



## **SCOTTISH EXECUTIVE**

Financial Partnerships Unit

**Education PPP Projects  
Pre-Preferred Bidder (PB) REVIEW DOCUMENT**

**June 2006**

## Education PPP Project Review – pre-Preferred Bidder (PB)

### *Introduction*

Councils considering a preferred bidder appointment may find the TTF Guidance Note 4; “How to appoint and work with a preferred bidder”, helpful and a source of useful information.

### *What is the purpose of this review?*

This review should not be regarded as a ticksheet or a pass / fail exercise. It is a tool to assist procuring Councils to pause and consider whether they have taken all possible steps to:

- Secure commitments from the prospective Preferred Bidder, and their funders, that will contain any deal “creep”;
- Clarify the parameters of the commercial negotiations and any outstanding commercial terms and, in particular, secure agreement on the project payment mechanism;
- Give transparency and seek approval on all aspects of the project’s affordability;
- Prevent reallocation of risk, or adverse changes to the project risk profile; and
- Ensure that the successful bid is developed in sufficient detail to minimise any need for Council changes.

In the following sections there are questions for Councils and their advisers to consider as part of a self-assessment.

Councils must have **agreed** any derogation from the SSSC with the Scottish Executive FPU, no later than the date of notification of this review.

### *How will this review be carried out?*

**No later than 4 weeks** prior to the KSR being submitted, Councils are required to give a preliminary indication of a proposed date for submission to:

Director  
Financial Partnerships Unit  
Scottish Executive  
Victoria Quay  
Edinburgh  
EH6 6QQ

**Two weeks before** the review is submitted the Council should confirm the final date to the FPU.

**One week before** the date of the review, the completed Pre-PB Review Document should be submitted to the Director of the FPU in electronic (CD-ROM) and paper format, with the responses given to each question.

A report will then be produced with recommendations. The Council will have the opportunity to comment on this report in draft prior to its submission to the Scottish Executive.

The Council's CE or Chair of the project steering group (assumed in this document to be the project sponsor), should make a written response to the Director of the FPU setting out the Council's response to any recommendations made. The Scottish Executive FPU will review this response and may ask to meet with the project manager, project team, or project sponsor to discuss any arising issues.

Councils should not announce preferred bidder until the Scottish Executive has confirmed that the KSR process has been completed successfully.

Project Outline	
<b>Council</b>	
<b>Project Title and Brief Description.</b> (Please highlight any scope change from that stated at ITPD KSR)	
<b>Estimated Project NPV at ITPD</b> (state discount date assumption and length of appraisal period from Base Date)  <b>Estimated Project NPV at PB</b> (state discount date assumption and length of appraisal period from Base Date)  Indicative 1 <sup>st</sup> full year Unitary Payment at ITPD (in real terms at Base Date)  Indicative 1 <sup>st</sup> full year Unitary Payment at PB (in real terms at Base Date)  Note; relate any material changes to scope changes noted in Project Description question.	

<b>Project Manager Contact details</b>	Name  Address   Tel E mail
<b>Second contact</b>	Name  Address   Tel E mail
<b>Project Sponsor</b>	Name  Address   Tel E mail

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## **SECTION ONE: PROJECT UPDATE**

**Key objective: the purpose of this section is to refresh the understanding of the project, to ensure the project risks are understood clearly and that there is transparency on any changes to project scope.**

1. A number of recommendations were made as part of the ITPD review of this project. Please list those recommendations as bullet points along with a brief summary on the outcome of the issues.
2. How many bids were received at ITPD, and submitted at Final Tender? Please detail number of bidders and number of variant bids, both mandatory and non-mandatory.
3. Is it the intention of the Council to progress with the original core bid or with a variant bid (if a variant please describe the variances together with the enhancements that the variants deliver including VfM and risk transfer benefits)?
4. Has the project scope been altered since the pre-ITPD KSR? If so, please detail and explain why.
5. In the view of the project team, which risks present the greatest threat to the project achieving a timely financial close?

## SECTION TWO: AFFORDABILITY

**Key objective:** The purpose of this section is to provide the Project Sponsor with a number of tools with which to assess the certainty of the stated affordability position of the project, and to highlight to the Project Sponsor that any lack of certainty, or changes to scope mid-procurement inevitably have delivery and affordability risks attached. It also seeks to verify Council support for the financial implications of the project on Council finances going forward.

6. Have there been changes to the affordability envelope committed to the project since ITPD?
7. Has the project all the required Council approvals to proceed to financial close, and are those approvals given on the basis of the stated affordability position, including the costs of retained services? Please confirm that a Council minute is available supporting the affordability implications of the Preferred Bidder's proposals.

Are there any conditions attached to the terms of the approvals?

8. Please confirm that the affordability envelope for the Project is deliverable based on current projections.
9. What is the Council's projected first full year affordability ceiling and what subsequent indexation adjustment is applied to this?
10. What is the first full year and subsequent year on year affordability surplus / gap, if any? Please explain how the affordability gap is being met and if it involves any capital injection? Please complete the table below to illustrate this answer. *(Figures shown for illustration only, please assume interest rate as in model approved by Council and state same.)*

Year	1	2	3	4	
<b>£m's</b>					
<b>Est. (first full year) UC</b>	7.0	7.3	7.5	7.8	
<b>Rev support</b>	3.5	3.5	3.5	3.5	
<b>Budget transfer</b>	2.5	2.6	2.7	2.8	
<b>Est. Affordability Gap</b>	1.0	1.2	1.3	1.5	

11. What is the "headroom" for the Council's current project affordability position in the PFI financial model (please state interest rate buffer assumption used and reference interest rate)?
12. What have been the major cost movements since the issue of the ITPD and Final Tender documents?

(This response is to be broken down into nominal capital cost, average real lifecycle costs and average real FM costs; explanation of any material movements in these should be noted).



13. Are all the cost inputs and financial assumptions (including risk pricing) in the Council's PSC up to date and do they mirror the specification that the Preferred Bidder has priced?
14. How long is the preferred bid valid for?
15. How long is the construction price valid for? What caveats attach to the construction pricing? For instance, is it subject to further surveys?
16. How are delays in financial close and indexation of input costs to be treated?
17. What is the protocol for cost increases due to Council variations post-PB appointment?
18. Is there a protocol in place for tracking funding rates and their implications on affordability throughout the commercial negotiations through to financial close?
19. Are there any other anticipated issues that may have an adverse impact on affordability, such as:
  - o outstanding surveys;
  - o insurance pricing;
  - o funding availability;
  - o town planning;
  - o design development;
  - o specific variations; and
  - o commercial matters outstanding?
20. Does the project team have any specific concerns regarding sub-contractor commitment to the cost and commercial terms of the preferred bidder's offer?

### SECTION THREE: COMMERCIAL / LEGAL ISSUES

**Key objective: the purpose of this section is to ensure that the parameters of the commercial negotiations are agreed and understood by all parties and to highlight areas which, if not resolved at this stage, can lead to deal creep and delay. These particular commercial issues are also a test of support at sub-contract level.**

21. Has a list of commercial issues for negotiation been drawn up and agreed in writing by the proposed preferred bidder (PB), its sub-contractors and lenders? Has the proposed PB indicated, in writing, its willingness to sign the commitment letter (SoPC 3 clause 33.3)?
22. What are the key commercial issues outstanding, and has the potential cost / time impact of outstanding issues been considered? Specifically, is the position on the following commercial terms confirmed and agreed in accordance with SSSC?
  - vandalism
  - termination triggers
  - third party income
  - benchmarking of soft services
  - energy/utilities
  - handback provisions
  - change mechanism
  - capital receipts
  - latent defects
  - refinancing
23. Does the current position on insurance reflect SE guidance on benchmarking and premium sharing?
24. What risks, if any, have been deemed uninsurable?
25. Have any derogations from the Scottish Standard Schools Contract been agreed with the Scottish Executive in advance of this review?
26. Is the payment mechanism, and its related calibration, agreed by the proposed PB, their sub-contractors and lenders?
27. To what extent has the PB demonstrated scenario testing of the Payment Mechanism calibration?
28. Has a programme been produced by the proposed PB (and agreed with their funders) for the various due diligence processes required to reach financial close? Is it realistic and is it synchronised with the overall projected timescale to reach financial close?
29. What is the proposed PB's track record in closing out commercial deals and does this support its proposed programme to close?
30. Has the senior lender accepted the draft Direct Agreement and are there any derogations from it?

31. If the Council funding contributions (e.g. from release of land and subsequent sale, from cash resources) are included in the project, are the arrangements in respect of the Council contribution in accord with the Scottish Executive guidance note? Do the arrangements demonstrate VfM? Are the arrangements recorded in the Project Agreement and agreed by the preferred bidder including the funders?

## Funding

**Key objective: The purpose of this section is to highlight to project sponsors some of the complexity involved in determining the most advantageous funding solutions for a project and to stress the need for strong management and input from the Council in determining the final funding solution.**

32. What is the current agreed or anticipated funding route to be utilised to close the project? Does the Council have full understanding of the proposed funding route, in particular its certainty in relation to pricing?
33. Was it evident from the bid submissions that a funding competition was run during the Dialogue phase to procure the best value and most deliverable funder and funding route (for example between respective banks and then bank vs. bond)?
34. If different sources of funding sources were competed / offered in the bidding competition, did the Council ensure that the underlying costs of funds e.g. bank rate vs. Gilt rate) were quoted on a consistent basis? Were sensitivities run on the areas of funding that cannot be controlled in the period to financial close (e.g. bond margin, underlying gilt and interest rates)?
35. Did the Council review the funding terms in light of the current funding market for education PPP Projects (in particular underlying credit ratings, funding tail, average DSCR and timescales to deliver the funding route through to financial close) as well as considering qualitative factors such as flexibility for additional funding, refinancing gains etc.
36. Is it appropriate to delay the selection of the final funding route (e.g. bank or bond, or fixed gilt vs. index linked bond) to a defined period post preferred bidder? If so, is a protocol in place to select the final funding route and is the detailed in the PBL?
37. Were all funders' comments sought (and given) on the contract?

## Employment

38. Is there any public sector involvement in delivery of FM services? If this is the case, please clarify:
- What services are involved and by what method the public sector involvement will be implemented.
  - The quantification process, and results, of the analysis of the risks for the public sector.

- That the service interface schedules have been drawn up in detail and agreed with the proposed PB
39. Are there staff transfers to the private sector? If this is the case, is there accurate and comprehensive staffing information available and, if so, is that information warranted? Has the PB accepted the employment provisions as drafted in SSSC?
  40. Does the proposed PB's programme to close take account of the required levels of staff consultation?
  41. Does the proposed PB's programme to close take account of the time required to achieve admitted body status of the LGPS (if applicable)?
  42. Have all the requirements, set out in the Staffing Protocol been adhered to? Please specify any deviations from the Protocol.
  43. Are there any unresolved staffing issues?

## SECTION FOUR: FINANCIAL / RISK ISSUES

**Key objective: The purpose of this section is to clarify that project risks are transparent, understood, quantified, and that an off balance sheet position will be achieved.**

44. What is the anticipated VfM position of the PFI solution in comparison to the risk adjusted PSC?

Were all bids evaluated on an equal and risk adjusted basis?

45. If applicable, what were the significant comparability adjustments to the proposed PB's submission (both against other bids and against the PSC)? Have any required adjustments been incorporated into the PSC and has the impact on the Council's retained risk and any related affordability / VfM implications been considered? (For example the impact of removal of a service, etc.)?

46. What % of the overall project cost is the value of risk in the PSC?

47. Has the Balance Sheet implications of the project been considered? What is timetable to secure and to provide the final Accounting Opinion report?

48. Has the Council run an up to date VfM analysis in accordance with SE guidance to verify the robustness of the investment decision, reviewing:

- qualitative VfM
- quantitative VfM?

### **Bidder's financial model**

**Key objective: To ensure that the bidders' financial model is complete and that the inputs are robust.**

49. Are the Council and the project's advisers, satisfied with the sufficiency of:
- The cost inputs (up-front capital)
  - The quantum of average annual operating costs
  - The Life Cycle Maintenance fund and profile
  - Assumptions underpinning the purchase and refresh of fixed and loose furniture and equipment (if applicable)
  - The robustness and deliverability of funding proposals
  - Tax efficiency of bidders proposals
  - The robustness of the financial model and its reflection of term sheets, etc.
  - That Financial Close procedures will be put in place to ensure that any figures in the PB's financial model which are required to be inserted in the Project Agreement will be readily identified and defined
  - SPV, bid and management costs
50. Has the proposed PB demonstrated that its building, FM sub-contractors and equity investors, agree to their price and key terms and conditions upon which they are being appointed and is this reflected fully in the financial model?

What evidence does the Council have to support this?

51. Has the proposed PB confirmed that composite trader tax treatment has been used as an assumption in their model, and if so, has the full benefit has been passed onto the Council? Has this been verified by the Council's financial advisers? Has a programme been confirmed for receiving COP 10?
52. What is the rate of Blended Equity IRR (nominal pre tax) in the prospective PB financial model?

## **SECTION FIVE: TECHNICAL ISSUES**

### **Built solution**

**Key objective: to ensure that the proposed PB has developed their design solution in sufficient technical detail, to the satisfaction of the Council, minimising the need for any change in the run-up to financial close.**

53. Is the Council and its technical advisers satisfied with the quality and level of detail supplied in respect of the design and build solution?
54. Are the footprints of the designs frozen?
55. Do any major concerns remain on the extent or quality of the technical information of the proposed PB submission, if so, what are they?
56. Has there been full evaluation carried out on the proposed PB construction cost assumptions? Were there any concerns as a result of the evaluation?
56. Are there any more technical surveys due to be undertaken by the proposed PB?
58. Is the Council, and their education advisers, satisfied with the construction method statements as they relate to any interface with the delivery of education?
59. Do any of the statutory consultees have significant objections to the designs as they stand?
60. Are the project room data sheets complete and the content agreed by the preferred bidder?  
  
If not, what remains outstanding?
61. Is there detailed information and full agreement on the level of provision, and ongoing maintenance, of fixed and loose furniture?

*Please explain the level of development that has been reached.*

62. Is there an agreed method of costing any Council changes in the run-up to financial close and during the construction period (and does it exclude prelims)?

### **Facilities Management and LCM**

63. Has the proposed PB, its sub-contractors, and its funders accepted the output service specification and associated rectification times?
64. Has there been full diligence carried out on all FM and LCM costs by the Council's technical advisers?
65. Are the services to be benchmarked clearly defined and the position on benchmarking agreed? Is the cost basis for benchmarking realistic?

## SECTION SIX: DELIVERABILITY

### Project Management

**Key Objective:** The purpose of this section is to highlight to the project sponsor that managing the project to a successful financial close requires careful risk and project management. A clear project plan with a risk management strategy embedded in it should be used by the Council to drive the process towards a timely, and advantageous, financial close.

66. How is the Council going to drive and manage the process from PB announcement to financial close? Is a detailed project management plan in place, including:

- schedule and management of all commercial meetings
- procedure and timescale for any Council approvals
- action lists for legal, financial and technical
- clarity on the PB's proposed due diligence processes

67. Have the procurement risks for this stage of the procurement (anything which may impact on a smooth run-in to financial close) been analysed by the Council and risk management plans put in place?

*This may relate to late delivery of a school, increased costs, unavailability of a site etc.*

68. Are there any outstanding land issues?

69. Is any land included as part of the deal and, if so, what conditions attach to the realisation of the agreed value?

70. Is there a mechanism for pricing variants on land value prior to close?

71. If land is being excluded from the deal, has the Council analysed the risks to the required values being realised? (For instance, ownership issues, valuation issues, environmental issues, internal pressures etc)

72. Can the proposed PB fetter land value in any way?

73. Can the designs now be submitted for Full Planning Permission?

74. Are there any outstanding planning or related land issues, which cause the Council or its advisers concern? (If so, please detail.)



## **SECTION SEVEN: FEEDBACK**

*In order to improve this review, and assist other Councils, your assistance in completion of this section is appreciated.*

75. Are there any particular aspects of the preferred bidder stage of PPP not covered by this review, which you feel should be?
76. Which part of the review did you find the most thought provoking or useful?
77. Which part of the review did you find the least helpful?
78. Do you have any other comments you would like to make?