to approximately £127,000 due almost entirely to increases in long term interest rates. Thus, whilst there had been no substantial increases in the cost of the works, funding costs had risen significantly, adding to the overall cost of the project. Importantly, from a Value for Money basis, the conventional funding source (i.e. the Public Works Loan Board (PWLB)) had risen in line with Swap rates and accordingly the Value for Money (VfM) benefit of PPP was maintained.

3.3.6 As will be noted by reference to Section 9.4 of the Final Business Case, the projected range for the First Year Unitary charge is from £10.228m to £10.802m producing compounding annual contributions by the Council of between nil and £28k per annum. In considering these figures it should be noted that the variations are almost entirely dependent on the variations in Swap rates which may occur between now and financial Close.

3.3.7 The variation between this figure and the last reported figure is attributable principally to the three factors.

Firstly, a number of costs which were identified as provisional sums have now been firmed up. This has resulted in some movement in the capital and revenue costs of the project, which in turn are rolled up into the unitary charge figure.

Secondly, the alteration to the scope of the project with the removal of the Dumbarton Campus (Dumbarton Academy, Dumbarton Primary and Dumbarton Early Education and Childcare Centre) by Council on 28th November 2007. This removal removed approximately £30 Million from the Capital costs and £2.86m from the 2012/13 Unitary Charge. However, it also removed £3.5m in estimated Capital Receipts from land sales and £750k annum in Administrative/ Operational savings.

Thirdly, since the report to the Schools Procurement Committee in August 2007 there has been a steady but marked reduction in the prevailing Swap rates. It will be recalled that the model is particularly sensitive to movements in these rates and accordingly these reductions have brought significant benefits to the Council. It is of course the case that this trend can be quickly reversed. Accordingly, in setting the range of rates which would be considered acceptable, this factor has been fully considered and modelled.

3.3.8 In addition to the sums which are payable through the Unitary Charge, there are a number of services and costs associated with the operation of the schools which the Council will pay separately from the Unitary Charge. It should be noted that these costs have been fully factored in as obligations on the Council when considering the relative Value for Money of the PPP Project and the Conventional Procurement Assessment Model (CPAM) which assesses the costs and value for money of non-PPP procurement of the same assets and services. The services and costs involved are detailed below:

Catering Services: Catering has been excluded from the model from formal launch of the project. This cost has therefore never been included in the Financial Model from the Revised Outline Business Case onwards as anything other than a pass through cost.

Cleaning Services: As noted in paragraph 3.1 above, Building Cleaning was exposed to competition from the in-house team as a mandatory variant cost. On a Value for Money exercise being undertaken it was determined that, for the vast majority of the Cleaning Services, the In-house bid represented the best value for money. Some factors such as deep clean and elements of emergency cleaning/spillages etc., were excluded from the in-house bid and these will be undertaken by HBG FM staff. The value of the services awarded to the In-house Team amount to approximately £761k per annum (2012/13 prices).

Grounds Maintenance: As with cleaning, Grounds Maintenance was exposed to competition as a Mandatory Variant, and was won by the In-house team. Some elements of maintenance of the all weather pitches have been retained by the SPV to avoid unacceptable risk transfer on the warranty; however, these costs are included in the Financial Model. The value of the services to be awarded to the In-house team is approximately £110k per annum (2012/13 prices).

Utilities: Utilities are modelled as a pass through cost (i.e. the Council will meet them). However, as the SPV is primarily responsible for ensuring the energy performance of the Schools, there will be a mechanism which will allow for the sharing of variations in utilities consumption, including any which are due to the buildings performing better or worse than the model had predicted. A cost of approximately £420k (2012/13 prices) has been allowed within the model for utilities.

Information Technology: Whilst the costs of the provision of an ICT network infrastructure (principally cabling and wall points) has been provided in the construction costs, the project has never included a managed ICT service. Accordingly Telephony and IT hardware costs are the responsibility of the Council. One exception to this general rule is the initial provision of Interactive Whiteboards in all general purpose classrooms and a number of specialist areas.

Rates: The Council will be responsible for paying the rates for each of the new schools. A sum of £50,000 has been allowed as an additional cost over and above the sums being paid at present. This sum has been agreed after consultation with the Valuation Joint Board.

As with all schools PPP projects in Scotland to date, costs of **curriculum delivery** and **teaching staff** etc. remain outwith the scope this project.

3.4 Staff Transferring and Trades Unions

- 3.4.1** One of the main developments in PPP in Scotland over recent years has been the increased recognition of the role of staff in the delivery of the projects and the need to ensure that individual employee rights and collective bargaining arrangements etc. are protected throughout the process from procurement, through operation and finally on handback.
- 3.4.2** During the procurement process, a number of meetings took place with Trades Unions to determine their views on the Council's proposals and to feed back on the likely impact of Council decisions.
- 3.4.3** The Unions also met with all bidders during the bid preparation stages and subsequently met with the SPV as Preferred Bidder to discuss employee terms and condition and operational issues.
- 3.4.4** Whilst all Unions would undoubtedly have wished to retain all employees within the public sector, it was recognised that the contract terms and conditions to be entered into between the Council and the SPV protected current and future employees to the maximum possible extent.
- 3.4.5** In particular, the following terms and conditions are being incorporated into the project agreement and are enforceable by the Council:
- BAM will seek an open Admitted Body arrangement with Strathclyde Pension Fund with a view to ensure that all current pension rights and arrangements are preserved for existing employees and further are offered to new starts during the 30 year contract. The obligation for the contractor is to enter such an agreement if possible. This is considered to be a high test and should ensure that these rights are preserved.
 - If such an admissions agreement is not available, the new starts or existing employees are to be offered a pension scheme which is certified by the Government Actuary's Department as providing benefits in respect of the Relevant Employees which are broadly comparable to those provided by the Local Government Scheme.
 - All current Terms and Conditions will be applied on transfer and will be maintained thereafter during the period of the concession unless negotiated differently by the employees or their representatives. Note that the Council has specifically ensured that the contract is aligned with the provisions of the Scottish Government/STUC *Protocol and Guidance Concerning Employment Issues in PPP Contracts* ("the Protocol"), whereby Trade Union or employee representative agreement is specifically needed for any changes. These provisions effectively ensure that, unless Trade Unions agree, the current collective bargaining arrangements will be maintained throughout the project duration, and the employees transferring back to the Council

will do so on terms materially the same as those which apply to the Council's own employees.

- As above noted, employees will re-transfer to the Authority on the termination.

3.4.6 The Trade Unions also made a number of observations and representations in respect of the retention of Soft Services and welcomed the outcome of the Mandatory Variant tenders. They have also indicated that, whilst they would ideally wish all employees to be retained in the Council's employment, they recognise the risk transfer issues associated with the retention of janitorial staff.

3.4.7 The proposal to be approved therefore is that the Cleaning and Grounds Maintenance services be retained in house with the staff remaining within the employment of the Council, while Janitorial services and staff (current c14) will transfer to the SPV with the benefit of full TUPE and Protocol rights.

3.5 Programme

3.5.1 If Financial Close is achieved before the end of 2007, HBG Construction will begin work on site on 7 January 2008 and the following key handover dates will be targeted:

- Vale of Leven Academy: 29/06/2009;
- Clydebank High School: 01/07/2009;
- St Peter the Apostle High School: 03/07/2009;
- St Eunan's Primary School: 18/10/2010.

3.5.2 It should be noted that, although the intention is for the school buildings to be handed over on the dates listed above, external sports facilities and other landscape features will not be available at these times, but will follow later, following the demolition of existing school buildings.

3.6 Operational Phase Arrangements for School and Community Use

3.6.1 Once the schools are handed over and become operational, a new management regime will apply for the project schools in which it is essential that all parties involved have clear and clearly understood roles and responsibilities.

3.6.2 Central to the day-to-day management of the schools will be the SPV's Helpdesk through which all matters relating to facilities management and building maintenance will be channelled.

3.6.3 It will be the responsibility of the schools to report promptly to the Helpdesk any faults or problems relating to the buildings and grounds.

- 3.6.4** It will be the responsibility of the contractor to respond to reported problems and faults within timescales which are predetermined within the Payment Mechanism. Failure to respond within the set timescales will result in financial penalties for the contractor; repeated failure could result in warning notices being issued and ultimately to the termination of the contract. It should be noted, however, that the principal purpose of the timescales, deadlines and penalties within the Payment Mechanism is to incentivise the contractor to deliver a high quality service rather than to increase the likelihood of contract termination.
- 3.6.5** The contractor will deliver Facilities Management services at all the project schools, encompassing janitorial/security, maintenance, life cycle replacement, energy management, pest control, disaster management and Helpdesk. The details are shown in Table 5 of Section 6.4 of the Final Business Case (Appendix 1).
- 3.6.6** The cleaning and grounds maintenance services will be delivered by the Council's in-house team. Interface arrangements have been established to ensure that a seamless service is delivered to the schools.
- 3.6.7** The Catering Service has been excluded from the Project and will be delivered by the Council's in-house team. An interface schedule has been developed to identify the interaction between the contractor and the Council to support the catering service delivery.
- 3.6.8** Every effort has been made to maximise the possibilities for community use of the project schools. Hospitality Home Economics Rooms, Music Recording Studios, internal sports facilities and other areas will be accessible to the community. Security zones have been designed throughout the schools to allow the shutting off of those areas which will not be used by the community out of hours. In particular, the sports and dance facilities will be able to be accessed entirely without the need to open other areas of the school. Access to Conference Rooms can be gained without opening up any other areas of the school and large welcoming open reception areas will be a feature at Assembly Halls through the use of adjacent dining halls or "internal streets". Floodlighting will be available at the all-weather sports pitches and running track.
- 3.6.9** The Council will be responsible throughout the 30 year operational lifespan of the project for monitoring the performance of the contractor. This will be done by the Schools Estate Unit (see section 3.8 for details). The Council will also have an automatic right to attend meetings of the Board of the Special Purpose Vehicle (SPV), the company established by BAM with the sole function of managing this project. It is recommended that the Council's representative on the Board should be the Head of Service – Resources within the Department of Educational Services.

3.6.10 The following features of the new schools should be noted:

- Schools which are fully accessible and compliant with current DDA legislation. One teaching room of each type will be equipped with height adjustable furniture and fittings and an induction loop. There will be lifts, ramps and numerous DDA toilets (including a full-service DDA toilet in each school);
- space standards for classrooms and social areas are amongst the most generous in Scotland with pupils enjoying an average of 10.3 square metres per pupil (secondaries), 7.9 square metres per pupil (primary) and provision in EECCs in excess of the Care Commission requirements;
- individual class sizes for general purpose classrooms again are higher than the Scottish average and are larger by 5 sq. m. than the current average classroom sizes in the project secondary schools;
- requirements for flexibility built into the authority's requirements ensure that these schools will be able to keep pace with future curricular demands with the minimum of physical disruption;
- a wide range of sporting facilities (internal and external);
- a contractual framework which incorporates a change mechanism which requires the SPV to respond timeously and fully to required changes by the Council, whether of a service or construction nature;
- recorded and measurable performance standards, backed up by a significant and robust system of financial penalties, which allow the Council to ensure that what is paid for is delivered;
- fully costed and funded reactive, pre-planned and lifecycle maintenance over the lifetime of the project;
- service delivery and facilities management guaranteed through the Payment Mechanism, which requires the SPV to deliver high quality services throughout the concession period on pain of significant financial penalty;
- environmental standards which are unprecedented in Scottish schools (see Appendix 12 of Appendix 1 to this Report – Final Business Case).

3.7 Future Development of Schools Estate

3.7.1 Early PFI/PPP projects were heavily criticised for being unresponsive to changing circumstances, thereby making it difficult and expensive for Councils to require contractors to alter aspects of the buildings or of the service provision. More recent projects have benefited from lessons learned from earlier schemes.

3.7.2 West Dunbartonshire's Schools PPP project has, from the outset, aimed to build in maximum flexibility and responsiveness into the building specification and the service provision requirements. For instance, all bidders were required to indicate how school buildings could be adapted to respond to changing legal/contractual requirements (eg on class sizes) or extended to cope with an unexpected rise in school rolls. If, at some point in the future, it

becomes necessary to alter the physical layout of any or all of the schools, or to change aspects of project which are covered by the Project Agreement, this can be achieved using the Change Mechanism.

3.7.3 In January 2008, Council will be asked to approve a Report which will outline a strategic approach to the portion of the schools estate which is not included in the PPP project. This Report will detail a range of options for all schools and will make recommendations as to the preferred options. If approved, this report should enable West Dunbartonshire Council to take advantage of any new funding methods which may be established by the Scottish Government over the coming years.

3.8 Council Project Management Arrangements

3.8.1 Although there will be some reduction in the workload for the Schools' Estate Unit after Financial Close, a significant volume of work will remain in the following areas:

- liaison with HBG Construction during the construction phase of the project;
- monitoring of the construction work to ensure that the terms of the Project Agreement are being met;
- coordination of the schools involved;
- dealing with technical and other problems as they arise;
- finalising of arrangements for transfer to the new school buildings;
- communication with Elected Members, the Council's Corporate Management Team, the Department's Resources Section, school communities and other stakeholders with regard to the progress of the project;
- liaison with the SPV before and after the schools are handed over;
- monitoring of the terms of the service agreement after the schools become operational.

3.8.2 Given the work outlined in 3.8.1 above, and in light of recent advice from the Scottish Government which stresses the importance of effective resourcing and project management on the part of Councils during the construction and operational phases of PPP projects, it is therefore proposed that the following staff should be retained within the Schools Estate Unit after Financial Close under the line management of the Head of Service (Resources):

- Manager of the Schools Estate;
- 2 Project Specification Officers;
- Projects Officer
- Administrative Assistant.

3.8.3 It should be noted that these members of staff would not only be involved in the management of the PPP project, but would also be involved in the development and implementation of "Phase 2" of schools' regeneration and would maintain a strategic management role for the schools estate as a whole.

3.8.4 Beyond Financial Close, the Schools Estate Unit would in addition require the services of the project's Legal Officer on a part-time basis for a period of 2-3 months and thereafter on an ad hoc basis as required by circumstances. It is therefore recommended that an annual sum of £20,000 be budgeted to cover such exigencies.

3.8.5 Similarly, while it is likely that the Schools Estate Unit will have a greatly reduced need to call on the services of the Council's Financial, Legal or Technical Advisers following Financial Close, it is essential that the facility should exist to seek their advice if required. It is therefore recommended that an annual sum of £150,000 be budgeted to cover such exigencies.

3.8.6 The costs involved in the project management arrangements described above have been allowed for within the budget of the Department of Educational Services.

3.9 Handback

3.9.1 The planned concession period for the project is 30 years from the date of the first service availability date. During that period the facilities will need to be kept in a good state of repair.

3.9.2 Additionally, however, the contract recognises that the specification provided to BAM required a design life considerably in excess of the 30 year period and accordingly reflects this by placing an obligation on the SPV to maintain the facilities in a state such as, at the expiry of the concession, they can be anticipated to have a five year period free from any major maintenance.

3.9.3 To achieve this, the Council is permitted in the final years of the contract to draw up a schedule of dilapidations, which will require to be remedied. Additionally, the Council may make deductions from the Unitary Charge under a formula within the Project Agreement. These deductions would be placed in a fund and applied to making good any wants of repair on or prior to the date of the handover.

3.9.4 Whilst ownership of the schools remains at all times with the Council, use of the school buildings is subject to the restrictions found within the Project Agreement. On the date of the expiry or termination of the agreement, the premises will revert to the Council's full and unrestricted use, and as noted in paragraph 3.4.5, all staff employed on janitorial duties will retransfer to the Council.

3.10 Legal and Contractual Framework

- 3.10.1** Unlike Early PFI deals where the parties to the contract were relatively free to set their own terms and conditions provided a sufficient level of risk transfer was achieved, the Scottish Schools PPP market is now heavily regulated, with all deals requiring to adhere to certain documentation and processes.
- 3.10.2** As part of the overall process, the Council has to ensure that sufficient risk associated with the construction, finance and operation of the project is transferred to ensure that the project appears off the balance sheet of the Council and value for money is achieved. Requirements are discussed in further detail in Section 6 of this report.
- 3.10.3** The Principal legal documentation associated with the project into which the Council enters comprises the Project Agreement itself, together with its Schedule and also the Lenders Direct Agreement.
- 3.10.4** The former governs our contractual relationship with the SPV. It captures the positions agreed by the Council and the SPV in relation to the construction of the schools and the operation of the services. It follows the Scottish Standard Schools Contract (version 3) together with Scottish Government required amendments and Project Specific Amendments agreed between the Council and BAM. The Council's In-house and external Legal Advisers are satisfied that the Project Agreement represents a robust and deliverable framework for the delivery of the project.
- 3.10.5** Both sets of legal advisers are also satisfied that the project has been procured within the appropriate legal framework of European, UK and Scottish legislation.
- 3.10.6** Finally, in relation to the legal framework, it should be noted that sub-clauses (a) - (e) of the Recommendations are in a format agreed with the Bank as meeting the necessary statutory requirements, and accordingly if Council is mindful to approve the project, then these provisions should not be altered.

3.11 Financial Framework

- 3.11.1** One of the conditions attached to the Scottish Government offer of Revenue Support Grant is that: 'The project is accounted for as off the Council's balance sheet'. The Council's External Auditor has considered a report prepared by the Council's financial advisers which provisionally concluded that the project should be off balance sheet. This conclusion was endorsed by the Head of Finance. The External Auditor has advised as follows: *'On the basis of the information provided to us, and subject to any further information that may come to our attention during the course of our audit, we have concluded that we are not minded to challenge the Council's view that it will be appropriate for the property provided under the scheme not to be accounted for on the Council's balance sheet.'*

The External Auditor will provide a final opinion prior to financial close of the project.

3.12 Consequences of Delay

3.12.1 While the project team's aim is to arrive at Financial Close before the end of 2007, it should be noted that there are circumstances in which it would not be prudent to proceed to Financial Close within this timescale.

3.12.2 If both the Council and BAM are convinced that they are very close to agreement on all outstanding educational, technical, financial, commercial and legal issues by mid-December, but are not in a position to sign the final agreement, then it may be possible to agree to Advance Works in order to protect the programme (see 3.13 below) in the knowledge that Financial Close is very likely to be achieved early in 2008.

3.12.3 If the Council is convinced that the Council and BAM are further away from resolving outstanding issues, and that Financial Close is unlikely to be achieved early in 2008, then it may be in the Council's interests to delay Financial Close until these issues have been resolved. It should be noted that any significant delay to Financial Close will have cost implications for the Council and is likely to delay the target Service Deliverability Dates of summer 2009 for the secondary schools and of October 2010 for St Eunan's Primary School. However, it should be remembered that this is a 30 year project and it is more important that the final deal represents the best educational, financial and contractual settlement which the Council can reasonably obtain, rather than that the contract is signed on a particular date.

3.13 Advance Works Agreement

3.13.1 One method of reducing the impact of cost overruns, should financial close not be possible prior to the 31st December 2007, is to enter into an Advance Works Agreement

3.13.2 This mechanism permits the construction team to commence operations in line with their programme, in advance of the formal documentation being signed.

3.13.3 It is generally agreed that, in line with best practice, such an agreement should only be used where there are an extremely small number of issues outstanding between the parties, and where it is considered highly probable that these will be satisfactorily resolved within a short timescale.

3.13.4 Typically, works undertaken under such agreements are site preparatory works and earthworks. All such works would be agreed in advance against strict timescales and agreed costs which, assuming Financial Close followed, would be absorbed into the overall payment structure of the project.

3.13.5 Our external legal advisers have indicated that an Advance Works Agreement which allows works to commence on the first projected date for works commencement (7th January 2008) will be deliverable at short notice if this is required.

3.14 Financial Close Procedures

3.14.1 The Financial Close of a PPP project occurs when all commercial and technical positions have been agreed between the parties. It is at this point that the project finances are drawn down and the final financial terms are fixed. The detailed procedures are considered in the following paragraphs.

3.14.2 In a bank financed project, as distinct from one financed through the issue of a bond, there are in fact two immediately consecutive processes: a Commercial Close and a Financial Close.

3.14.3 The Commercial Close will fix the legal and technical obligations on all parties and the parameters within which the financial close will proceed.

3.14.4 Financial Close itself involves the placing of the funding package on the financial markets with a view to fixing the interest rates (“the Swap Rate”) at the most favourable terms possible.

3.14.5 This will involve the advisers for the Council, the Bank and the SPV monitoring the fluctuations in the Capital Markets and agreeing when best to place the funding package on the market. The Council will have a pre-determined maximum rate within which it will be willing to place the deal.

3.14.6 Rates fluctuate throughout the day, and it is a matter of judgement as to when it is best to place the funding package.

3.14.7 If the pre-determined maximum is not met or bettered, or the Council, on advice taken, has grounds to believe that a significantly better deal may be obtained in the very near future, then financial close will not proceed and the process will be repeated on the next day on which the Capital Markets are open.

3.15 Outstanding Issues

3.15.1 While almost all educational, technical, financial, legal and commercial issues have been agreed between the relevant parties, here remain a number of outstanding issues which require to be addressed before Financial Close.

3.15.2 Most of these outstanding issues are routine in nature and will not materially affect the affordability or commercial viability of the project.

3.15.3 Two significant outstanding issues, however, are:

- the remediation of the contaminated land at the site to be used for part of the playing fields at St Peter the Apostle High School; and
- the presence of peat (which potentially affects ground stability) at the same site.

3.15.4 Discussions are ongoing between BAM, SEPA and the Council's Environmental Health officers to determine the most appropriate solution to the contamination. This matter will require to be resolved to satisfy a Planning Condition and to permit Financial Close. An update on this matter and any financial implications will be provided to Council at the meeting on Tuesday 11 December. The solution agreed for the contaminated land will in part determine how the issue of the peat will be resolved.

4. Personnel Issues

- 4.1** As previously reported, the decision to award the contracts for Cleaning and Grounds Maintenance to the Council's in-house team means that only janitorial staff will be transferred to the employment of HBG FM.
- 4.2** TUPE and the STUC/Scottish Executive Protocol will apply to all transferring employees.
- 4.3** HBG FM will apply for Admitted Body Status in relation to the Strathclyde Pension Scheme. It has been successful in previous similar applications.

5. Financial Implications

- 5.1** The financial implications are outlined in Appendix 2 to this Report.
- 5.2** It should be noted that the final cost to the Council of this project cannot be specified at this point. The final cost will be determined by the Swap Rates which apply at the time when Financial Close is achieved. These rates vary on a daily and sometimes on an hourly basis and it will be the role of the Project Team and its advisers to ensure that Financial Close is reached at a time when the rates provide maximum benefit to the Council. Appendix 2 provides details of the implications for the Council of achieving Financial Close when Swap Rates are within the range of 4.89% (the current swap rate) and 5.35% (the highest rate which has applied since the Preferred Bidder was appointed).
- 5.3** As indicated in paragraph 3.3.2, if the current Swap Rates apply, the affordability gap is zero.

6. Risk Analysis

- 6.1 The Council's project team, with the help of its external advisers, undertook a detailed analysis of the risk and Optimism Bias factors which would apply to the Schools Partnership, in accordance with the Treasury Green Book *Appraisal and Evaluation in Central Government* and in particular the Supplementary Guidance contained therein on Optimism Bias.
- 6.2 The analysis determined that the proposed schools development is a Standard Buildings project for the purposes of appraising Optimism Bias (OB). In common with other schools projects, the design and construction of the West Dunbartonshire Schools project is unlikely to involve buildings for which the construction methods or materials used are unique or involve an exceptionally high degree of complexity and/or difficulty. Key factors in the OB assessment included the following:
- i **Project complexity:** if the WDC schools procurement were to be implemented under a direct Council contract, the Council would need to use the Major Contract Form, and be procuring a project of a far greater scale than any it has implemented to date.
 - ii **Contractor Capabilities:** Under traditional procurement, at the time of tender Council would need to be satisfied that the contractors had the required resources, as the Council would have followed the advertised procedures. Under both traditional and PPP procurement routes, the Council would use the Prequalification process to ensure that the tender list comprised experienced contractors with a track record of delivery success at this scale of procurement.
 - iii **Disputes & Claims:** disputes and claims are possibilities under a direct procurement, although this possibility has been partly mitigated by the consultation process to agree the output specification and scope of services.
 - iv **Inadequacy of Business Case:** the Council has only developed a business case for a PPP option. It has not prepared a business case for a Council-procured project, financed within the Prudential Borrowing regime.
 - v **Funding Availability:** the uncertainties associated with funding availability have been partially mitigated under the PPP alternative, as the Council has secured approval for £7.15m p.a. from the Scottish Executive to augment its own resources. For a direct procurement, there would be wider uncertainties with respect to funding availability, which could lead to significant delays and cost escalation.

- vi **Economic factors:** the Council has no control over external economic factors, such as interest and inflation rates, or the extent of construction-specific escalation.

6.3 It should be borne in mind that, while the PPP procurement has been progressed towards Financial Close, no similar development of a Conventional Procurement has occurred since submission of the Revised Outline Business Case. Therefore, were the PPP procurement option to be discontinued, the reality is that it would not be possible to progress a conventional procurement to commence in January 2008, leading to a significant delay in the date at which new schools would become available – and hence a loss of benefits – as well as cost escalation.

6.4 In addition to the OB factor, the Council also assessed the likely risk contingency which should be added to Conventional Procurement Assessment Model (CPAM) cost estimates, and concluded that:

- the total risk percentage on annual facilities management and Life Cycle Maintenance costs is 16.75%; and
- the total risk percentage on capital expenditure (capex) is 11.94%.

6.5 The most significant elements of risk which could be transferred to a PPP partner are:

- during installation and commissioning phase, the risk of increases in materials costs during procurement, and the risk of sub-contractor default;
- during operational phase, the risk of incurring increased costs to comply with contractually specified quality standards, and the risk of increases in the costs of labour or materials to deliver FM services.

7. Conclusions

7.1 Provided the outstanding issues outlined in 3.15.3 can be resolved, it is the opinion of the project team and its advisers that all outstanding educational, legal, commercial financial and technical matters can be agreed in time to allow commencement of works on site on 7 January 2008. This may involve an Advance Works Agreement as described in 3.13 if advisers consider this to be appropriate.

7.2 If work begins on site on 7 January, the SPV should be able to deliver its programme, with school handover dates as outlined in 3.5.1.

7.3 Arrangements also require to be put in place to allow the management of the project through its construction phase and into its operational phase. The necessary arrangements are outlined in 3.6 – 3.6.9 and 3.8 – 3.8.6 above.

7.4 At this stage, it is necessary to define the financial tolerances within which the Council may proceed to Financial Close without further Reports to Elected Members. Allowing for potential costs arising from the outstanding issues and the potential volatility of the financial markets, it would be reasonable to permit the Chief Executive to authorise Financial Close if the total package results in a net annual compounding contribution (ie Affordability Gap) of not more than £26k.

7.5 It is worth noting that, notwithstanding the removal of the Dumbarton Academy campus from the project, this project will still represent by far the largest ever capital investment in West Dunbartonshire's school buildings and will go a considerable way towards addressing the two key issues of dilapidated buildings and overcapacity. While there remains significant work to be done on the remainder of the schools estate, the new schools in this project will set a benchmark for future school buildings and will become the Council's flagship physical resources for many years to come.

8. Recommendations

8.1 Council note the foregoing report and appendices and agree:-

- (a) That, the Council notes the foregoing report relative to the design, construction, financing and operation of three new community learning centres at (1) St Peter The Apostle High School, St Eunan's Primary and St Eunan's Early Education and Childcare Centre, Clydebank, (2) Clydebank High School, Clydebank and (3) Vale of Leven High School, Alexandria and the provision of associated services in accordance with the Government's Public Private Partnership Programme.**
- (b) In pursuance of the Project the Council authorises David McMillan, Chief Executive, to negotiate, agree and enter into on behalf of the Council, and resolves that the Council will perform the obligations contained in, *inter alia*, the Project Agreement (the "Contract") between the Council and West Dunbartonshire Schools Limited, (the "Contractor"), the Funders Direct Agreement between the Council, the Contractor and Dexia Management Services Limited to be provided in connection with the Project (the "Direct Agreement"), all Project Documents to which the Council is a party and all other documents which the Council may require to enter into in relation to the Project.**

- (c) That, the Council has the power to enter into the Contract and the Direct Agreement in terms of Section 1, Section 6, Section 17, Section 20 and Section 53 of the Education (Scotland) Act 1980; Section 14 and Section 15 of the Local Government and Planning (Scotland) Act 1982; Section 69, Section 123 and Section 163 of the Local Government (Scotland) Act 1973; and Section 20 of the Local Government in Scotland Act 2003.**
- (d) That, Stephen Brown, Head of Legal, Administrative and Regulatory Services, Alan Douglas, Manager: Best Value and Special Projects, Nigel Ettles, Principal Solicitor, and/or Sally Michael, Principal Solicitor are duly authorised to sign and deliver on behalf of Council the Contract and the Direct Agreement, the Project Documents to which the Council is a party and all other documents which the Council may require to enter into in relation to the Project.**
- (e) That, the Contract and the Direct Agreement shall be certified contracts within the meaning of Section 2 of the Local Government (Contracts) Act 1997 (the "1997 Act") and shall meet the certification requirements within Section 3 of the 1997 Act and that the said Stephen Brown, Head of Legal, Administrative and Regulatory Services, Alan Douglas, Manager: Best Value and Special Projects, Nigel Ettles, Principal Solicitor, and Sally Michael, Principal Solicitor are duly authorised to sign and issue the certificates in terms of the 1997 Act.**
- (f) That the provision of the Cleaning and Grounds Maintenance Services comprised in MV3 be the responsibility of the Council's In-house service provider and that they operate the services in accordance with the specification and terms and conditions negotiated with the Project Team.**
- (g) That the Chief Executive be authorised to enter into an Advance Works Agreement with the SPV, BAM and/or HBG Construction Limited if deemed necessary and advisable to preserve the programme of works and prevent cost overruns.**
- (h) To approve the Council's Project Management Arrangements for the Construction and Operational phases as outlined in this Report.**

- (i) To approve the establishment of a sinking fund which will receive interest at the Council's rate for interest on revenue balances. This fund will be applied to offset the estimated shortfall between the annual payments in respect of the project and the funding available from the Scottish Government combined with operational/adminitrative cost savings. The insurance receipt from the fire at Vale of Leven Academy will be immediately deposited in the Fund and the sum required from the sale of sites will be deposited as and when received.

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David McMillan
Chief Executive
Date: 6 December 2007

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Appendix 1: Final Business Case (with appendices)

Appendix 2: Financial Tables

Appendix 3: Report to PPP Project Board of 8 August 2007 on Mandatory Variant Bids

Background Papers: Outline Business Case

Wards Affected: All wards