

NHS Scotland Revenue Finance Briefing Session

SGHD: Mike Baxter

SFT: James King, Viv Cockburn

18 April 2011

Welcome and Introduction

MIKE BAXTER
SCOTTISH GOVERNMENT HEALTH
DIRECTORATE

- Introduce speakers
- Objectives for today
 - Raise awareness and understanding of the key issues
 - Gather issues from the Service
 - Outline development work required
- It is the Start of a journey !!!!
- Agenda for today

1. Welcome and Introduction
2. What are revenue funded projects?
3. hub DBFM contracts – how do these work?
4. How will projects be selected for the different funding structures?
5. Governance arrangements and business case processes?
6. What does this funding approach mean for your schemes?

- UK CSR Settlement – 36.5% real terms reduction in capital
- Demand for infrastructure investment increasing and high levels of commitment in the system
- Review of capital planning 2010 – preparing for the inevitable
- The mixed economy approach to public capital and revenue finance
- £2.5bn pipeline – a planned and sustainable approach to revenue financed investment
- A corporate approach across SG

QUESTIONS AND ANSWERS

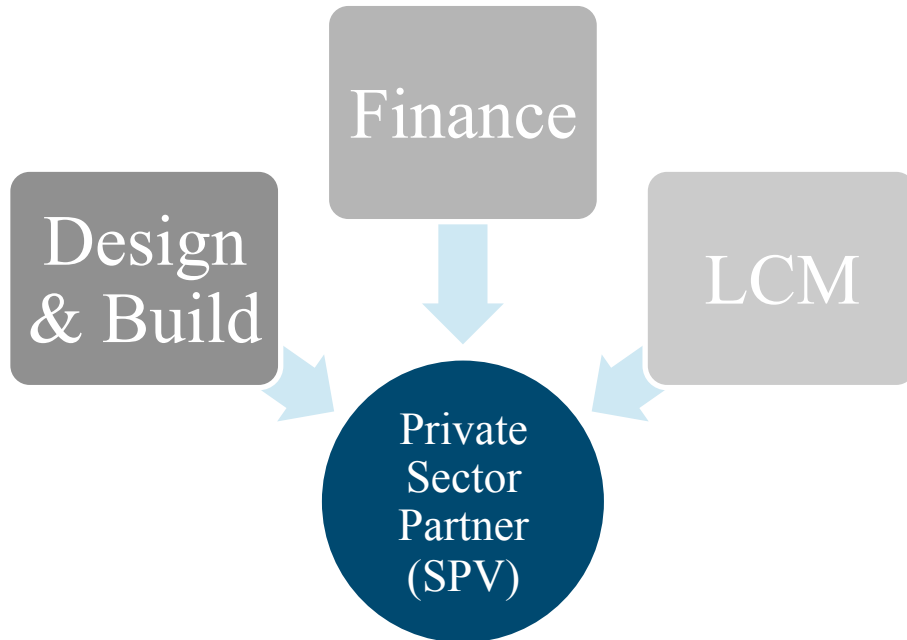
What are revenue funded projects?

VIV COCKBURN
SCOTTISH FUTURES TRUST

What are revenue funded projects?

1. How do revenue funded projects work?
2. What revenue funded project structures are available?
3. How do revenue funded NPD projects work?
4. What are the differences between NPD projects and hub DBFM projects?
5. How will these projects be different to previous PFI/PPP models?
6. What services will be procured under revenue funded projects?

How do revenue funded projects work?

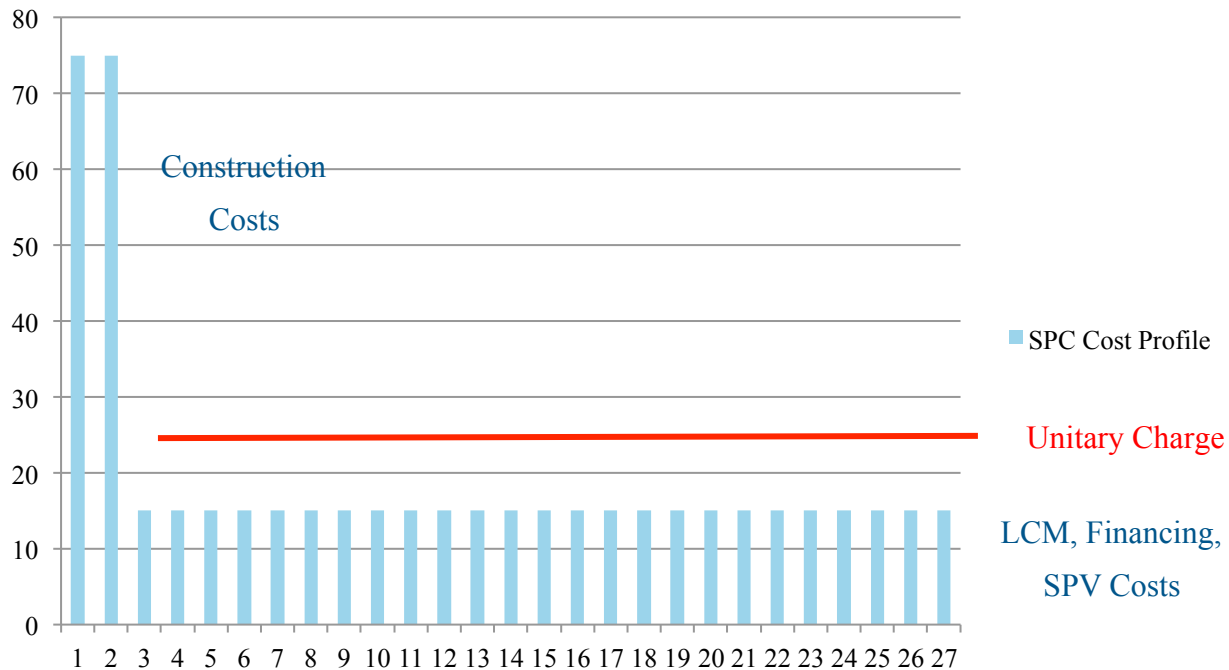


Procuring Authority:

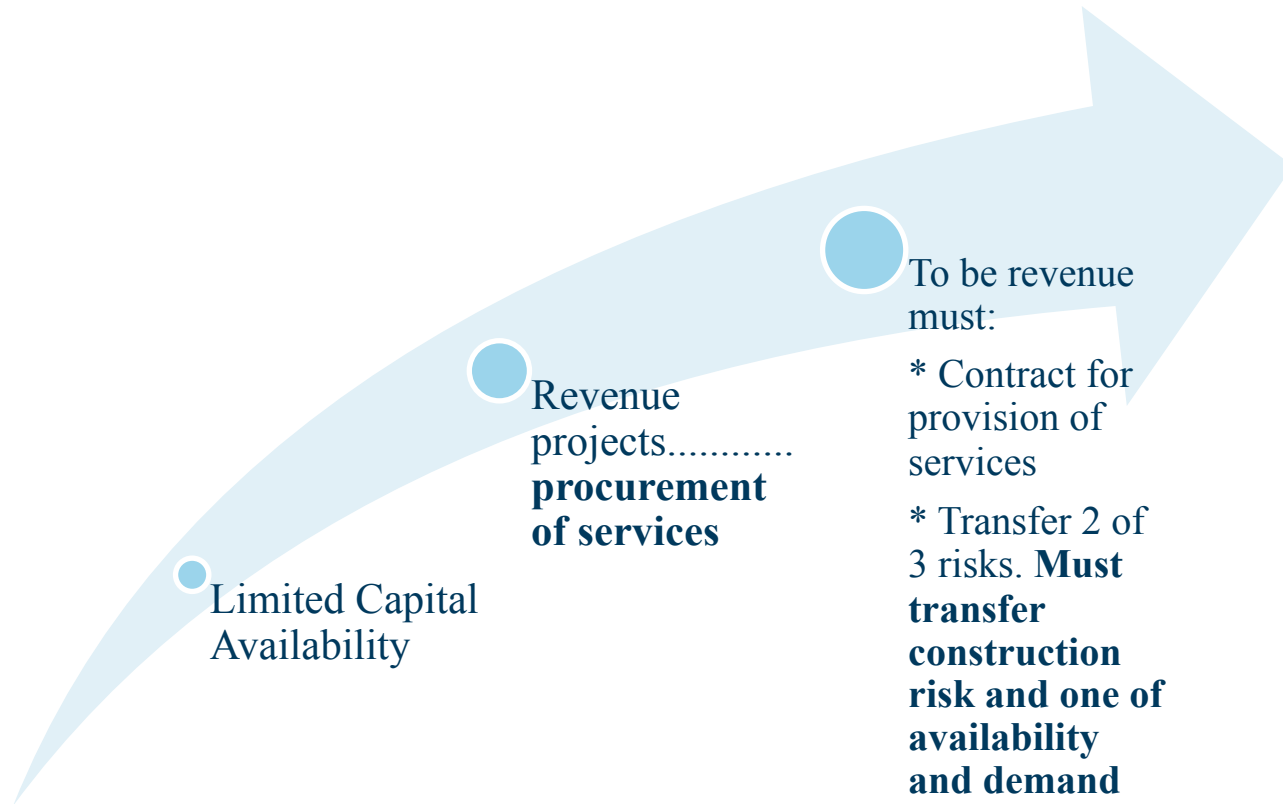
- Pays monthly for the services over the contract period
- The monthly payment is subject to:
 - Performance deductions
 - Availability deductions

How do revenue funded projects work?

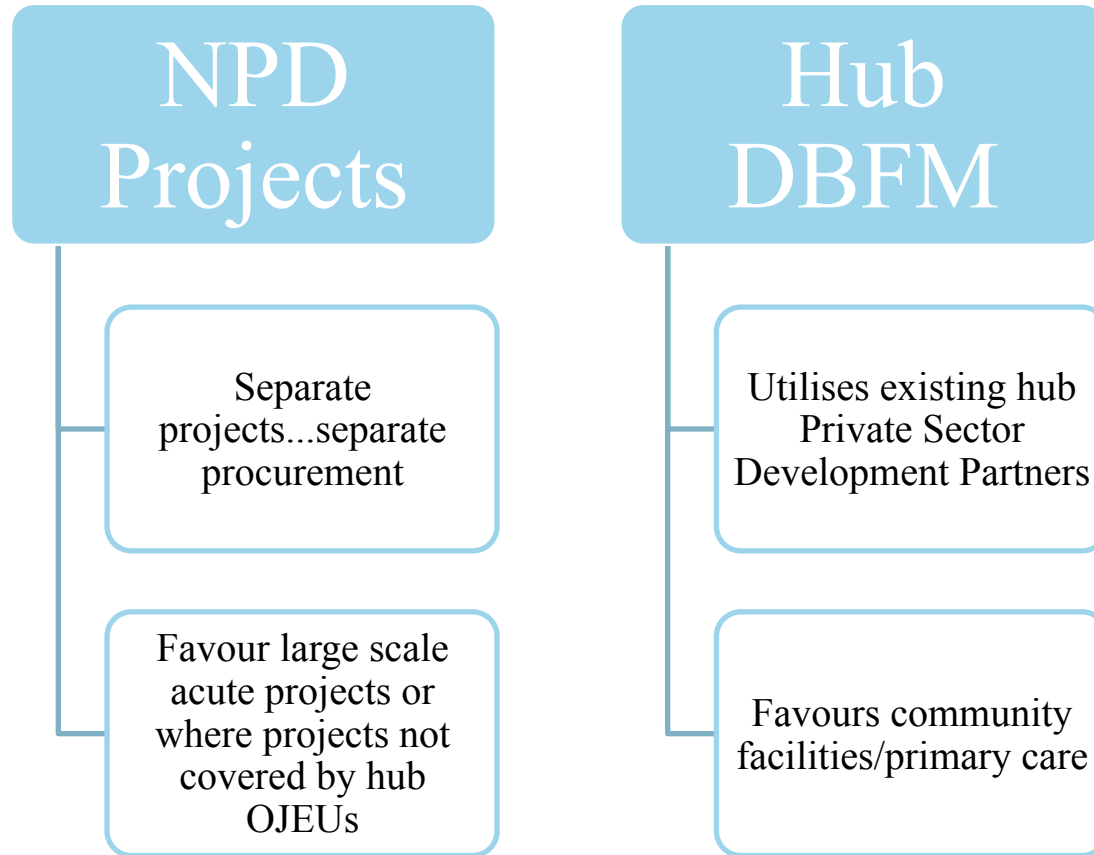
SPC Cost Profile



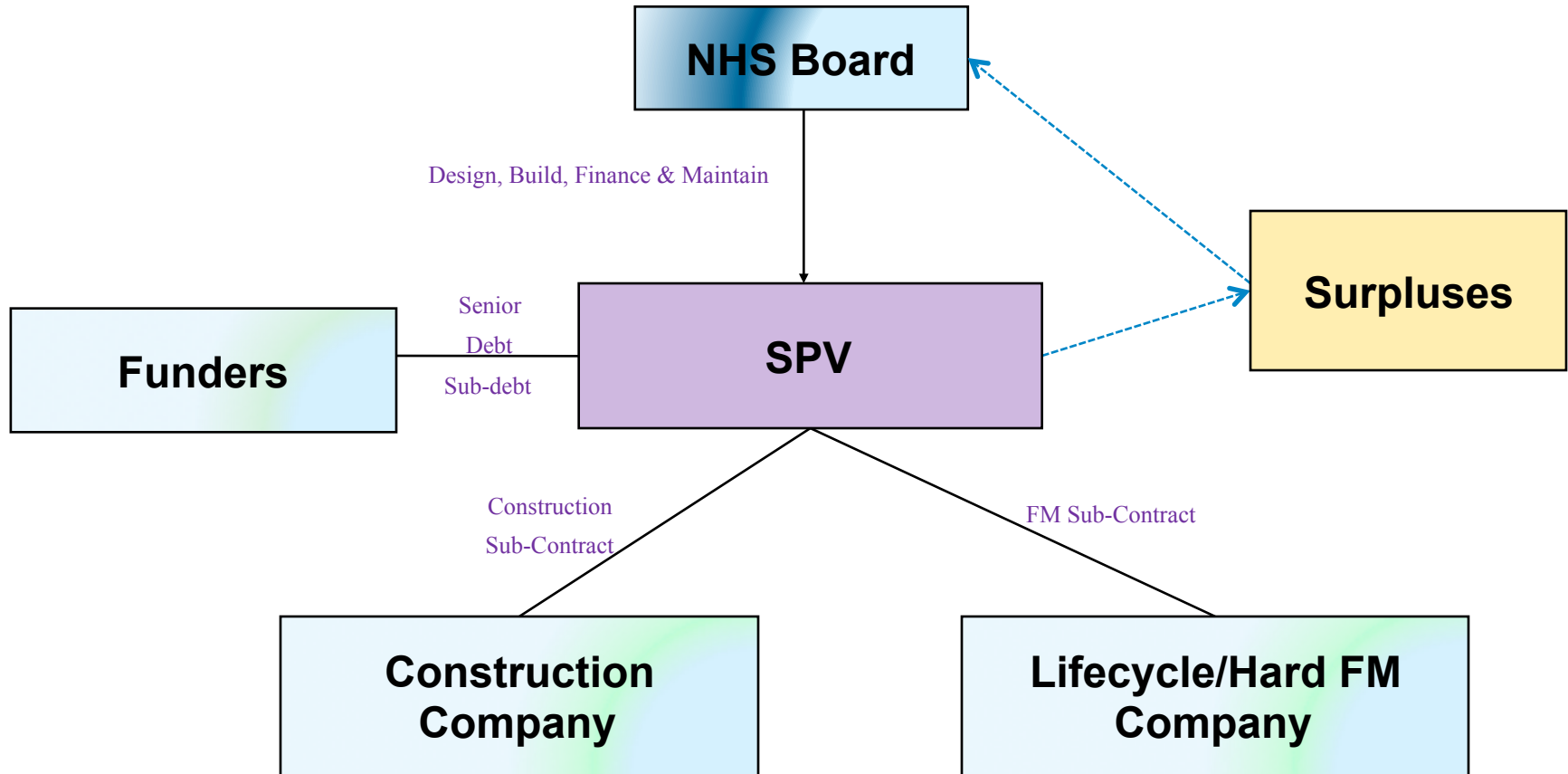
How do our projects become revenue funded?



What revenue funded project structures are available?



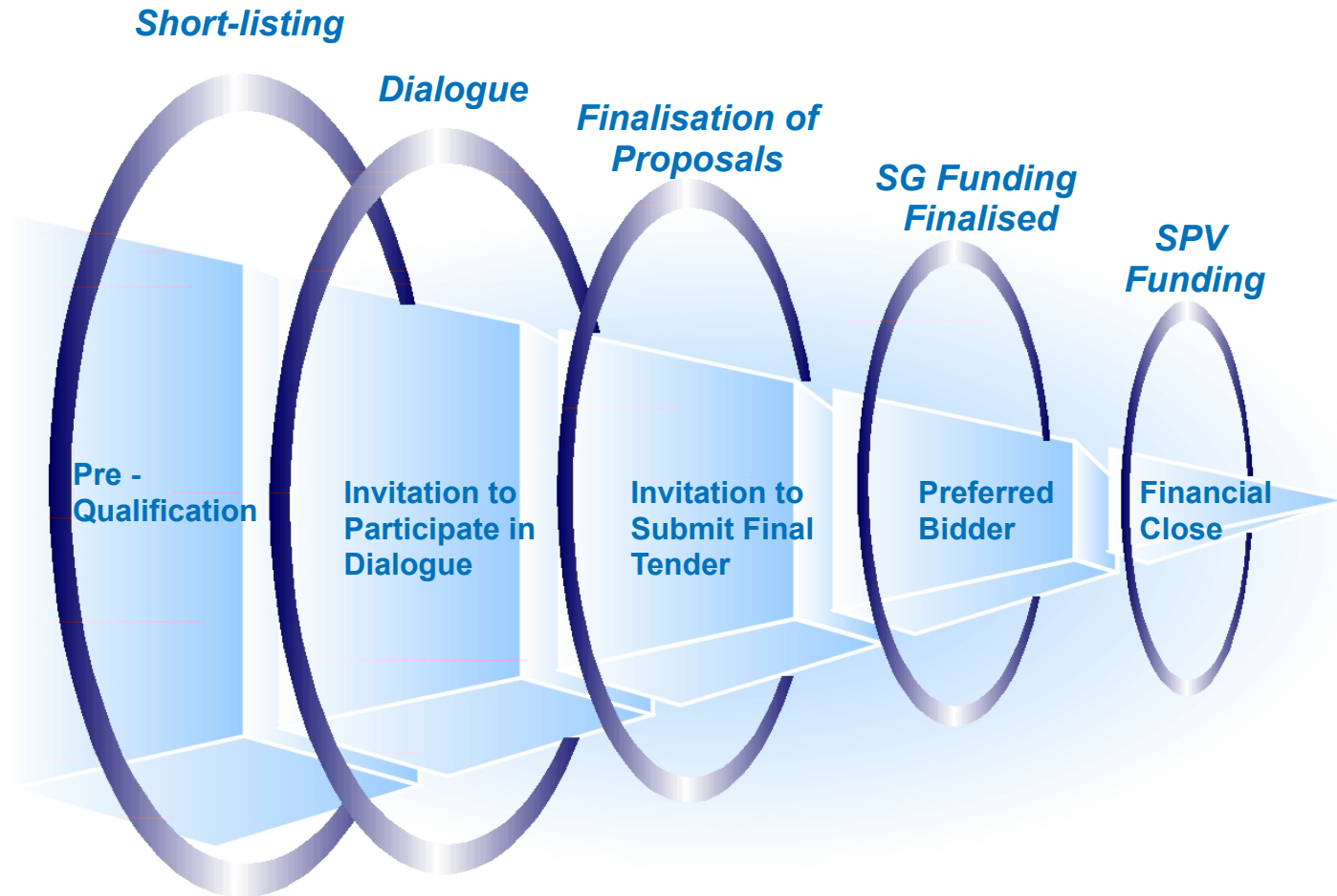
How do revenue funded NPD projects work?



What revenue funded projects are available?

	NPD	Hub DBFM
Contract Structure	Project Agreement for a design, build, finance and maintain contract	Project Agreement for a design, build, finance and maintain contract
Principles	Not for Profit Distribution Surpluses over the contract are returned to the procuring authority/SG	Delivered by hub partner. Sharing mechanism for surpluses.
Ownership & Funding	No public ownership or funding of SPV	SPV – 100% owned by hubco. hubco is 40% owned by the public sector. Public funding up to 4% of SPV.
Representation on Board	Public Interest Director	2 Public sector directors
Procurement Approach	Competitive Dialogue	Partner already procured /in procurement / pre-procurement

Procuring NPD Revenue Funded Projectscompetitive dialogue



How will they be different to previous revenue funded projects?

Contract

Previously:
NHS Scotland
Standard Contract

Now: hub DBFM/
NPD Standard
Project Agreement
Consistent across
sectors

Services

Previously: hard
FM, LCM,
catering, cleaning
security etc...

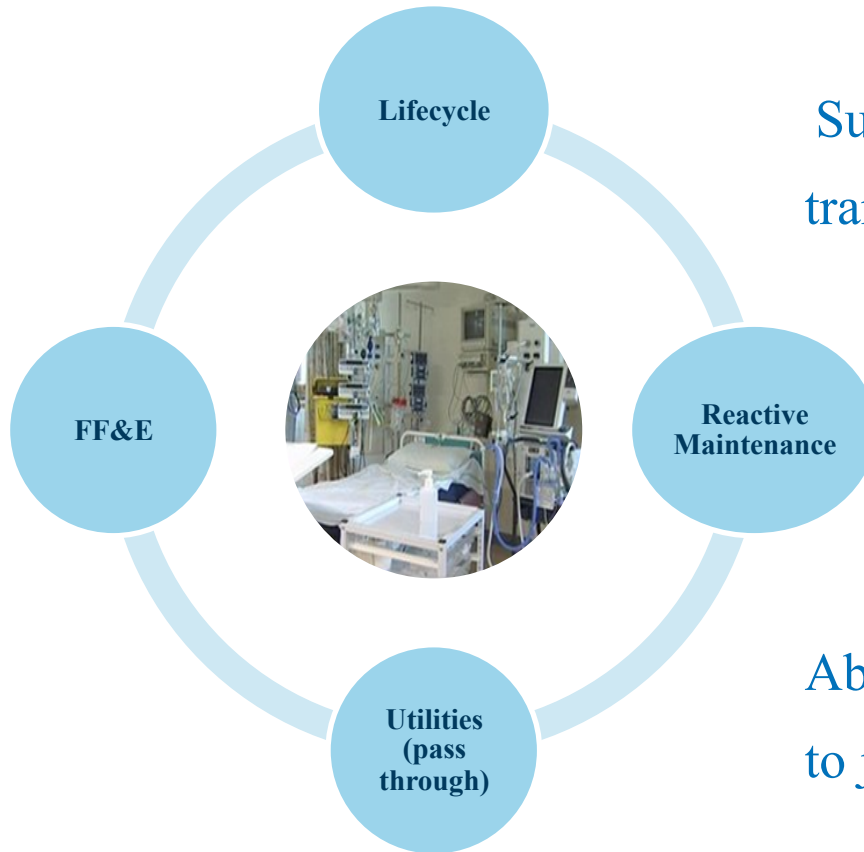
Now: hard fm &
LCM. Narrower
range

SG Funding

Previously: funded
by NHS Boards

Now: SG funding
package consistent
across sectors

What services will be procured?



Sufficient service provision and risk transfer to meet ESA95 requirements

Ability to include other services but need to justify on VfM grounds

QUESTIONS AND ANSWERS

COFFEE BREAK

Hub DBFM Projects

JAMES KING
ASSOCIATE DIRECTOR
SCOTTISH FUTURES TRUST

Session Agenda

- Exclusivity
- Brief outline of hub structure
- Delivery of Value for Money and affordable projects under hub DBFM
- Process of procuring DBFM projects under hub
- Brief discussion in respect of hub DBFM Contract

hub Programme

“working together to build better buildings, for better Public Services, for communities across Scotland...”



Qualifying Projects

- All Participants - Identified Projects (those in the current TDP)
- NHS – >£3.5m capital value for primary or community health services in first 10 years of Hubco (different for South East, North and East Central hubcos)
- Joint NHS and Local Authority if >£3.5m value and lead participant is NHS (different for South East, North and East Central hubcos).

- 10 years from Commencement of Territory Partnering Agreement (TPA)
- Provision of all On-going Partnering Services;
- Project Development Partnering Services for Qualifying Projects (i.e. bring forward proposals for these new projects);
- Project Services for Qualifying Projects that become “Approved Projects” i.e. if approved the project will then be procured via a “Project Agreement” (DB/DBFM) between the Participant and hubco (or a subhubco) who will then subcontract to Supply Chain.

hub – project development process

New Project Request

- **Affordability Cap**
- Brief
- Programme
- Preparatory work done ?
- Novation options ?
- agree comparators and adjustments for Project Development fee

Stage 1 Approval

- **Agree affordability cap**
- Agree **comparators** for elements/ components of the new project and agree any adjustments.
- **Pricing cap adjustments**
- Option Appraisal
- Initial design & feasibility
- Develop preferred option
- VFM assessment

Stage 2 Approval

- Develop design
- Pre-planning Consultation
- Planning Consent
- Procure Contractor
- Confirm VfM
- Procure FM Contractor
- Procure Funding

Contract Finalisation

- Financial Close
- Conditions Precedent
- Documentation
- Resolving residual risks
- Arrange Finance

Delivery of Value for Money

- Value for Money at Project Level
 - Key part of both Stage 1 and Stage 2 submissions
- Method
 - Comparators
 - Taken from appropriate parts of pricing data
 - Benchmarks - Previous hub projects/other market data (e.g. BCIS indices)
 - Costs always shown on open book basis, showing steps taken at supply chain to get VFM and continuous improvement
- Market Testing
 - At Participant request
 - Procedure for agreeing evaluation, selection, tendering etc
- Value for Money at Pipeline Level
 - Driving improvements in design
 - Driving reduction in construction and hard FM costs

Ongoing

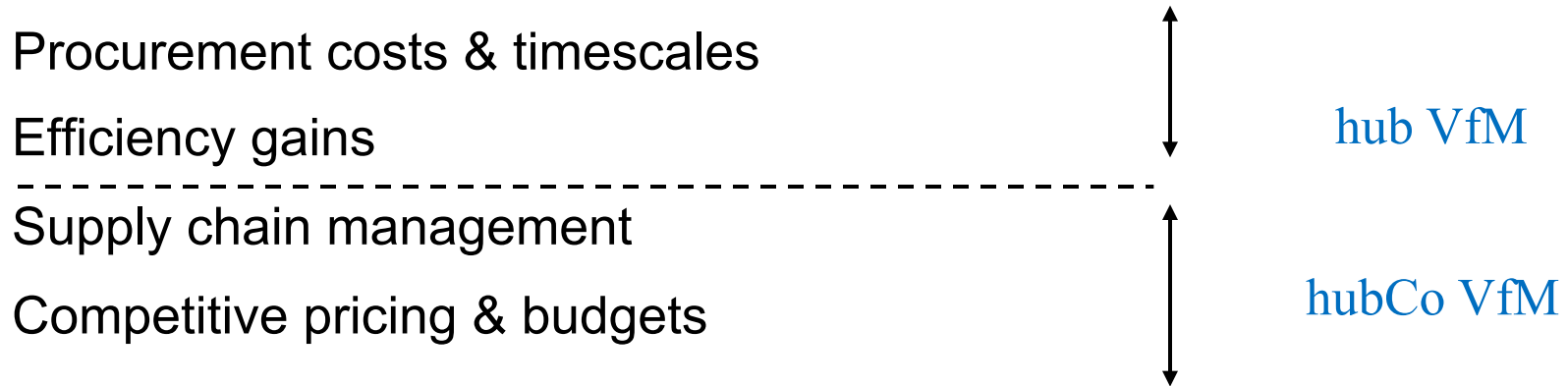
- Develop Territory Delivery Plan with Participants
- Supply Chain Management
- Support TPB

Project Development

- New Project Development/Delivery (*hubco does not need to tender for work – no OJEU*)
- Supply Chain Selection
- Funding

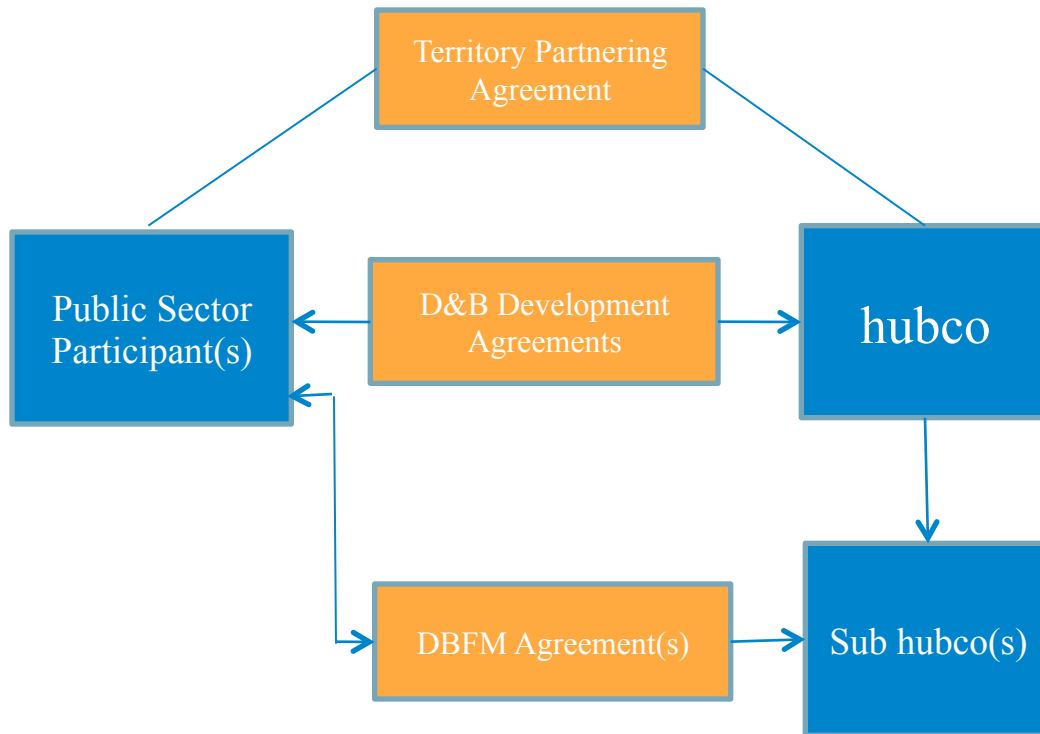
Strategic Support

- Strategic Estate Planning – if requested
- Service Planning – if requested



- Procurement costs & timescale savings
 - minimum 100 day savings on OJEU process.
 - Relationship exists with hub co working alongside Participants
 - Early engagement of supply chain
 - Volume of projects through increases procurement savings.
 - Less procurement risk & cost
 - Procurement measured through KPI's

- Robust tiered approach
 - Tier 1, Tier 2 & Tier 3
- Contractors & consultants all signed up at FC
- Commitment to deliver and tied to KPI's
- Members appointed on a competitive basis, inc cost, quality, partnering, etc
- Measures in contract for reviewing & refreshing



Territory Partnering Agreement

- Contains process for hubco to develop proposals for New Projects at request of a Public Sector Participant
- Contains approvals process for New Project proposals developed by hubco
- Contains Template D&B Development Agreement and Template DBFM Agreement to be entered into once hubco's proposals for a New Project have been approved

D&B Development Agreement

Design and Build contract entered into between the relevant Public Sector Participants (i.e. those procuring the facilities in question) and hubco on New Projects that are capially funded

DBFM Agreement

Design, Build, Finance and Maintain contract entered into between the relevant Public Sector Participants (i.e. those procuring the facilities in question) and Sub hubco on New Projects that are revenue funded. The expectation is that special purpose vehicles will be established by hubco (and wholly owned by hubco) for delivering DBFM projects.

Project Delivery – DBFM

Design, Build, Finance & Maintain Agreement

Lead Participant

Hubco
100% Sub-hubco Equity

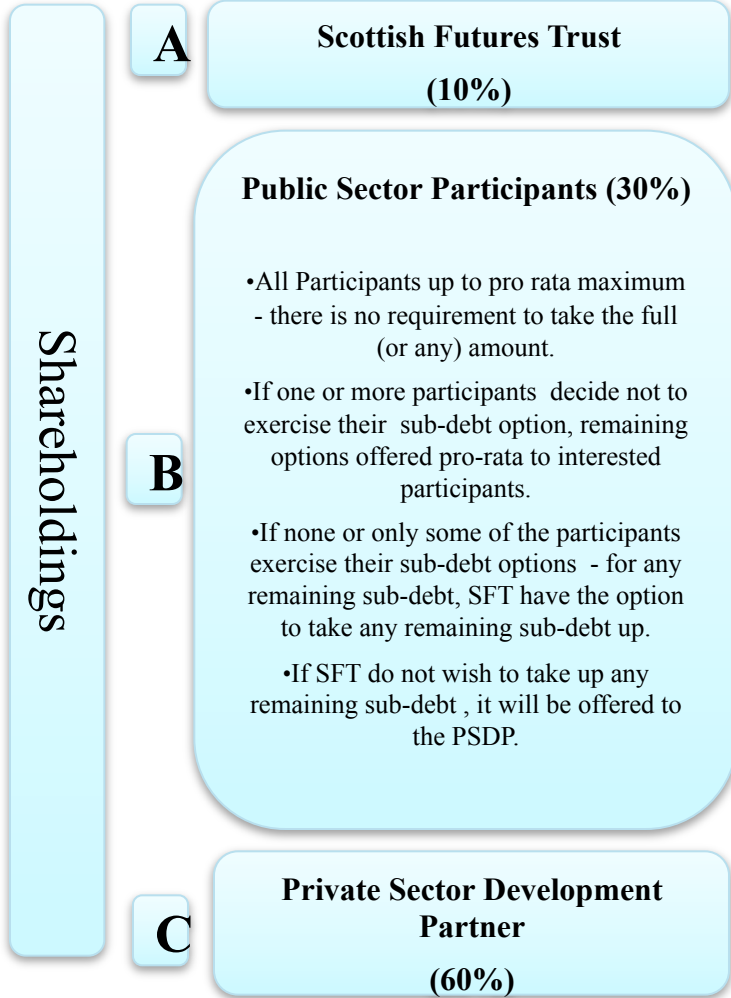
Sub-hubco

Sub-debt Provision

Sub Contracts

Construction Contractor

FM Contractor



Lead Participant

- Where there are joint projects, the TPA envisages that only the Lead Participant will enter into the DBFM;
 - Joint Working Arrangements – not pre-determined;
- Key areas to cover will be:
 - liability for payment to hubco under DBFM, VAT;
 - issues that require joint consent/issues that Lead Participant can agree unilaterally;
 - reliance by non-Lead Participants on hubco (and supply chain)

- Once a New DBFM Project is approved a project-specific “subhubco” (wholly owned by Hubco) will enter into the DBFM with the Lead Participant procuring that New Project;
- DBFM Based on Standard health PPP contract with revisals e.g.;
 - Authority takes unforeseen capex change in law risk during operational period
 - IRR cap and collar
 - Other adjustments to reflect current market position and provisions for Local Authorities
- In terms of DBFM, where hubco is to secure funding, these contracts are known and acceptable to commercial funders in the projects market;
- Project specific provisions require to be negotiated on a project by project basis.

QUESTIONS AND ANSWERS

MORNING SESSION WASH UP

LUNCH

How will projects be selected for the different funding structures?

MIKE BAXTER
SCOTTISH GOVERNMENT HEALTH
DIRECTORATE

Three stage process

1. High level analysis based on existing value for money guidance referred to in the Scottish Capital Investment Manual (SCIM) based on review of existing capital plans
2. More detailed assessment of suitability based on characteristics, scope and scale of projects
3. Business case process as per existing approvals process

CSR Period – funding for legal commitments and formula – assumption of no capital for new developments

Hub is a programme based approach to development – not all projects currently identified

Review of scope and nature of those projects unsuitable as currently configured

Ultimately needs not wants – links to service strategy and supported by robust Property and Asset Management Strategies (PAMS)

Deciding between hub DBFM or Stand alone NPD

Is it within the scope of the hub procurement?

Scale – too small – too big?

Stand alone NPD – min £20m

Opportunities for bundling/ batching via hub

QUESTIONS AND ANSWERS

Governance arrangements and business case processes

MIKE BAXTER
JAMES KING
VIV COCKBURN

1. General issues
2. External reviews (Gateway Reviews and Key Stage Reviews)
3. Approvals processes (NPD & hub)
4. Business case processes
5. How will hub DBFM' s and NPD projects be assessed for vfm?
6. How will hub DBFM' s and NPD projects be assessed for affordability purposes?

Not operating in vacuum – we have processes in place to deal with revenue financed projects – gives us a good foundation on which to build

Changes needed to respond to provision of funding and degree of challenge exerted

Clarity of roles and responsibilities – integrated processes essential

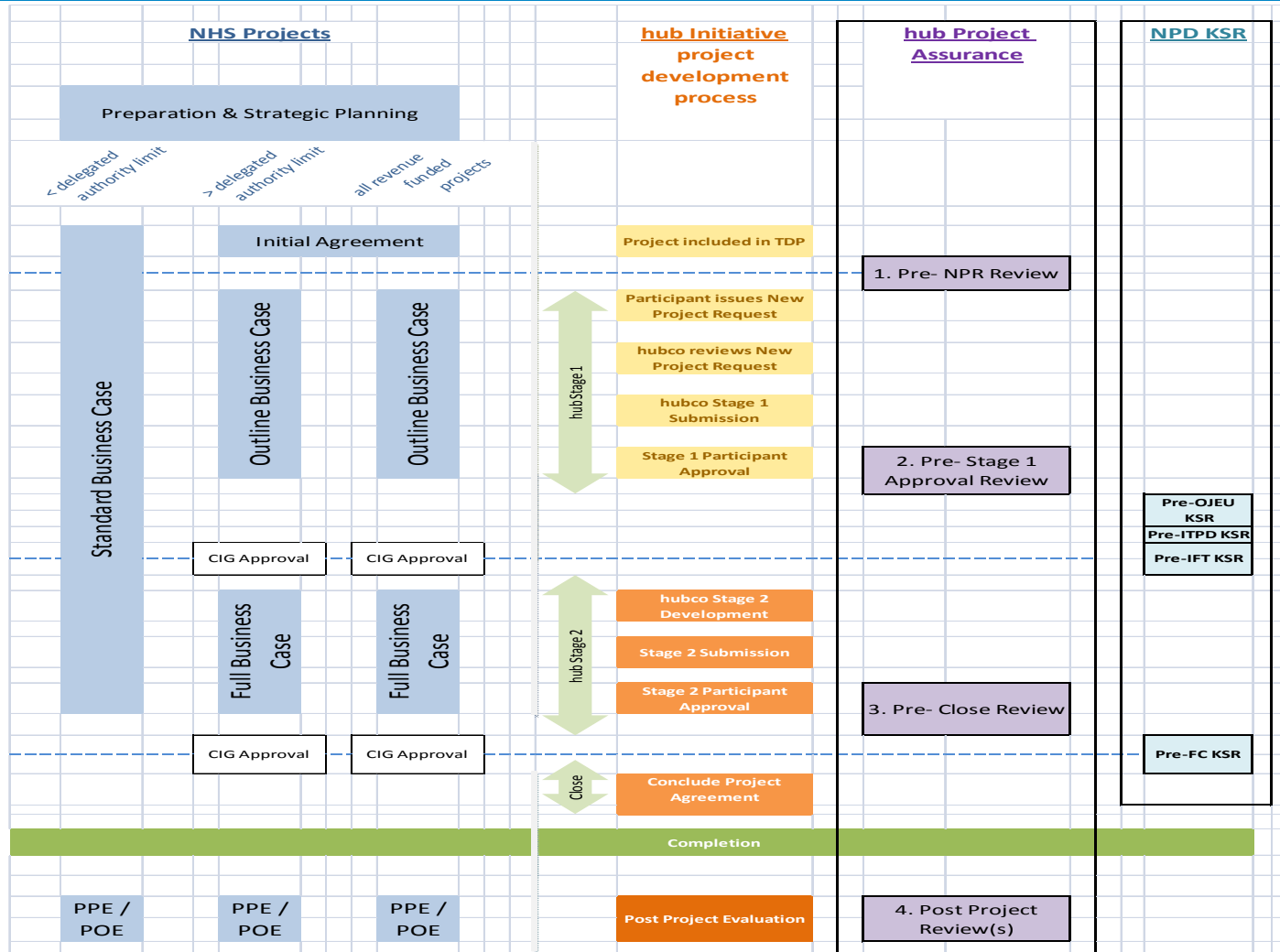
Degree of local challenge vital – needs not wants

Central challenge will be much stronger on aspects of proposals – capital requirements in particular



- All projects subject to review and validation
- Existing processes will continue – Gateway Reviews and KSRs
- Additional verification and examination – for example, components of revenue support

What are the key validation stages?



Initial Agreement	<ul style="list-style-type: none">•case for change•validation of work to generate OBC•part of the planned programme•assessment of organisational capacity & skills
Outline Business Case	<ul style="list-style-type: none">•authority to procure•setting the funding parameters•procurement strategy
Full Business Case	<ul style="list-style-type: none">•the deal on the table•formal agreement of funding•authority to conclude the deal

Four Stage approach to development

1. Review role, membership and operation of CIG to ensure consistent with SG objectives and revised funding arrangements and allow full assessment to be conducted as part of one process
2. Develop Standard checklists of questions to be addressed on a consistent basis in cases (for each procurement type and approval stage)
3. Update SCIM guidance to reflect changes and develop standard templates for business cases and presentation of evidence within them
4. Training and Development

How do we assess value for money?

Programme Level:

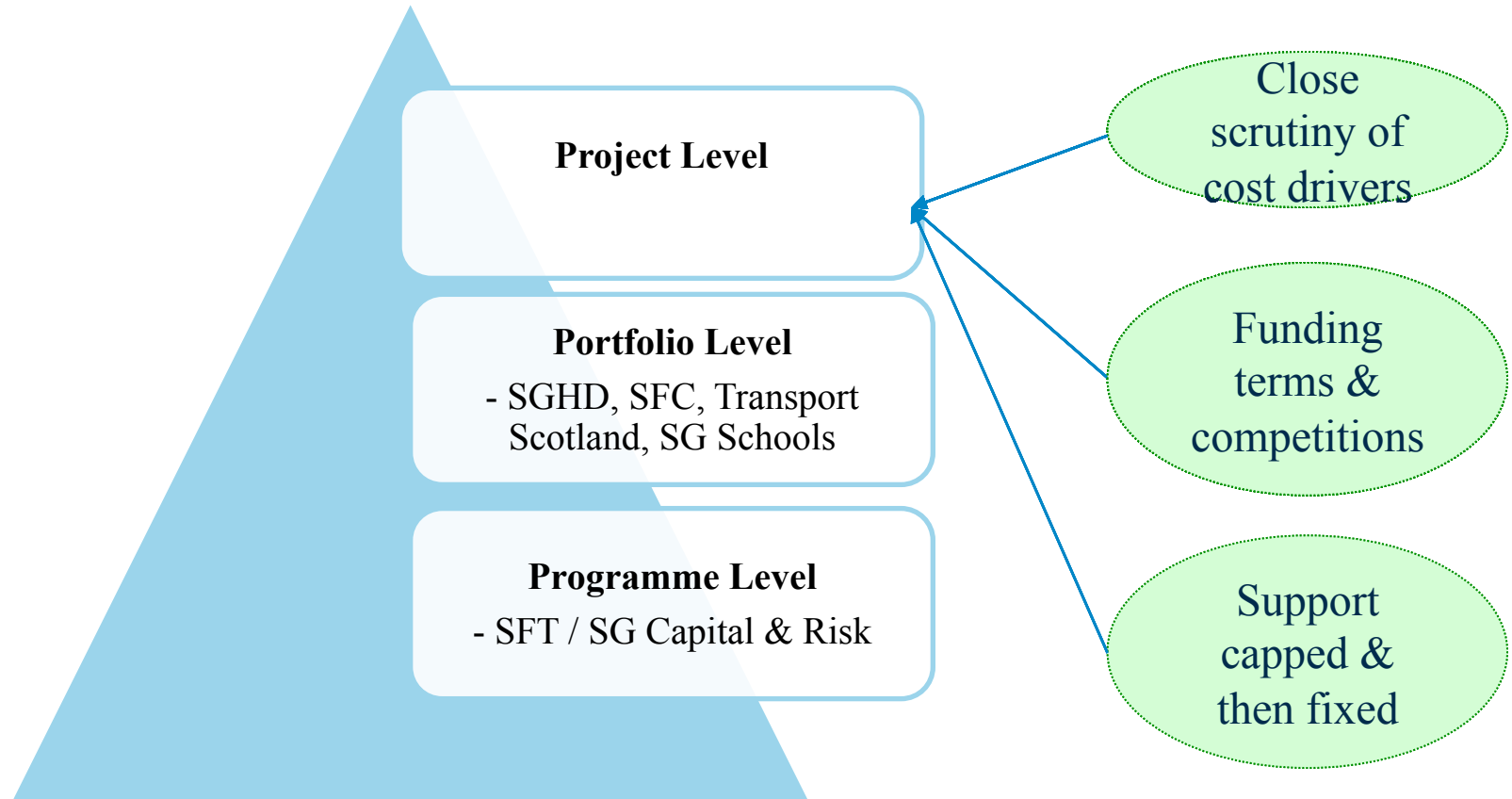
- Comparison of procurement routes



Project Level:

- Economic Appraisal
- Needs not wants
- Competitive Process

How do we assess affordability of NPD Programme?



QUESTIONS AND ANSWERS

What does this funding approach
mean for your schemes?

MIKE BAXTER
VIV COCKBURN

What does this funding approach mean for your projects?

1. How will projects be supported with central funding?
2. SG Funding Principles – SGHD letter of 22 March 2011
3. What is funded and what is not?
4. Identified capital requirements
5. SFT role

How will projects be supported with central funding?

Pipeline to be finalised and agreed – market and pipeline management nationally will be vital to support effective delivery

Funding based on set of principles agreed by Ministers. These are set out in letter from Derek Feeley to Chief Executives – 22 March 2011

Dynamics of funding mean SG and Boards have interest in minimising impact of different expenditure components in projects i.e. capital expenditure v hard FM/ lifecycle

Clear responsibilities on Boards for delivery and effective client function

- Standard contract and adherence to it
- Capacity and governance
- Value for money and business cases
- Preparatory work and development costs
- What is funded and what is not
- SFT Role

- The procuring body is required to submit an Outline Business Case (OBC) to the Scottish Government, with a shadow bid model, which demonstrates how the project will deliver value for money in quantitative and qualitative terms. The OBC must be in line with Green Book guidance, the Scottish Public Finance Manual and appropriate sector specific guidance as outlined in Section 4.
- Before the project can enter procurement, the Outline Business Case must be approved by the procuring body and ultimately Scottish Ministers. SFT will have an oversight role and will provide comment to Scottish Ministers prior to their formal approval.
- The procuring body and the Scottish Government must both confirm at OBC stage that the project is affordable in terms of both unitary charge and non-unitary charge costs.
- Approval of the OBC will cap the revenue support based on agreed capital value supported at an agreed base date with an agreed construction inflation assumption and agreed centrally provided financing assumptions. [\[1\]](#)

[\[1\]](#) Revenue consequences of any upward movement in construction cost or timing after this date are likely to be the Authority's account, although in exceptional cases with a full justification in the Final Business Case, may be centrally funded.

After the procuring body has selected a preferred bidder but in advance of financial close, the procuring body is required to submit a Full Business Case (FBC) to the Scottish Government, with detailed costings which confirms that, following a competitive procurement process, the project offers value for money in both quantitative and qualitative terms. The FBC must be in line with Green Book guidance, the Scottish Public Finance Manual and appropriate sector specific guidance as outlined in Section 4.





Before the project can reach financial close the Full Business Case must be approved by the procuring body and ultimately Scottish Ministers. SFT will have an oversight role and will provide comment to Scottish Ministers prior to their formal approval.

The procuring body and the Scottish Government must both confirm at FBC stage that the project is affordable in terms of both unitary charge and non-unitary charge costs.

Approval of the FBC will fix Scottish Government revenue support based on the out-turn capital value of the project; anticipated financing terms; and maintenance and life cycle costs at an agreed base date.

What is funded centrally and what is not?

Revenue Support: Where fixed within the procurement process

	OBC	OJEU – Bid Receipt	IFT – Final Tender Evaluation	PB – Financial Close	Post FC
KSR Stages					
Components of Funding Support					
Construction Costs – 100% funded	OBC ✓				
Private Sector Development Costs – 100% funded				✓FBC	
Financing Interest & Fees – 100% funded				FC ✓	
SPV Running Costs – construction – 100% funded				✓FBC	
SPV Running Costs – operation – 100% funded				✓FBC	
Lifecycle Maintenance Costs – 50% funded	OBC ✓				
Funding Support Fixed: Financing Cost: interest rates at financial close All other costs at PB appointment				FC ✓ ✓PB	

✓ Revenue Support Capped

✓ Revenue Support Fixed

Capital expenditure required to support projects not covered within NPD contracts or hub DBFM e.g. enabling works, equipment

Timing and value has to be explicit to support planning at national level

Capital requirements for such projects will require to be bid for as part of SR processes

LDP' s need to be explicit about such requirements



Programme Level

Standard contracts, affordability, ESA95, vfm, assurance & approvals, market interface



Portfolio Level

Revenue support confirmation, assurance and approvals, progress reporting/monitoring



Project Level

Governance, business case development, assurance and approvals, procurement process support, contract derogations

Work streams	Programme	Portfolio	Project
Contract, NPD principles	Develop standard contract & NPD/hub DBFM principles	-	Approve project specific changes
ESA95	Programme clearances	-	Review Project clearances
Affordability	Monitor and provide updates on programme affordability	-	Track project affordability implications on programme
VfM	Support development of vfm guidance	-	KSR – challenge vfm implications
Revenue Support	Assist in developing methodology	Verify RS claimed and support Portfolio	Verify RS claimed
Assurance & Approvals Process	Develop assurance & approvals approach	Key Stage Reviews	Key Stage Reviews
Project Governance	-	-	Share best practice. May include SFT representation on Project Board
Business Case Development	-	-	Support as required by Portfolio
Procurement Process Support	-	-	Share best practice and provide support as agreed
Progress Reporting	Timescales, budgets, issues arising	Timescales, budgets, issues arising	-

QUESTIONS AND ANSWERS

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