HIGHLAND COUNCIL

EDUCATION PPP2 FULL BUSINESS CASE

22 December 2006

Financial Close Version

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1. EXECUTIVE SUMMARY

1.1 Summary of the Procurement Process

The Highland Council embarked on a project to develop a number of schools in 2001.

In December 2001, an Outline Business Case was submitted to the Scottish Executive, which responded in July 2002 with a lower offer of funding than that requested. A Revised OBC was submitted in October 2002, and in December 2002, the SE approved the project, with Revenue Support of £7.16m pa for 30 years. The Council gave approval to move forward with the procurement phase early in 2003. This process led to the placing of a notice in OJEC inviting expressions of interest from potential private sector partners in January 2003.

Only one bidder responded, and subsequent to discussions with the Scottish Executive, the Council decided in April 2003 to progress the PPP2 project with this Bidder – Alpha Schools (Highland) Ltd, a Project Company in which the equity shareholders are Morrison Project Investments Ltd (a subsidiary of AWG plc) and Noble Fund Management Ltd. The Project Co will enter into contracts with Morrison Construction to undertake the construction programme and Morrison FM Services to provide facilities management.

The private sector partner will design and build the schools, provide the necessary finance to do so, own and maintain them throughout a 30 year period and also provide cleaning and janitorial services.

The Invitation to Negotiate was issued in February 2004, with Preferred Bidder status reached early in 2005.

Financial Close was reached on 30 March 2006 the first school building becoming available in April 2007, the remaining school buildings by June 2008 and all schools including playing fields and external works by June 2009.

1.2 Outline of Preferred Option

At OBC, the preferred Option for the Council covered:

- replacement of four secondary schools – the Dingwall Academy, Kinlochleven High School, and Millburn Academy, Inverness; and Portree High School;
- the construction of a new primary school at Inshes, Inverness;
- replacement schools at Drummond Special School, Inverness, and St Clements Special School, Dingwall;
- the replacement of primary schools at Cawdor, Culbokie and Kinlochleven;
- a new school to replace primary schools at Cullicudden and Newhall;
- a new purpose-built primary school in Inverness for Gaelic Medium pupils; and

- a new hostel at Mallaig High School.

Subsequently, Mallaig Hostel and St Clements Special School were withdrawn from the project. The project now comprises the schools listed in the Table below, with their current rolls and design capacities also given.

School	Roll at Sept 2003	Design capacity	Additional under 5's provision
Cawdor PS	129	145	30
Culbokie PS	82	121	20
Cullicudden/ Newhall PS	86	96	20
Dingwall Academy	1,064	1,000	Nil
Drummond Special School, Inverness	114	80	6
New Inverness Primary at Inshes	NA	306	60
New Gaelic Primary School, Inverness	110	150	30
Kinlochleven High School	105	120	Nil
Kinlochleven Primary School	62	96	20
Millburn Academy	1,092	1,100	Nil
Portree High School	674	700	Nil
Total	**3,518**	**3,914**	**186**

1.3 Summary of Value for Money and Affordability

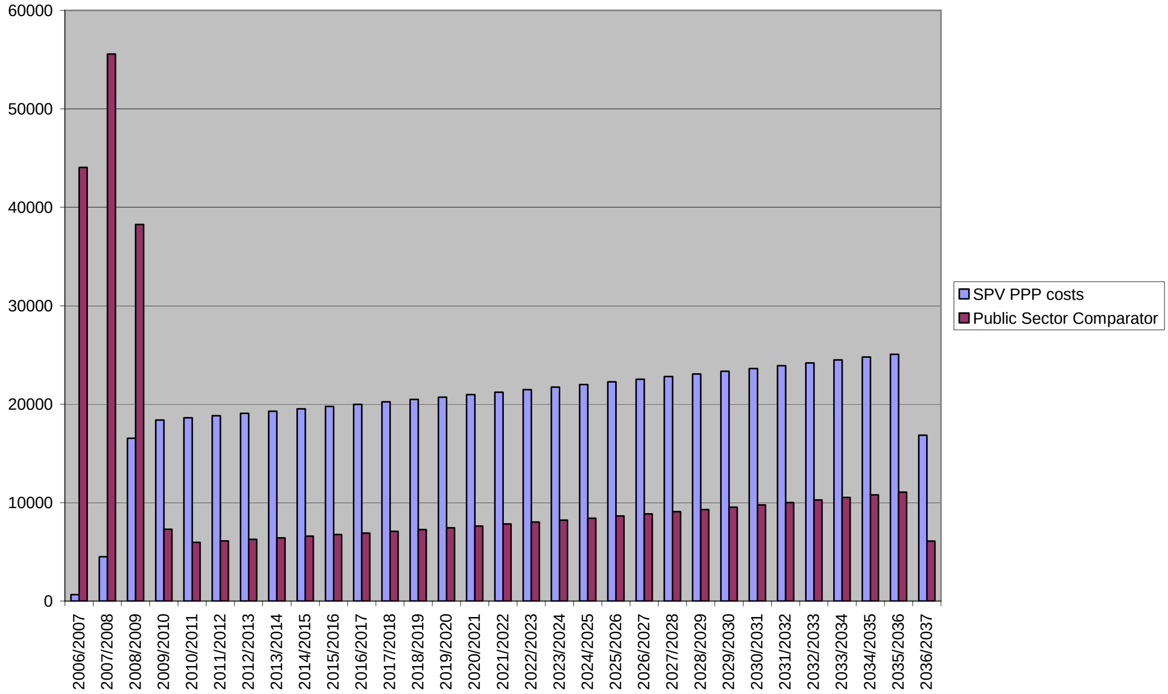
The first full year of full school building availability is 2009/10 (based on Alpha's financial year end dates) and the resulting estimated Alpha service charge is £18.38 million. This service charge is given in 2009/10 cash prices, based on a forecast inflation rate of 2.5% per annum, and equates to an April 2004 price of £15.725 million.

It will increase thereafter at a rate of 48% of the increase in the Retail Price Index. Assuming RPIx increases by an average of 2.5% p.a., in line with the Bank of England's RPIx inflation target, this would imply a nominal increase in the unitary charge of 1.2% p.a.

On this basis, the NPV of the Alpha payment stream over the term of the Project Agreement is £246.723 million, compared to an NPV of the PSC, adjusted for risk, optimism bias and tax, computed as £265.058 million – a Value for Money (VfM) differential of £18.335 million, or 7.43% in favour of the Alpha bid.

The cashflow to the Council under the two alternatives is shown graphically in Figure 1.1 below. It shows that, under the PSC, the Council would need to invest a significant amount in the early years to build the schools, but thereafter would need to pay a lower annual cost than under the PPP to maintain and insure them. The PPP payment profile is smoother, reflecting the fact that the amortisation of Alpha's initial investment costs is recovered through the availability element of the unitary charge.

Figure 1.1:
Comparative Highland Council cashflows under the PSC and PPP



Source: Adapted from the PSC at Financial Close reproduced as Appendix 1, and Alpha Bid Model "Model for launch dayFINAL.xls"

The VfM margin between the two payment streams of 7.43% does not take account of the following qualitative factors:

- Under the PPP, maintenance standards are contractually enforceable, with penalties applying in the event that contractual performance standards are not achieved, whereas under the PSC they are not;

- Under the PPP, funders will insist that the Alpha Project Co sets aside a dedicated Life Cycle Maintenance reserve to ensure that the schools are properly maintained over their life cycle. Under the PSC, this would not be the case, and, while any Council will use its best endeavours to fund the life cycle maintenance requirements of its buildings, in practice budgetary constraints and political priorities have in the past meant this has not always been achieved in local authorities throughout the UK, leading to a progressive deterioration in the quality of public buildings;

- Under the PPP, Alpha will face contractual penalties for failure to meet the Services Availability Dates for each school. If the Council was to undertake the project through direct procurement, there would be significant deliverability risks which they would be required to manage. The Council has not managed a construction programme of this scale – the largest construction programme that they have managed to date, is for the rebuild of the secondary school at Ullapool which has a capital value of less than £20 million.

- If the PPP procurement were cancelled at this stage there would be a considerable delay in implementing a direct procurement, taking account of the need to work up detailed designs, secure planning consents for them, and tender the contracts under a traditional contract structure. These delays would lead to cost escalation.

Taking these factors into account, the PPP is judged as offering superior value for money, offering a lower NPV than direct Council procurement when account is taken of optimism bias, and offering qualitative benefits in terms of the phasing of the new schools programme and the contractual enforceability of maintenance standards following their commissioning.

1.4 Milestones / timetable from Financial Close to full service Delivery

The key milestones are shown in the Table 1.1 below:

Table 1.1: Procurement Timetable

Milestone	Date
Contract Award and Financial Close	March 2006
First School Building available	April 2007
Final School Building available	September 2008
All Schools, including paying fields and external works, complete and fully operational	October 2009

1.5 Key Commercial Project Issues

This FBC includes a short section (Section 4.5) addressing particular project issues resulting from the preferred bond-financing structure, the particularly remote locations of Portree High School and Kinlochleven and the Payment Mechanism.

A full list of the derogation from the Scottish Schools Standard Form Project Agreement is included as Appendix 5. The main derogations which the Council have considered as giving additional value for money to the Project, which has either been incorporated within the bid pricing or terms or which have been obtained since bid submission are as follows:

- The Council have accepted a cap on malicious damage costs, thereby reducing the annual FM charge by £120,000;
- There have been various changes to the financing definitions and provisions relating to compensation payable on early termination of the project, largely to reflect the method of funding used in this project (being bond funding as opposed to more traditional bank finance);
- Provisions have been inserted to reflect that the construction period for certain external areas will take longer than the construction period for the new schools;
- Provisions have been inserted dealing with co-operation between the project company and the Council's catering provider, since catering does not form part of the project;
- The concept of flexible use hours has been introduced to allow the Council cost effective use of the schools outwith normal educational periods;
- There have been various changes to the employment and pension provisions to ensure that the Council employees who are transferring and those who are employed during the course of the project are protected and that the risk sharing between the Council and the project company represents value for money;
- Insurance premium sharing proposals have been inserted since the ITN, reflecting the proposals released by the Scottish Executive in March 2005.

2. THE OUTLINE BUSINESS CASE

2.1 Business Need

The Council carried out a rigorous review of its education properties as a means of identifying its priorities for this PPP project and in support of the Council's 21st Century Schools Improvement Programme.

This needs analysis identified that the majority of the Highland Council's school estate pre-dates the 1970s and that over 50% of these pre-1970s schools actually pre-date 1900. As a result, a significant number of Highland Schools are no longer deemed fit for purpose in a modern 21st Century education environment

Added to the requirement for a major investment programme is the amount of backlog maintenance that will simply allow schools to be brought up to a minimum acceptable standard. There is a clear need for the Council to pursue this, its second education PPP, in order to radically improve education provision in the Highlands in line with national education priorities and Highland Council's strategic aims.

2.2 Scoping of the project and options appraisal

The long-list of schools to be included within the proposed PPP project was identified as a result of the review of the school estate referred to above. This long-list was then prioritised in order that a short-list of schools could be objectively identified if affordability constraints indicated that the long-list might prove unaffordable to the Council.

An options appraisal exercise was then carried out on a variety of options identified for improving each project school (e.g.: refurbishment, new build, amalgamation). This appraisal identified the costs and benefits associated with each option for each school and established in value for money terms what the best case option for each should be.

This best case option was converted into the preferred option for this project by reducing the long-list of schools to a level that was affordable to the Council. The preferred option included a total of twenty-eight schools and one hostel.

After the Scottish Executive response to the Council's OBC, which did not give the full Revenue Support requested, the Council re-scoped the project to reflect the Scottish Executive funding available and trends within the PPP market, for example to take account of increasing capital costs. The rescoped project prioritised schools on the basis of dealing with the worst problems first, securing value for money and to ensure that the project was attractive to the market.

The re-scoped Preferred Option involved the following:

- the replacement of the four Secondary Schools –Dingwall Academy in Ross & Cromarty, Kinlochleven High School in Lochaber, Millburn Academy in Inverness and Portree High School in Skye;
- the construction of a new primary school at Inshes, Inverness;

- the replacement of two special educational needs (SEN) schools – the Drummond Special School in Inverness and St Clements Special School in Dingwall;
- the replacement of the existing primary schools at Cawdor, Culbokie and Kinlochleven;
- a new school, Resolis, to replace two existing primary schools at Cullicudden and Newhall;
- the construction of a new purpose-built primary school in Inverness for Gaelic Medium pupils; and
- the construction of a new hostel serving Mallaig High School.

Subsequently, the Mallaig Hostel and St Clements Special School were taken out of the project, to ensure that it could be delivered within the Council's affordability limits.

3. THE PPP PROCUREMENT PROCESS

3.1 The Council Team

The Council had an established a ‘PPP Schools’ team which procured its first Education Public Private Partnership of 4 new schools, which became operational in August 2002. This team, largely unchanged in terms of personnel, carried forward the experience gained into the new PPP2 Schools project.

The Project Director, the Director of Property and Architectural Services, took up appointment on 17th June 1999 for the original PPP1 Project, and along with the other members of the in-house PPP Team comprising the Head of Support Services (Education, Culture & Sport Service), the Head of Legal Services, Principal Accountant, PPP and Joint Ventures, Head of Contracts and a Depute Headteacher assigned to the team.

The Council’s in-house Legal Advisers were commissioned separately to carry out title searches on all the PPP School sites. This was managed by the Head of Legal Services who reported any land-related issues back to the Project Team. The purchase of land for the PPP School sites was jointly undertaken by the Property and Architectural Services, Education, Culture and Sport and Legal Services under the direction of the Project Director.

The Council has been supported by the following External Advisors:

- Project Manager - Turner & Townsend Project Management Ltd
- Legal Advisers - MacRoberts
- Financial Advisers – Caledonian Economics.

3.2 The Project Board

The Council has one PPP Project Board at present which considers all of the Council’s PPP activities. This Board includes the Council Chief Executive, Service Directors for Education Culture & Sport, Finance, Corporate Services, Property and Architectural Services, and Technical Environment and Community, together with Trade Union Representation and Scottish Executive Representation.

3.3 Project Team Reporting Structure

The Project Team met, on average, on a fortnightly basis throughout the procurement process with additional meetings to suit specific requirements of the process. An agenda was prepared for each of the meetings and minutes were prepared by the Project Manager.

The Project Team provided reports to the Project Board on a six weekly basis highlighting issues which the Board required to consider and covering general progress with the procurement.

3.4 Project Management Reporting Structure

Project Board meetings were held throughout the procurement of the project on a frequent basis. The Project Board assumed the strategic management of the Project and gave direction to the frequency and detail of political reporting. All the meetings had a prior agenda and were noted.

3.5 Timescales

The key stages in the procurement are shown in the Table 3.1 below:

Table 3.1: Procurement Timetable

Procurement Milestone	Date
OJEU Notice Despatched	January 2003
Bidders' Conference	February 2003
Bidder appointed	April 2003
Invitation to Negotiate issued	February 04
Bid received	May 2004
Revised Bid received	August 2004
Preferred Bidder appointed	May 2005
Contract Award and Financial Close	March 2006
First School Building available (Culbokie)	April 2007
Final School Building available (Millburn)	September 2009
All Schools including playing fields and external works complete and Operational	October 2009

4. THE PREFERRED BIDDER AND THE PPP SOLUTION

4.1 Description of the Consortium and its members

The Highland Council received a single bid from Alpha Schools (Highland) Ltd ("Alpha"), which, at the time of the bid submission was, a consortium jointly owned by Morrison Project Investments Ltd (a subsidiary of AWG Plc) and Noble Fund Management Ltd. The Council's approach to ensuring VfM in a single bidder situation is described in greater detail in Section 7. The obligations of the consortium members will be guaranteed by their respective parent company where appropriate.

Morrison Construction will take responsibility for the delivery of the design and build programme, subcontracting to Tulloch for part of the construction programme. Morrison FM will be responsible for the delivery of facilities management including janitorial services and have retained MITIE as a sub-contractor for cleaning services.

On 2nd March 2006, AWG plc announced that it had entered into an agreement to sell the Morrison Construction and Morrison Project Investments Ltd businesses to Galliford Try plc. A legal due diligence on the documentation for the Project was carried out by MacRoberts. This concluded that the sale would have minimal effect on the Project. In addition, AWG support for the Project will remain in place and the personnel and management involved in the Project on behalf of MCSL and its subsidiaries are not planned to change.

4.2 Financial Strength of the Consortium

The financial strength of the members comprising the bidding consortium was initially assessed at the prequalification submission stage. This assessment focussed on the likely size of the commitments that the individual members would undertake in relation to their roles, together with an overall assessment of the fund-raising capability. These aspects were reviewed again at the time of ITN submission. In addition, the degree of commitment demonstrated in relation to bidders financial proposals and the financial robustness of the project company were analysed.

There are two equity providers to the Project Co, with Morrison Project Investments Ltd (a subsidiary of AWG Plc) and Noble Fund Management Ltd contributing equal proportions of both equity and subordinated debt. The equity investment is a minimal £50,000 to establish ownership of the SPV and meet the funders' cover ratio requirements. The subordinated debt, at £15.245 million, together with equity represents 9.73% of the total funding requirement. The Alpha financial close model indicates that the shareholders have a target post-tax nominal blended equity IRR of 12.34%.

In late 2005 Nobles formed a new investment vehicle in conjunction with its principal investor 3i to invest in UK PPP projects. The new entity is known as Northern Infrastructure Investments LLP ("NII") and will invest ordinary equity and subordinated debt in the Highland Schools project through Alpha Schools and Alpha Schools Holdings Ltd. (Shareholdings remain 50% NII and 50% Morrisons.) NII's deferred sub debt commitments at construction completion will be supported by a corporate guarantee for approx £7m from 3i Group PLC – this has been accepted by the senior lenders.

Noble Fund Managers ("NFM"), as well as investing through the partnership, act as the representative of this investment structure under an arrangement with the limited partnership in sourcing, arranging and negotiating PPP transactions and managing the investment post Financial Close. NFM will represent NII at project/shareholder meetings and will appoint representatives to the Alpha Board.

The project will be financed by means of a bond issue arranged by Royal Bank of Canada with a value of £81.4 million, and an EIB term loan of £60 million. A wrap will be provided by Ambac covering the entire senior debt and bond funding requirement.

AWG plc is to provide parent company guarantees in relation to the performance of the FM sub-contracts.

The obligations of MCSL under the building contract are guaranteed by a parent company guarantee in favour of ProjectCo from AWG Group Limited ("PCG"). In addition Galliford Try plc are providing a second, direct, joint and several parent company performance guarantee ("GPG") under substantively similar terms to the PCG. The GPG will therefore be a further level of security for both ProjectCo and the Security Trustee.

The total project cost is estimated at £176.752 million, as shown in Table 4.1 below.

Table 4.1:
Alpha Schools – Highland Schools PPP Project Cost

	£
Core Construction	133,946,565
Start Up costs	8,961,145
Sub debt commitment fees	375,121
Bond/EIB interest and financial guarantee fee during construction	24,589,364
Sub debt interest roll up during construction	1,708,754
Senior Debt Reserve – initial requirement	4,803,476
Change in Law Reserve – initial requirement	2,015,741
Lifecycle provision – initial requirement	76,744
Tax on interest income prior to first school handover	6,803
Output VAT recovered after construction	44,292
Bank Balance	223,776
TOTAL	176,751,781

Source: Alpha Schools Financial Model, "Model for launch dayFINAL.xls"

The financing structure for the project costs (including interest during construction) is shown in Table 4.2 below.

Table 4.2:
Alpha Schools – Highland Schools PPP Financing Structure

	£	%
External Financing:		
Equity	50,000	0.0319%
Subordinated	15,245,041	9.7291%
e	81,400,000	51.9480%
EIB Debt	60,000,000	38.2909%
Sub-total:	156,695,041	
Project Co cash generation during construction:		
Phased net revenue during construction	14,373,674	
Interest earned on cash balances during construction	25,662	
GIC Interest	5,433,438	
Change in Law Reserve Interest	223,966	
TOTAL	**176,751,781**	

Source: Alpha Schools Financial Model, "Model for launch dayFINAL.xls"

4.3 Price

Alpha provided an updated financial model reflecting the agreed commercial position and price at financial close and is based on the interest rates agreed at financial close. The price in the first full fiscal year of Full School Building and Pitch Availability (April 2010 to March 2011) is forecast as £18.534[1] million nominal, inclusive of insurance and a rates pass-through.

4.4 Description of Technical Solution

Further to detailed technical meetings and discussions with the client, the bidder's drawn technical solutions as offered are aligned with the client required facility content as demanded within the project facilities accommodation schedules and room data sheets.

There is offered by the bidder, a functional solution that meets the client's operational and managerial requirements in the delivery of educational services within these facilities. Design and development is progressing through the design review process for all schools.

The Highland Council Project Team has not issued any directional instructions to the bidder in relation to the architectural design and aesthetics of the facilities as design risk lies completely with the bidder. However, there is no doubt that the planning and community liaison process has demanded design changes to be incorporated into the project that better meet the desires of the local communities, with regard to appearance and material content.

4.5 Key Commercial Project Issues

The project conforms to the SSSC except for derogations submitted to the Scottish Executive.

[1] Calculated as the sum of cells L8:W8 of sheet "UC by month" of book "Model for launch dayFINAL.xls"

5. THE PUBLIC SECTOR COMPARATOR

5.1 Derivation of The Public Sector Comparator

5.1.1 Introduction

A Public Sector Comparator (PSC) has been prepared taking account of the relevant OGC and Scottish Executive and in consultation with Audit Scotland.

The PSC for the Full Business Case is based on the figures used in the PSC for the Outline Business Case. The model has been prepared to represent the solution the Council would adopt if it was to procure the project conventionally and within the timescale of the PPP contract and included a detailed review of the risk quantification.

5.1.2 Contents

The PSC represents the underlying cost to the Council for directly supplying the services required to meet the Output Specification (produced as part of the PPP procurement process) including an assessment of the value of optimism bias and risks transferred to the private sector.

The PSC therefore represents the cost to the public sector of:

- Building eleven new schools, and fitting and furnishing them to the to the standard specified in the project ITN;
- Facilities management services, maintenance and lifecycle expenditure to the portfolio of schools from the PPP contract award date to its expiry date (equivalent to the term of the PPP contract);
- The cost of procuring the design, development and construction of the eleven facilities;
- The cost of managing the delivery of the services, ensuring that facilities management and life cycle regimes are implemented and managed to a standard that reflects the contractually binding arrangement that would be in place under a PPP;
- The pass-through cost of rates on the new school buildings;
- The costs of insuring the facilities during the construction and operational phases of the project.

The basis of the PSC is that the Council would deliver the services to the same Output Specification as under the PPP. The PSC assumes that assets are acquired through conventional funding and that the Council retains significant managerial responsibility and exposure to risk.

Table 5.1 below presents the results of the PSC after the inclusion of the value of transferred risks.

Table 5.1:
Highland Schools Project - NPV of the Public Sector Comparator

NPV without Risk Adjustment	213,465
Tax adjustment	10,673
NPV of Risk and OB adjustments	40,920
Total Risk Adjusted NPV of PSC	*265,058*

Source: "Highland Schools PPP - PSC and SBM FINAL (020606).xls"

A summary of the assumptions in the PSC is shown in Appendix 1. The key assumptions are summarised in the following sections.

5.1.3 Key Assumptions

Economic Assumptions

The following economic and financial assumptions have been used for the purpose of the PSC:

- Inflation of 2.5% per annum
- Discount rate of 3.5% real, 6.0875% nominal;
- Third party revenue is not considered to be material and has been excluded;
- Land values are excluded from the PSC;
- Residual values are assumed to be nil.

Capital Expenditure

Capital Expenditure costs were calculated by the Council's Property and Architecture Service on the basis of contract costs of relevant comparable projects undertaken by the Council, adjusted to reflect the particular requirements of the project and the prevailing market. Costs are shown below in Table 5.2.

Table 5.2:
Outturn capital costs for the Highland Schools PSC

School	Area, m^2	£'000 (Q4 2007) *	Rate per m2 *
Cawdor Primary	1,900	£4,407,748	£2,367.58
Culbokie Primary	1,557	£3,711,558	£2,432.82
Dingwall Academy	15,011	£29,540,544	£2,008.40
Drummond SEN	6,237	£12,847,279	£2,102.21
Inshes Primary	3,027	£6,984,854	£2,354.98
Gaelic School	1,679	£4,090,801	£2,486.56
Kinlocheven Primary	1,022	£2,944,327	£2,940.20
Kinlochleven Secondary	3,987	£8,918,230	£2,282.83
Millburn Academy	15,822	£29,623,606	£1,910.81
Resolis Primary	1,208	£3,266,739	£2,759.87
Portree High School	12,894	£27,841,053	£2,203.63
Installation of sprinklers in all facilities		£2,759,624	
Total	**64,344**	**£136,936,363**	**£2,128.19**

Source: The Highland Council, "PSC Cost Summary (30-01-06).xls"
*The outturn development cost is based on an estimated mid-point of the first quarter of 2007 for the construction programme. Costs per m^2 include an apportionment of the cost of installing sprinklers.

In addition to the above, Council procurement costs are estimated as £250K per annum during the construction period and £130K per annum during the operational period.

Revenue Expenditure

The following economic and financial assumptions have been used for the purpose of the PSC:

- The cost of providing Facilities Management services (covering Janitorial, Cleaning, Grounds Maintenance, Security and Waste Disposal) to the same standard (including meeting performance standards and rectification periods) will be £42.50 m^{-2};

- Rates are a pass-through cost. Alpha has included an estimate of £500K per annum as a pass through within their Unitary Charge. To ensure consistent treatment a similar figure has been included in the PSC.

5.2 Risk and Optimism Bias Analysis

5.2.1 Approach to the Risk and Optimism Bias Analysis

Detailed Technical Risk Appraisals have been undertaken during the procurement to assess the likelihood and impact of cost overruns on design, construction, Life Cycle Maintenance (LCM) and Facilities Management (FM) costs. The analysis and results of these appraisals were set out in two Risk Evaluation Reports, respectively dated May 2004 and September 2004.

The technical risk evaluation was updated at a workshop held in Inverness on April 27th 2005 and in Perth on August 9th 2005 attended by the Council's procurement team and its financial advisers, Caledonian Economics Ltd. The purpose of these reviews was not to undertake a completely new risk evaluation, but rather to update the September 2004 assessment in the light of information received since then, and to confirm that there was no double-counting between the technical risk factors and the allowance for Optimism Bias contained in the financial model.

5.2.2 Caveats on the Methodology

In applying the Treasury's Optimism Bias (OB) methodology, the following caveats should be borne in mind:

- Optimism Bias is assessed for a direct procurement option, under which the Council would commission the design for the new schools, tender and supervise the works contract, and accept maintenance risks thereafter. However, the Council has not worked up designs for a direct procurement option beyond concept stage. The effective choice facing the Council in August 2005 was therefore between a notional direct procurement option – the Public Sector Comparator (PSC) – and an alternative PPP option with Alpha Schools, whose design has been worked up in detail and whose costs are being rigorously analysed and negotiated by the Council against established market benchmarks;

- Were the PPP to be cancelled, the view of the Council is that there would be very few contractors in the Highland region capable of undertaking a contract of this size under a direct procurement route other than AWG / Morrison and Tulloch Construction – the two main contractors within the Alpha Schools consortium;

- As with any Optimism Bias appraisal, there is inevitably a degree of subjectivity in the assignment of applicable factors, because OB by its nature applies to factors which are inherently uncertain.

Subject to these caveats, the Council and its advisers have sought to provide an objective assessment of plausible levels of optimism bias to be entered into the public-sector comparator, in a form that is transparent and auditable.

A detailed report on the Risk and Optimism Bias analysis is contained within Appendix 2 to this report.

5.2.3 Findings of the Risk and Optimism Bias Analysis

In summary, the Workshop concluded that:

- the Optimism Bias factor that should be applied to Works Duration should be 2.56%, and to capital expenditure 8.45%. Following discussions with Audit Scotland, the Optimism Bias in the model was altered to the Treasury ‘minimum’ level of 2% on capital expenditure and 1% on works duration;
- a risk adjustment of 18.03% should be applied to the construction costs;
- a risk adjustment of 14.88% should be applied to the ongoing FM and Lifecycle costs;

The general point emerging from workshop was that, if the PPP procurement were abandoned, it could not be assumed that the same project would proceed on the same timetable. On the contrary, the most likely scenario is that project implementation would be considerably delayed by the need for extensive consultation and political debate over the scope, design and affordability of a conventionally procured schools package. Alpha Schools is responsible for detailed schools design issues which will be subject to stakeholder consultation.

6. THE SHADOW BID MODEL

6.1 Derivation of the Shadow Bid Model

6.1.1 Introduction

A Shadow Bid Model (SBM) was prepared to provide a value for money comparator for the PSC and the bid received from Alpha Schools.

6.1.2 Contents

The SBM represents the predicted cost to the Council for procuring the services from a hypothetical private sector bidder. Its primary purpose is to confirm at OBC stage that the PPP represents better value than direct procurement as represented by the PSC.

The SBM therefore represents the hypothetical cost to the public sector of procuring via a PPP:

- eleven new schools, and fitting and furnishing them to the standard specified in the project ITN;
- Facilities management services, maintenance and lifecycle expenditure to the portfolio of schools from the PPP contract award date to its expiry date (equivalent to the term of the PPP contract);
- The cost of procuring the design, development and construction of the eleven facilities;
- The cost of managing the delivery of the services, ensuring that facilities management and life cycle regimes are implemented and managed to a standard that reflects the contractually binding arrangement that would be in place under a PPP;
- The costs of insuring the facilities during the construction and operational phases of the project.

6.2 Results of the Shadow Bid Model

The shadow bid model predicts a 2010/11 unitary charge payable by the Council of just under £20 million, in outturn prices, which is approximately £1.4 million more than that agreed with Alpha.

7. APPROACH TO SINGLE BIDDER STATUS

7.1 Introduction

This section summarises the approach adopted by Highland Council to managing the single bidder procurement.

The section provides a background to:

- The single bidder response to the OJEU and the decision taken by Highland Council to proceed with the procurement.
- The approach adopted by Highland Council to managing the procurement process to ensure that competitive tension was maintained, where possible, within a single bidder situation.
- A summary of how competitive tension has been demonstrated within the PPP procurement and how Highland Council has reassured itself that it has obtained a value for money bid from Alpha Schools.

7.2 Single Bidder Procurement

The Council received one pre-qualification submission from Alpha Schools in response to its OJEC notice. On receipt of the pre-qualification submission the Council adopted a two stream approach. Firstly, it evaluated its options to either continue with the procurement with a single bidder or to retender the project and secondly, it continued with the evaluation of the pre-qualification submission in accordance with its evaluation methodology.

7.3 Review of Single Bidder Procurement

The Council undertook an analysis of why only a single pre-qualification submission had been received. This included undertaking market soundings from Bidders who had decided not to express an interest in the project. The process informed the Council's analysis of their options going forward. These were:

- continuing with a single bidder procurement;
- retendering the project in the hope of attracting a second and third bidder;
- to cease the procurement, rescope the project and retender it in a way that was more attractive to the market – for example, as two grouped schools projects of approximately £60m capital value each.

The Council considered each of these three options by reference to their specific objectives for the project; through a market analysis of why the response to the OJEU was limited and through reviewing how they could adapt the procurement process to ensure that in a single bidder situation a value for money bid could still be achieved.

The results of these considerations indicated that even if Highland Council was to retender the project, there was unlikely to be any significant increase in consortia submitting pre-qualification submissions. This was due to the number of Schools PPP projects coming to market at the same time; the level of opportunities available in other sectors within the UK; a number of withdrawals from the market including Gleeson who was the contractor on the Council's first PPP project, Jarvis and Atkins, and the involvement of Tulloch as a sub contractor in the Alpha consortium.

The Council also reviewed the options available to it to manage a single bidder procurement process and to determine whether these would be sufficient to generate competitive tension and a value for money bid. Details of the Council's Single Bidder Procurement Strategy are included within Section 7.5.1 of this report.

7.4 Results of Pre-qualification Evaluation

In parallel with the Review of the Single Bidder Procurement, the Council completed its evaluation of the Alpha Schools Pre-qualification Submission. This concluded that Alpha Schools provided the required technical skills and financial and economic standing to undertake a project of this scale.

The Council therefore, decided to continue with a single bidder situation because on balance, the benefits of proceeding with Alpha Schools as a single bidder were judged to be more advantageous to the Council than the risks associated with of stopping the procurement. This position was discussed with the Scottish Executive in 2003 and the decision to proceed was approved by The Highland Council on April 10th 2003.

In making this decision the Council was aware of the potential pitfalls of proceeding with a single bidder situation and determined that the procurement process and timetable should be tailored to respond to these concerns with the objective of maximising competitive tension and ensuring that the Council received a value for money bid from Alpha Schools.

7.5 Decision to Proceed with a Single Bidder

7.5.1 Single Bidder Procurement Strategy

Prior to commencing the single bidder procurement, the Council carefully reviewed its approach to the procurement process to ensure that a value for money bid would be received and that this would proceed to financial close. The areas the Council reviewed in detail included:

- Where there were any legal/regulatory factors to be considered;
- How the procurement process could be run to maximise competitive tension;
- How the Council should interact with the Bidder to maximise competitive tension and demonstrate that the bid submitted was competitive; and
- How value for money could be demonstrated.

The results of the above analysis are summarised below.

7.5.2 Where there any legal/regulatory factors to be considered?

The following advice on legal/regulatory factors was provided by the external legal advisers at the time:

- The Council is entitled to proceed with the procurement. It must pre-qualify the single applicant in accordance with the pre-qualification scheme already devised and agreed upon by the project team. If the single applicant pre-qualifies, the Council may negotiate with the single applicant within the scope of the OJEC notice currently in issue. The format of those negotiations is a matter for the Council to decide.
- The Council is also entitled to abandon the current procurement. If so, the single applicant should be notified. The Council may then commence a new procurement, whether for the same or an amended scope.
- The Council is under no obligation to follow either of the above options. It may decide at its discretion. Under the Council's Standing Orders, where less than three bidders are to be short-listed, Council officials must seek the direction of the relevant committee on the selection process to be adopted (see Standing Order 8(iv)). Consequently, the decision to proceed to invite the single applicant to negotiate a contract is a Member decision. It appears that Council officials could take a decision to abandon the procurement, although it may be safer to refer this decision to the Members also.

7.5.3 How the process could be run to maximise competitive tension?

Within traditional procurements, competitive tension is maximised in the period from pre-qualification to preferred bidder. Following preferred bidder selection, the competitive tension is weakened, although the inclusion of a reserve preferred bidder can address this to a certain extent.

The Council examined how it could replicate the competitive tension and ensure that Alpha submitted a bid that was value for money. This focused upon the costs bid by Alpha Schools, the process agreed for optimising the financing and taxation treatment within the financial model and the approach to negotiating the Project Agreement and risk transfer.

Demonstrate the Costs in the bid are competitive

The first area of analysis focused upon the need to demonstrate that the core costs included with Alpha's model were competitive. Table 7.1 below summarises, the approach agreed to ensuring this within the procurement process:

Table 7.1:
Approach to Cost Analysis

Cost Category	Approach to ensuring competitive costs tendered
Construction Costs	The Council determined that the costs presented by Alpha Schools should be compared to a robust Public Sector Comparator and benchmarks. Technical Advisers have conducted this analysis by comparing the ITN bid costs against costs developed for the PSC, costs bid by Gleesons on PPP1 (adjusted for inflation), and BCIS national benchmarks.
Lifecycle and FM Costs	The Council agreed that the costs presented by Alpha Schools should be analysed and compared to costs seen on 'live' bids. Technical, Project Management and Financial Advisers have conducted this analysis by comparing the ITN bid costs against costs bid by other consortia.
Financing Costs	The Council determined that Alpha Schools should hold a funding competition to demonstrate that the most competitive financial terms had been achieved. The funding competition not only required that different sources of bank finance were compared but that Alpha Schools also reviewed EIB and bond financing to establish which would deliver best value for Highland's project.
Taxation	At the time of issuing the ITN, the composite trade tax approach to PPP projects was being introduced. Within the ITN documentation, the Council indicated that it wished the bidder to achieve the optimal tax treatment and that this should include the review of the composite trade approach. This approach requires different provision within the Project Agreement. This therefore allows the Council to establish whether this approach has been adopted and prevents the Bidder tendering on the basis of capital allowances and later switching tax treatment to accruing all the benefits to ProjectCo. The Council would also be able to review its adoption and ensure that the tax treatment had been optimised within the financial model.

Optimisation of the Financial Model

Within the ITN documentation, the Council required that Alpha Schools work with the Council to optimise both the financing costs within the model and the tax treatment. The tax treatment within the Alpha bid model has been reviewed and confirmed as reasonable.

Project Agreement and Risk Transfer

The Schools PPP sector is a relatively mature sector with common market positions regarding risk transfer and Project Agreement especially following the introduction of the Scottish Schools Standard Contract and Payment Mechanism. Within this environment, the ability for Alpha Schools to pursue amendments to the Project Agreement that did not reflect market precedent was limited. In addition, the Scottish Executive's requirements that no red areas of the Standard Contract could be altered and only green and amber areas could be adjusted to reflect Project Specific requirements, further strengthened the Council's position.

7.5.4 How the Council should interact with the Bidder to maximise competitive tension and demonstrate that the bid submitted was competitive?

Within a single bidder situation, there is a potential risk that the bidder will abuse its position through for example, not providing fully developed bid proposals, not cooperating with the Procuring Authority in demonstrating that a value for money bid has been received and through unwillingness to follow a partnership approach. In a single bidder situation there is always the danger that the bidder may withdraw and that a Procuring Authority therefore accepts a position it would not normally have followed.

Highland Council's approach to this aspect of the single bidder procurement process was to:

- discuss and agree with Alpha, the obligations' placed on Highland Council to demonstrate that a single bidder procurement could deliver value for money and to gain their agreement to working with the Council in this respect;
- agree with Alpha schools an open book approach to the costs included within the Alpha bid including negotiations on the level of costs and a willingness to benchmark these costs;
- To agree with Alpha Schools that they would work with the Council to ensure that the financial model and tax treatment was optimised.

7.5.5 How VFM could be proven demonstrated

The applicable guidance on value for money indicated that this would be demonstrated if the Alpha bid demonstrated better value for money than a risk adjusted public sector comparator. Value for money being measured on the basis of:

- the comparison of the net present values of the Alpha bid and the risk adjusted PSC; and
- a comparison of the qualitative benefits which the Alpha bid provided.

In recognition of the single bidder situation, the Council also determined that the Alpha bid would be compared in detail to the shadow bid model. In order to ensure that the shadow bid model and PSC would be effective evaluation tools, the Council ensured that their advisors provided realistic and substantiated assumptions regarding the inputs into these models.

It was also agreed that the inputs would be reviewed during the course of the procurement and revised to reflect changes in the timing of the project and scope of services to be provided. In accordance with best practice, it would be subject to no other adjustments.

7.5.6 Conclusion – Decision to Proceed with a Single Bidder

The Council carefully reviewed the options available to it to manage the procurement process in such a way that competitive tension was maximised. The measures noted above were discussed and agreed with the Project Director and Project Board. In the meeting of 10th April 2003 The Highland Council decided that sufficient safeguards could be put in place to mitigate the risks associated with a single bidder procurement, and gave the Project Team approval to proceed with the single bidder.

Detailed discussions were also undertaken with the Scottish Executive and their agreement to the single bidder procurement obtained.

7.6 Implementation of the Single Bidder Procurement Strategy

7.6.1 Introduction

This area of the report outlines the approach the Council has adopted to ensuring that the risks associated with the single bidder procurement were mitigated, and the evidence that these have been successful.

7.6.2 Mitigation Strategies

Having considered the options open to it and taken note of the range of Treasury and TTF/OGC guidance and the National Audit Office recommendations arising from a report "Delivering Better VfM from the PFI", the Project team recognised a number of risks associated with proceeding with a single bidder, and put in place mitigation strategies. The risks identified, and the actions taken to mitigate these risks are summarised as follows:

- **Risk:** the tendency to conduct Negotiations with a Single Bidder in a less formal manner than would be the case where there was competition.

  Mitigation: meetings have been fully minuted and documented. Council team has maintained control of Issues List. All decisions and agreements have been properly authorised and recorded. Council has been successful in negotiating price reductions and commercial concessions during the period from appointment of Preferred Bidder to contract signature;

- **Risk:** weak negotiating position due to lack of competition.

  Mitigation: Alpha Schools have been warned on several occasions that the Council is prepared to stop the procurement on the grounds that the cost of recommencing are less than the cost of securing a poor deal. This has proved a successful tactic.

- **Risk:** poor value for money compared to PSC**.**

  Mitigation: The Council has actively used value for money and affordability as a negotiation tool. This strategy has resulted in an annual decrease in the unitary charge from the costs included within the Preferred Bidder model.

- **Risk:** poor value for money compared to competitive market priced**.**

  Mitigation: a Robust Reference Model / “Should Cost” model has been maintained for the capital and lifecycle costs throughout the procurement, in the form of the Shadow Bid model reproduced as Appendix 1. This has been updated during the negotiation period using benchmark input costs from other concurrent procurements to ensure validity and accuracy. Benchmarks have been established for key costs including: financing costs, hard and soft facilities management costs, Lifecycle maintenance costs, construction costs, insurance costs, SPV running costs, start-up costs.

- **Risk:** poor value for money in financing**.**

  Mitigation: bidder required to conduct funding competition to establish:
  - Best value senior debt provider;
  - Best value bond arranger and wrapper;
  - Whether senior debt or bond finance provides better value.

8. VALUE FOR MONEY ANALYSIS

8.1 Methodology

The purpose of the VfM analysis is to compare the Net Present Value (NPV) of the financial close model "Model for launch dayFINAL.xls", against the hypothetical PSC to confirm that, under reasonable assumptions, the PPP is likely to offer better value than direct procurement. VfM is achieved if the NPV of the PPP is lower than that of direct public sector procurement, as measured through the PSC.

The PSC is of particular importance in the Highland Schools procurement, because of Alpha's single bidder status.

To carry out the VfM analysis, it is therefore necessary to compare the NPV of the forecast service charge with the PSC adjusted for both technical risks and Optimism Bias in line with the new Green Book.

8.2 PPP Cost Elements and Service Charge

8.2.1 Alpha's Construction Costs

The Council's Technical Advisers to the project have undertaken a comprehensive analysis of the construction and related costs within the Alpha Schools submission. This analysis compared Alpha Schools cost structure with:

- The Public Sector Comparator;
- The costs (adjusted for inflation) on the PPP1 schools;
- BCIS index costs.

8.2.2 Alpha's Costs versus the PSC

The core Alpha construction cost is just under £134 million in outturn prices. The PSC estimate is just under £137 million on a non-risk adjusted basis, also in outturn prices.

Once the risk and Optimism Bias factors applying to the PSC cost estimate are taken into account, the Alpha Bid Price looks more attractive, because the Risk and OB factors applying to the PSC are significantly greater than to the Alpha Bids, reflecting the undeveloped nature of the client design which underpins the PSC.

8.2.3 Alpha's Costs compared to the BCIS Index

The comparison of Alpha's costs with the BCIS Index concluded that:

- The average costs per m^2 of gross internal floor area submitted for Primary, Secondary and SEN schools generally fall within expected cost parameters and would appear, in relation to the comparisons undertaken, to be competitive in their origin;

- The comparison of cost with the BCIS average costs highlights that all are towards the higher centile suggested by BCIS.

The following reasons have been given for the building costs being towards the higher centile of the BCIS average schools costs:

- The higher level of specification required by The Highland Council as Client;

- The need to design the schools to suit diverse highland climate conditions over varying school locations;

- The diverse location of the schools in relation to core labour and material sources;

- The inclusion of loose furniture and equipment costs in Bid costs, which are excluded in the BCIS average costs; and

- The impact of sustainability on design solutions.

8.2.4 Alpha's costs compared to Highland Schools PPP1

A comparison of the Alpha schools average costs with the projected average PPP1 costs, adjusted to 2007 outturn costs, indicated that the Alpha costs are lower than the escalated PPP1 costs.

8.2.5 Alpha's Financial Structure

To ensure that value for money was delivered by the project's financial structure, Alpha Schools was required to run a funding competition among senior lenders as part of their proposals. This concluded that the preferred senior lenders were Dexia Bank. The European Investment Bank agreed to provide £60 million. A report on the Funding competition was produced by Alpha's financial adviser, Grant Thornton, and has been included at Appendix 6.

8.2.6 Indexation of the Bond

Alpha schools were asked to prepare models comparing indexed and fixed rate bond structures. In order to make the fixed bond and the index linked bond models comparable 'live' gilt rates were used as per the Financial Times 27th April 2005.

This exercise demonstrated that whilst the index linked structure offers the Council a lower first year Unitary Charge, it does not offer best value over the full contract period due to the fact that the Unitary Payment is being indexed at 2.5% under the index linked bond solution as opposed to c. 1.5% under the fixed bond solution.

The assessment of the qualitative and quantitative factors (including sensitivity tests) led the council to conclude that the Fixed rate bond, using the 'x' indexation factor provided the best combination of value for money and cost certainty.

8.3 Comparison of FM, Lifecycle and SPV Operating Costs

Alpha Schools FM, Lifecycle and SPV Operating Costs have been subjected to close scrutiny to ensure that they represent value for money. The Table below compares the FM, LCM and SPV operating costs in the latest version of the Alpha model compared to those in the PSC and market benchmarks.

GFA: 64,344m^2 (Alpha)	Annual (Sept 05 prices)	Cost £m^{-2}	PSC £m^{-2}	Benchmark range £m^{-2}
FM[2]	£2,934,504	£45.61	£42.50	£41 to £45
Insurance (subject to market test)	£464,264	£7.22	£6.20	£6 to £8
SPV costs including Staff, Finance/Admin and Funders' TA	£130,000	£2.02	n/a	£6 to £10
Routine Maintenance Lifecycle Maintenance[3]	£450,408[4] £660,228			
All Maintenance	£1,110,636	£17.26	£22.65	£16 to £21, including routine maintenance

The benchmark data is derived from the rates seen in recent bids, including some where Alpha Schools has been in direct competition with other prominent players in the market. The analysis indicates that the recurrent costs in the Alpha model appear to be within the range typically seen in the market, and taken as a whole, better value than the PSC.

8.4 The Public Sector Comparator

8.4.1 Risk and Optimism Bias Factors

A detailed appraisal of risks and optimism bias was prepared to estimate the likelihood and impact of cost overruns on design, construction, LCM and FM costs. This is given as Appendix 2 of the Full Business Case.

8.4.2 Tax Adjustment

In accordance with Treasury Guidance, a factor needs to be added to the NPV of the PSC to allow for corporation tax that would be payable by a Project Co, which represents a net receipt to the Treasury. Applying the methodology set out in the Supplementary Green Book Guidance, *Adjusting*

[2] Calculated as figure in Alpha (£3,384,912) model minus £7 per m2 maintenance, over 64,344.
[3] Total LC costs of £19.8M over 30 years per 'Lifecycle Costs' sheet in Alpha model
[4] £7m^{-2} over 64,344 m^2.

for Taxation in PFI vs. PSC Comparisons, a tax factor of 5% has been added to the non-risk adjusted PSC.

8.5 NPV Comparison

The NPV of the PSC, adjusted for risk, optimism bias and tax, is computed as £265.058 million in current prices. The full PSC and Shadow Bid models are appended in Appendix 1 to this report.

To get a like-for-like comparison with the latest Alpha Bid model, the forecast stream of service charges payable to Alpha was rebased to April-March financial years, to arrive at NPV estimates for the two. The results are summarised in Table 8.1 below.

Table 8.1
Net Present Value Comparison

	£'000
NPV of the PSC at current prices - risk adjusted	£213,465
NPV of Risk and OB adjustment	£40,920
Plus: Adjustment for PPP Imputed Tax Element	£10,673
Current risk adjusted PSC including imputed tax	£265,058
NPV of the Alpha payment stream by fiscal year	£246,723
Value for Money Margin, £'000s	***£18,335***
Value for Money as a % of Alpha NPV	***7.43%***

Source: Highland Schools PPP - PSC and SBM FINAL.xls and Model for launch dayFINAL.xls

The NPV comparison shows that the whole life cycle cost of the Alpha Bid in NPV terms, at £246.723 million, is approximately £18.335 million less than the NPV of the risk-adjusted PSC, at £265.058 million – a Value for Money differential of 7.43% in favour of the Alpha bid.

The VFM margin does not take account of the following qualitative factors:

- Under the PPP, maintenance standards are contractually enforceable, with penalties applying in the event that contractual performance standards are not achieved, whereas under the PSC they are not;

- Under the PPP, funders will insist that the Alpha Project Co sets aside a dedicated Life Cycle Maintenance reserve to ensure that the schools are properly maintained over their life cycle. Under the PSC, this would not be the case, and, while any Council will use its best endeavours to fund the life cycle maintenance requirements of its buildings, in practice budgetary constraints and political priorities have in the past meant this has not always been achieved, leading to a progressive deterioration in the quality of public buildings;

- Under the PPP, Alpha will face contractual penalties for failure to meet the Services Availability Dates for each school. If the Council was to undertake the project through direct procurement, there would be significant deliverability risks which they would be required to manage. The Council has not managed a construction programme of this scale – the largest construction programme that they have managed to date, is for the rebuild of the secondary school at Ullapool which has a capital value of less than £20 million.

- If the PPP procurement were cancelled at this stage there would be a considerable delay in implementing a direct procurement, taking account of the need to work up detailed designs, secure planning consents for them, and tender the contracts under a traditional contract structure. These delays would lead to cost escalation.

Taking these factors into account, the PPP is judged as offering superior value for money, offering a lower NPV than direct Council procurement when account is taken of optimism bias, and offering qualitative benefits in terms of the phasing of the new schools programme and the contractual enforceability of maintenance standards following their commissioning.

9. AFFORDABILITY ANALYSIS

9.1 Target Affordability Position

In November 2003 the Council agreed a funding structure to meet an estimated full year Unitary Charge of £15.982 plus a contingency of £500,000 for potential interest rate increases on an April 2004 price base. After taking account of Scottish Executive Revenue Support of £7.16m per annum, and other funding streams, this resulted in an affordability gap of £7.529m on an April 2004 price base and is detailed in Table 9.1 below.

Table 9.1 – Target Affordability Position

	£m
Estimated full year Unitary Charge	15.982
Less	
Scottish Executive Revenue Support	7.160
Budgets for Transferred Services	1.630
Assumed Organisational Savings	0.163
Affordability Gap (Project Only)	**7.029**
Interest Rate Contingency	0.500
Total Affordability Gap	**7.529**

This remained the Council's approved affordability limit throughout the procurement process.

9.2 Funding the Unitary Charges

The full year Unitary Charge for the project, agreed at Financial Close, is £15.725m in April 2004 prices and is within the Council's agreed affordability limit £15.982m.

The funding structure approved by the Council in November 2003 is comprised of the three funding methods outlined below:

- Savings, resulting from demographic changes, which can be realised from the Education, Culture & Sport budget. These savings will accrue on a phased basis over four financial years commencing from 2006/07 and be sustained over the remainder of the 30 year life of the PPP contract. The Director of Education, Culture & Sport initially estimated that cumulative savings of £0.5 million per annum can be achieved from this source in each year over the four-year period, releasing a total of £2 million in year 4. The Director of Education Culture & Sport subsequently increased this £2m figure to £4m of which a maximum of £3.1m could be utilised to fund the PPP project;

- Utilising part of the School Building Fund allocation to Highland Council. At the meeting in November 2003, the Council agreed to allocate £1.522 million p.a. from this source;

- Four annual 1% increases in Council Tax over and above that which would otherwise be required to meet the balance of the affordability requirement. The November 2003 Council meeting agreed in principle that they would approve a Council Tax increase of up to 1% p.a. for four years to meet the funding requirement, generating a cumulative amount of £3.9 million in 2003/04 prices by year 4.

The Council, having now agreed the Unitary Charge, has approved a refined funding structure to match the funding requirements of the actual unitary charge.

Whilst the Council's approved Affordability level was stipulated on a 2004 price base, the Council has taken account of indexation of the Unitary Charge in its funding arrangements by using the indexed Unitary Charge figures specifically in the long term funding calculations for the project and generally in the Council's long term funding strategy to meet budgetary pressures. A summary of the Unitary Charge and the sources of funding that the Council will use to meet it are shown below in Table 9.2

Table 9.2 – UC and funding sources

FY	Service Charges based on 2.5% inflation	SE Revenue Support	Budgets for Transferred Services	Demographic Savings	Schools Buildings Fund	Increases in Council Tax	Total Revenue
2007/2008	£2,730,016	£1,143,492	£431,000	£1,480,000	£2,400,000		£5,454,492
2008/2009	£13,031,168	£6,146,485	£1,478,000	£2,474,000	£1,522,000	£1,850,000	£13,470,485
2009/2010	£18,148,741	£7,146,206	£1,857,000	£3,507,000	£2,768,535	£2,870,000	£18,148,741
2010/2011	£18,534,300	£7,420,882	£1,938,000	£3,595,000	£1,620,418	£3,960,000	£18,534,300
2011/2012	£18,756,712	£7,420,882	£1,986,450	£3,684,875	£1,704,505	£3,960,000	£18,756,712
2012/2013	£18,981,792	£7,420,882	£2,036,111	£3,776,997	£1,787,802	£3,960,000	£18,981,792
2013/2014	£19,209,574	£7,420,882	£2,087,014	£3,871,422	£1,870,256	£3,960,000	£19,209,574
2014/2015	£19,440,089	£7,420,882	£2,139,189	£3,968,207	£1,951,811	£3,960,000	£19,440,089
2015/2016	£19,673,370	£7,420,882	£2,192,669	£4,067,413	£2,032,406	£3,960,000	£19,673,370
2016/2017	£19,909,450	£7,420,882	£2,247,486	£4,169,098	£2,111,984	£3,960,000	£19,909,450
2017/2018	£20,148,364	£7,420,882	£2,303,673	£4,273,325	£2,190,484	£3,960,000	£20,148,364
2018/2019	£20,390,144	£7,420,882	£2,361,265	£4,380,158	£2,267,839	£3,960,000	£20,390,144
2019/2020	£20,634,826	£7,420,882	£2,420,296	£4,489,662	£2,343,986	£3,960,000	£20,634,826
2020/2021	£20,882,444	£7,420,882	£2,480,804	£4,601,904	£2,418,854	£3,960,000	£20,882,444
2021/2022	£21,133,033	£7,420,882	£2,542,824	£4,716,952	£2,492,375	£3,960,000	£21,133,033
2022/2023	£21,386,629	£7,420,882	£2,606,395	£4,834,875	£2,564,537	£3,960,000	£21,386,629
2023/2024	£21,643,269	£7,420,882	£2,671,554	£4,955,747	£2,635,086	£3,960,000	£21,643,269
2024/2025	£21,902,988	£7,420,882	£2,738,343	£5,079,641	£2,704,122	£3,960,000	£21,902,988
2025/2026	£22,165,824	£7,420,882	£2,806,802	£5,206,632	£2,771,508	£3,960,000	£22,165,824
2026/2027	£22,431,814	£7,420,882	£2,876,972	£5,336,798	£2,837,162	£3,960,000	£22,431,814
2027/2028	£22,700,996	£7,420,882	£2,948,896	£5,470,218	£2,901,000	£3,960,000	£22,700,996
2028/2029	£22,973,408	£7,420,882	£3,022,619	£5,606,973	£2,962,934	£3,960,000	£22,973,408
2029/2030	£23,249,089	£7,420,882	£3,098,184	£5,747,147	£3,022,876	£3,960,000	£23,249,089
2030/2031	£23,528,078	£7,420,882	£3,175,639	£5,890,826	£3,080,731	£3,960,000	£23,528,078
2031/2032	£23,810,415	£7,420,882	£3,255,030	£6,038,097	£3,136,406	£3,960,000	£23,810,415
2032/2033	£24,096,140	£7,420,882	£3,336,405	£6,189,049	£3,189,804	£3,960,000	£24,096,140
2033/2034	£24,385,293	£7,420,882	£3,419,816	£6,343,775	£3,240,820	£3,960,000	£24,385,293
2034/2035	£24,677,917	£7,420,882	£3,505,311	£6,502,370	£3,289,354	£3,960,000	£24,677,917
2035/2036	£24,974,052	£7,420,882	£3,592,944	£6,664,929	£3,335,297	£3,960,000	£24,974,052
2036/2037	£25,273,740	£7,420,885	£3,682,767	£6,831,552	£3,378,536	£3,960,000	£25,273,740

In setting the affordability limit for the project and agreeing the funding structure to meet the affordability limit, the Council is aware that the project is at the limits of its affordability and that the School Building Fund is only provided on a 3 year allocation basis. As a result, a Contingency Plan was approved by the Council to cover the potential of a shortfall in the approved funding structure.

The approved Contingency Plan covers the use of the following funding sources to meet any potential shortfall:

- Using a greater proportion of the savings resulting from demographic changes;
- Making further savings within the Education Culture & Sport Revenue Budget or Capital Programme;
- Making savings across all Council Services either in their Revenue Budget or Capital Programme;
- Further increases in Council Tax; or
- A combination of the above.

In summary the Council has agreed a Unitary Charge at Financial Close which is within the approved affordability limit and the ongoing project costs have been included in the Council's long term funding strategy.

10. ACCOUNTING TREATMENT

The Council has received confirmation from Audit Scotland, by way of a letter dated 24 February 2006 confirming that:

- the process followed to determine whether the council should account for the transaction on or off its balance sheet was in accordance with the current underlying guidance; and
- the final judgment on the accounting treatment that the project facilities should not be accounting for on the Councils Balance Sheet is reasonable.

11. THE PROJECT AGREEMENT

11.1 Overview

This Section:

- describes the contractual framework of the Project,
- outlines the legal relationship between the various parties; and
- sets out the derogations from the Scottish Schools Standard Form Project Agreement (Appendix 5).

11.2 Contractual Framework of the Project

The Highland Council (**THE COUNCIL**) is developing a contract for the design, construction, financing and operation of certain educational facilities in the Highlands and associated services under the Private Finance Initiative of Her Majesty's Government (**the Project**) based as closely as possible on the Scottish Schools Standard Form Project Agreement, Version 3 (**SSSC v3**). The contract structure recognises the interests of all parties to the Project Agreement (**the Agreement**), including the funders and the various sub-contractors providing services to THE COUNCIL. The terms of SSSC v3 are being retained, but in line with applicable guidance for using SSSC v3 some provisions of the Agreement have been tailored to the particular requirements of the Project. These are described in more detail in Appendix 5.

11.3 Principal Sub-Contracts

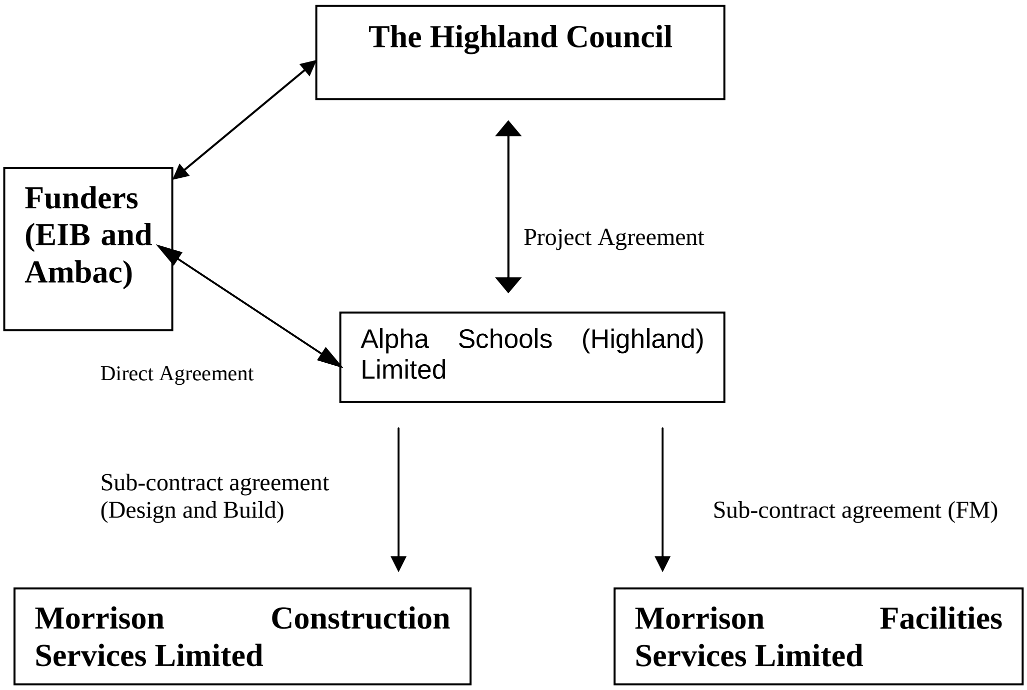
The principal subcontracts within the project are:

- Design & Build contract with Morrison Construction Services Limited
- FM Agreement with Morrison Facilities Services Limited
- Financing Agreement and other documentation with the European Investment Bank and Ambac Assurance UK Limited

These contracts create the contractual relationships represented in diagrammatic form in 11.4 below.

11.4 Legal Relationships between the Parties

A Special Purpose Company (Alpha Schools (Highland) Limited) has been established to deliver the project. The proposed structure is described by diagram as follows;



11.5 Key Commercial Terms

A full list of the derogation from the Scottish Schools Standard Form Project Agreement is included as Appendix 5. The main derogations which the Council have considered as giving additional value for money to the Project, which has either been incorporated within the bid pricing or terms or which have been obtained since bid submission are as follows:

- The Council have accepted a cap on malicious damage costs, thereby reducing the annual FM charge by £120,000;
- There have been various changes to the financing definitions and provisions relating to compensation payable on early termination of the project, largely to reflect the method of funding used in this project (being bond funding as opposed to more traditional bank finance);

- Provisions have been inserted to reflect that the construction period for certain external areas will take longer than the construction period for the new schools;
- Provisions have been inserted dealing with co-operation between the project company and the Council's catering provider, since catering does not form part of the project;
- The concept of flexible use hours has been introduced to allow the Council cost effective use of the schools outwith normal educational periods;
- There have been various changes to the employment and pension provisions to ensure that the Council employees who are transferring and those who are employed during the course of the project are protected and that the risk sharing between the Council and the project company represents value for money;
- Insurance premium sharing proposals have been inserted since the ITN, reflecting the proposals released by the Scottish Executive in March 2005.

12. PROJECT MANAGEMENT ARRANGEMENTS

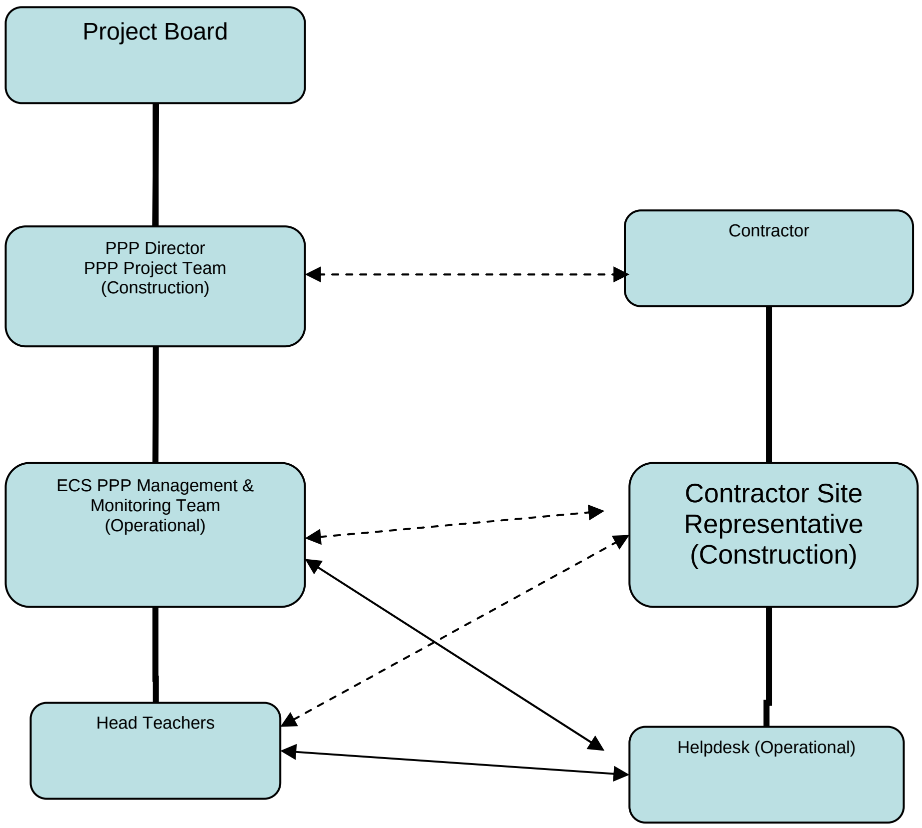
12.1 Introduction

The Council has established contract monitoring procedures in place to monitor their first Schools PPP and it is their intention to extend these to the second Schools PPP following financial close. This section outlines the contract monitoring structures to be adopted for both the construction and operational phases and the monitoring which will be implemented following Services Availability.

12.2 Project Management Structures

Figure 1.1 below summarises, the Project Management Reporting Structures to be implemented by Highland Council during both the construction and operational phases of Schools PPP2.

Figure 1.1: Project Management and Monitoring Arrangements



Key:
Operation
Construction

12.3 Monitoring

The Council anticipates monitoring the following aspects of the Contractor's performance to meet its management and monitoring obligations after the facilities become available:

- Compliance with the project agreement, payment mechanism and life cycle programme. & FM costs.
- Compliance with the FM output specification
- Compliance of the Helpdesk mechanism
- Compliance of the annual PPM schedules
- Compliance of service delivery, including spot audits, analyse monthly contract monitoring reports.
- Compliance with the school & community letting services
- Compliance of all health & Safety legislation including but not limited to the adherence of the mobilisation plan, site specific method statements and the QMS
- Compliance with the handover process to ensure that the as built submission information is all in place and that all manuals etc are present and correct, not forgetting workshops on how all areas of the school work including details of any extended guarantees
- Monitoring of the defect rectifications from the final snagging lists
- Ensure all insurance policies are in place, - buildings, contents, public liability & employers Liability
- Performance monitoring, self monitoring audits & condition surveys

12.4 Monitoring Process

The Post Construction Project Management process will include a commissioned Project Management Liaison Committee which will meet with the contractor/SPV on a monthly basis to discuss any issues which have arisen from the previous month and to discuss any relevant deductions. The Liaison Committee will have received a written and verbal report from the Education, Culture & Sport ("ECS") PPP Management & Monitoring Team on these issues so that these issues can be raised at this forum.

The Project Board will rarely be in attendance unless there are issues of grave importance, the Board will as a rule receive reports prior to and post meeting so that they are aware of any situations and the resultant outcomes. The Project Board will meet six monthly or as required in the event that any extraordinary problems arise.

The ECS PPP Management & Monitoring team will also monitor the interface mechanisms, not only for compliance, but to address issues that are not apparent but may cause future friction. The reports issued in advance of the Project Management Liaison Committee Meetings noted above will also include information pertaining to the interface mechanisms and will be made available to both the Liaison Committee & the Project Board.

APPENDIX 1 - PUBLIC SECTOR COMPARATOR AND SHADOW BID MODEL

APPENDIX 2 – RISK AND OPTIMISM BIAS REPORT

APPENDIX 3 – VALUE FOR MONEY ANALYSIS

APPENDIX 4 – AUDIT LETTER FROM AUDIT SCOTLAND

APPENDIX 5 – TABLE OF DEROGATIONS FROM THE SSSC

APPENDIX 6 – FUNDING COMPETITION REPORT

PSC

construction starts 05/06

		yr		2006/2007	2007/2008	2008/2009	2009/2010	2010/2011	2011/2012	2012/2013	2013/2014	2014/2015	2015/2016	2016/2017	2017/2018	2018/2019	2019/2020	2020/2021	2021/2022
		mid	01/04/06	30/09/06	30/09/07	30/09/08	30/09/09	30/09/10	30/09/11	30/09/12	30/09/13	30/09/14	30/09/15	30/09/16	30/09/17	30/09/18	30/09/19	30/09/20	30/09/21
		XNPV	0	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
Base capital		0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Base Capital (nominal)		125,600	0	43,546	54,501	36,699	2,191	0	0	0	0	0	0	0	0	0	0	0	0
Construction Cost Risk	18.03%	22,646	0	7,851	9,826	6,617	395	0	0	0	0	0	0	0	0	0	0	0	0
		148,246	0	51,397	64,327	43,316	2,586	0	0	0	0	0	0	0	0	0	0	0	0
check npvs up and across		TRUE																	
		148,246	0	51,397	64,327	43,316	2,586	0	0	0	0	0	0	0	0	0	0	0	0
optimism bias		4,447	0	1,542	1,930	1,299	78	0	0	0	0	0	0	0	0	0	0	0	0
Captial per model		152,694	0	52,939	66,257	44,615	2,664	0	0	0	0	0	0	0	0	0	0	0	0
check npvs up and across		TRUE																	
FM		44,853	0.00	0.00	316.04	588.98	2,626.10	3,093.97	3,171.32	3,250.60	3,331.87	3,415.17	3,500.54	3,588.06	3,677.76	3,769.70	3,863.95	3,960.55	4,059.56
Rates		9,021	0.00	0.00	63.56	118.46	528.17	622.27	637.83	653.78	670.12	686.87	704.05	721.65	739.69	758.18	777.14	796.56	816.48
Admin		2,939	0.00	256.25	262.66	269.22	275.95	147.08	150.76	154.53	158.39	162.35	166.41	170.57	174.84	179.21	183.69	188.28	192.99
Insurance		7,148	0.00	256.25	262.66	269.22	275.95	452.56	463.88	475.47	487.36	499.55	512.03	524.83	537.96	551.40	565.19	579.32	593.80
		63,961	0.00	512.50	904.91	1,245.88	3,706.18	4,315.89	4,423.79	4,534.38	4,647.74	4,763.94	4,883.04	5,005.11	5,130.24	5,258.50	5,389.96	5,524.71	5,662.82
check npvs up and across		TRUE																	
Risk adjustment per CE excl rates		8,175	0.00	76.26	125.19	167.76	472.89	549.61	563.35	577.43	591.87	606.67	621.83	637.38	653.31	669.65	686.39	703.55	721.14
OB adjustment		1,546	0.00	0.00	10.89	20.30	90.51	106.63	109.30	112.03	114.83	117.70	120.64	123.66	126.75	129.92	133.17	136.50	139.91
FM etc Risk and OB adjusted		73,682	0.00	588.76	1,041.00	1,433.94	4,269.58	4,972.13	5,096.44	5,223.85	5,354.44	5,488.30	5,625.51	5,766.15	5,910.30	6,058.06	6,209.51	6,364.75	6,523.87
LCM unadjusted		23,904	0.00	0	168	314	1,400	1,649	1,690	1,732	1,776	1,820	1,866	1,912	1,960	2,009	2,059	2,111	2,164
LCM risk adjustment		3,557	0	0	25.06222411	46.70687221	208.2542664	245.3570381	251.490964	257.7782381	264.2226941	270.8282614	277.5989679	284.5389421	291.6524157	298.9437261	306.4173192	314.0777522	321.929696
LCM Provision Risk adjusted		27,461	0.00	0.00	193.49	360.60	1,607.81	1,894.26	1,941.62	1,990.16	2,039.91	2,090.91	2,143.18	2,196.76	2,251.68	2,307.97	2,365.67	2,424.82	2,485.44
check npvs up and across		TRUE																	
LCM Optimism Bias		549	0.00	0	4	7	32	38	39	40	41	42	43	44	45	46	47	48	50
		101,692	0.00	588.76	1,238.36	1,801.75	5,909.55	6,904.28	7,076.89	7,253.81	7,435.15	7,621.03	7,811.56	8,006.85	8,207.02	8,412.20	8,622.50	8,838.06	9,059.01
check npvs up and across		TRUE																	

NPV without Risk Adjustment	213,465
Tax adjustment	10,673
NPV of Risk and OB adjustments	40,920
Total Risk Adjusted NPV of PSC	265,058

2022/2023	2023/2024	2024/2025	2025/2026	2026/2027	2027/2028	2028/2029	2029/2030	2030/2031	2031/2032	2032/2033	2033/2034	2034/2035	2035/2036	2036/2037	2037/2038	2038/2039	2039/2040	2040/2041	2041/2042	2042/2043	2043/2044
30/09/22	30/09/23	30/09/24	30/09/25	30/09/26	30/09/27	30/09/28	30/09/29	30/09/30	30/09/31	30/09/32	30/09/33	30/09/34	30/09/35	30/09/36	30/09/37	30/09/38	30/09/39	30/09/40	30/09/41	30/09/42	30/09/43
17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	34	35	36	37	38
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
4,161.05	4,265.07	4,371.70	4,480.99	4,593.02	4,707.84	4,825.54	4,946.18	5,069.83	5,196.58	5,326.49	5,459.66	5,596.15	5,736.05	2,939.73	0	0	0	0	0	0	0
836.89	857.81	879.26	901.24	923.77	946.86	970.54	994.80	1,019.67	1,045.16	1,071.29	1,098.07	1,125.52	1,153.66	591.25	0	0	0	0	0	0	0
197.81	202.76	207.82	213.02	218.35	223.80	229.40	235.13	241.01	247.04	253.21	259.54	266.03	272.68	139.75	0	0	0	0	0	0	0
608.65	623.86	639.46	655.45	671.83	688.63	705.84	723.49	741.58	760.12	779.12	798.60	818.56	839.03	860.00	0	0	0	0	0	0	0
5,804.40	5,949.51	6,098.24	6,250.70	6,406.97	6,567.14	6,731.32	6,899.60	7,072.09	7,248.89	7,430.12	7,615.87	7,806.27	8,001.42	4,530.73	0	0	0	0	0	0	0
739.16	757.64	776.59	796.00	815.90	836.30	857.20	878.63	900.60	923.12	946.19	969.85	994.09	1018.95	586.19	0	0	0	0	0	0	0
143.41	146.99	150.67	154.43	158.29	162.25	166.31	170.47	174.73	179.09	183.57	188.16	192.87	197.69	101.31	0	0	0	0	0	0	0
6,686.97	6,854.14	7,025.49	7,201.13	7,381.16	7,565.69	7,754.83	7,948.70	8,147.42	8,351.10	8,559.88	8,773.88	8,993.23	9,218.06	5,218.24	0	0	0	0	0	0	0
2,218	2,273	2,330	2,388	2,448	2,509	2,572	2,636	2,702	2,769	2,839	2,910	2,982	3,057	1,567	0	0	0	0	0	0	0
329.9779384	338.2273869	346.6830716	355.3501484	364.2339021	373.3397496	382.6732434	392.2400744	402.0460763	412.0972282	422.3996589	432.9596504	443.7836416	454.8782327	233.1250943	0	0	0	0	0	0	0
2,547.57	2,611.26	2,676.54	2,743.46	2,812.04	2,882.34	2,954.40	3,028.26	3,103.97	3,181.57	3,261.11	3,342.63	3,426.20	3,511.86	1,799.83	0.00	0.00	0.00	0.00	0.00	0.00	0.00
51	52	54	55	56	58	59	61	62	64	65	67	69	70	36	0.00	0.00	0.00	0.00	0.00	0.00	0.00
9,285.49	9,517.63	9,755.57	9,999.46	10,249.44	10,505.68	10,768.32	11,037.53	11,313.47	11,596.30	11,886.21	12,183.37	12,487.95	12,800.15	7,054.06	0.00	0.00	0.00	0.00	0.00	0.00	0.00

FYs beginning April 5th	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Project Years	1	2	3	4	5	6	7	8	9	10	11	12
Capital Required												
Capital Costs (net of land transactions)	43,546	54,501	36,699	2,191	0	0	0	0	0	0	0	0
Setup Costs	4,575											
Arrangement fees - senior debt	1,782											
Commitment fees - senior debt		642	359	169	0	0	0	0	0	0	0	0
Arrangement fees - sub debt	267											
Commitment fees - sub debt		128	72	34	0	0	0	0	0	0	0	0
Pre-funded Reserve Account	0	0										
Total Costs to be Funded	**50,170**	**55,271**	**37,130**	**2,394**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Funded by:												
Senior Debt	49,852	56,461	38,019	2,270	0	0	0	0	0	0	0	0
Equity	554	627	422	25	0	0	0	0	0	0	0	0
Sub-ordinated debt	4,985	5,646	3,802	227	0	0	0	0	0	0	0	0
Step - up Unitary Charge												
Total Funding	**55,391**	**62,735**	**42,243**	**2,522**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Source & Application of Funds:												
Equity Subscriptions	554	627	422	25	0	0	0	0	0	0	0	0
Sub-ordinated debt drawdowns	4,985	5,646	3,802	227	0	0	0	0	0	0	0	0
Senior Debt Drawdown	49,852	56,461	38,019	2,270	0	0	0	0	0	0	0	0
Part payment of contract debtor	0	0	0	0	3,284	3,470	3,667	3,875	4,094	4,327	4,572	4,831
Interest earned on positive cash balances	19	138	240	127	220	223	255	295	342	369	395	422
Operating surplus	-1,104	422	1,520	11,919	10,365	10,289	10,191	10,082	9,960	9,825	9,675	9,512
Total sources:	*54,307*	*63,295*	*44,003*	*14,568*	*13,869*	*13,982*	*14,113*	*14,252*	*14,396*	*14,520*	*14,643*	*14,765*
Applications:												
Investment programme net of land transactions	43,546	54,501	36,699	2,191	0	0	0	0	0	0	0	0
Furniture & Fixtures	0	0	0	0	0	0	0	0	0	0	0	0
Professional fees & uplift	0	0	0	0	0	0	0	0	0	0	0	0
Loan repayments - Senior Debt	0	0	0	0	2,799	2,957	3,125	3,302	3,490	3,687	3,896	4,117
Interest payments - Senior Debt	1,413	4,427	7,106	8,248	8,312	8,154	7,986	7,809	7,622	7,424	7,215	6,994
Loan repayments - Sub debt	-	-	-	-	90	101	114	128	144	162	182	205
Interest payments - Sub debt	312	976	1,567	1,818	1,833	1,821	1,809	1,794	1,778	1,760	1,740	1,717
Interest payments - overdraft	0	0	0	117	57	99	55	0	0	0	0	0
Setup Costs	4,575	0	0	0	0	0	0	0	0	0	0	0
Arrangement fees - senior debt	1,782	0	0	0	0	0	0	0	0	0	0	0
Commitment fees - senior debt	0	642	359	169	0	0	0	0	0	0	0	0
Arrangement fees - sub debt	267	0	0	0	0	0	0	0	0	0	0	0
Commitment fees - sub debt	0	128	72	34	0	0	0	0	0	0	0	0
Insurance costs during construction	256	263	269	276	0	0	0	0	0	0	0	0
Pre-funded Reserve Account	0	0	0	0	0	0	0	0	0	0	0	0
Corporate taxation paid	0	0	0	0	0	115	131	179	232	271	303	335
Dividends paid	0	0	0	0	0	0	0	0	539	628	703	777
Transfer to (from) debt reserve account	862	1,839	1,635	755	1,454	21	0	-22	-28	0	0	0
Change in cash balances	1,293	519	-3,703	960	-676	713	893	1,061	619	588	603	620
Total applications:	*54,307*	*63,295*	*44,003*	*14,568*	*13,869*	*13,982*	*14,113*	*14,252*	*14,396*	*14,520*	*14,643*	*14,765*

FYs beginning April 5th	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Profit & loss account:												
Escalation factor applying to unitary charge	1.025	1.051	1.064	1.077	1.091	1.104	1.118	1.132	1.146	1.160	1.175	1.190
% of unitary charge calculation	0.0%	11.0%	20.0%	87.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Total service payments by The Highland Council	0	2,113	3,889	17,130	19,936	20,185	20,437	20,693	20,951	21,213	21,478	21,747
Of which:												
Part repayment of finance debtor	0	0	0	0	-3,284	-3,470	-3,667	-3,875	-4,094	-4,327	-4,572	-4,831
Operating income to Project Co from non-D&B services	0	2,113	3,889	17,130	16,652	16,715	16,770	16,818	16,857	16,887	16,906	16,916
Property revenue (FM) costs	0	316	589	2,626	3,094	3,171	3,251	3,332	3,415	3,501	3,588	3,678
Life cycle maintenance provision	1,104	1,228	1,529	1,565	1,545	1,573	1,612	1,653	1,694	1,736	1,780	1,824
Rates	0	64	118	528	622	638	654	670	687	704	722	740
Insurance costs	0	0	0	0	453	464	475	487	500	512	525	538
Annual agency fee for loan monitoring		25	27	23	27	28	28	28	29	29	29	30
Annual costs of SPV administration		58	106	469	545	552	559	566	573	580	587	595
Operating surplus:	-1,104	422	1,520	11,919	10,365	10,289	10,191	10,082	9,960	9,825	9,675	9,512
Interest earned on positive cash balances	19	138	240	127	220	223	255	295	342	369	395	422
Interest charges on debt servicing	0	0	0	0	10,202	10,074	9,850	9,603	9,400	9,184	8,955	8,711
Profit before tax:	-1,084	561	1,760	12,046	383	438	597	774	902	1,009	1,116	1,223
Corporation tax payable	0	0	0	0	115	131	179	232	271	303	335	367
Profit after tax:	-1,084	561	1,760	12,046	268	306	418	542	631	707	781	856
Dividends declared	0	0	0	0	0	0	0	539	628	703	777	852
Retained profits for the year	-1,084	561	1,760	12,046	268	306	418	3	3	4	4	4
Retained profits brought forward	0	-1,084	-524	1,237	13,283	13,550	13,857	14,275	14,277	14,280	14,284	14,288
Retained profits carried forward:	-1,084	-524	1,237	13,283	13,550	13,857	14,275	14,277	14,280	14,284	14,288	14,292
Balance Sheet:												
Non-current asset: contract debtor	52,151	113,088	159,160	172,013	168,729	165,259	161,592	157,717	153,623	149,296	144,724	139,893
Debt Reserve Account	862	2,702	4,336	5,091	6,545	6,566	6,566	6,544	6,517	6,517	6,517	6,517
Cash	1,293	1,812	-1,890	-931	-1,607	-893	0	1,061	1,680	2,268	2,871	3,491
less: Corporation tax payable	0	0	0	0	-115	-131	-179	-232	-271	-303	-335	-367
Dividends payable	0	0	0	0	0	0	0	-539	-628	-703	-777	-852
Net current assets	1,293	1,812	-1,890	-931	-1,722	-1,025	-179	290	782	1,262	1,759	2,272
Total assets :	**54,307**	**117,602**	**161,605**	**176,173**	**173,553**	**170,800**	**167,979**	**164,552**	**160,921**	**157,075**	**153,000**	**148,682**
Financed by:												
Share capital	554	1,181	1,604	1,629	1,629	1,629	1,629	1,629	1,629	1,629	1,629	1,629
Retained profits	-1,084	-524	1,237	13,283	13,550	13,857	14,275	14,277	14,280	14,284	14,288	14,292
Sub-ordinated debt	4,985	10,631	14,433	14,660	14,570	14,469	14,355	14,227	14,083	13,921	13,739	13,534
Sub-total, equity:	4,455	11,289	17,273	29,572	29,750	29,955	30,259	30,133	29,993	29,834	29,656	29,455
Senior Debt	49,852	106,313	144,332	146,602	143,803	140,846	137,720	134,418	130,929	127,241	123,345	119,227
Total financing:	**54,307**	**117,602**	**161,605**	**176,173**	**173,553**	**170,800**	**167,979**	**164,552**	**160,921**	**157,075**	**153,000**	**148,682**

FYs beginning April 5th	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Project Years	13	14	15	16	17	18	19	20	21	22	23	24
Capital Required												
Capital Costs (net of land transactions)	0	0	0	0	0	0	0	0	0	0	0	0
Setup Costs												
Arrangement fees - senior debt												
Commitment fees - senior debt	0	0	0	0	0	0	0	0	0	0	0	0
Arrangement fees - sub debt												
Commitment fees - sub debt	0	0	0	0	0	0	0	0	0	0	0	0
Pre-funded Reserve Account												
Total Costs to be Funded	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Funded by:												
Senior Debt	0	0	0	0	0	0	0	0	0	0	0	0
Equity	0	0	0	0	0	0	0	0	0	0	0	0
Sub-ordinated debt	0	0	0	0	0	0	0	0	0	0	0	0
Step - up Unitary Charge												
Total Funding	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Source & Application of Funds:												
Equity Subscriptions	0	0	0	0	0	0	0	0	0	0	0	0
Sub-ordinated debt drawdowns	0	0	0	0	0	0	0	0	0	0	0	0
Senior Debt Drawdown	0	0	0	0	0	0	0	0	0	0	0	0
Part payment of contract debtor	5,105	5,394	5,700	6,024	6,365	6,726	7,107	7,510	7,936	8,386	8,862	9,364
Interest earned on positive cash balances	450	479	508	538	569	600	631	663	694	726	758	789
Operating surplus	9,332	9,136	8,923	8,691	8,440	8,169	7,875	7,559	7,218	6,852	6,458	6,036
Total sources:	*14,888*	*15,010*	*15,132*	*15,253*	*15,374*	*15,494*	*15,613*	*15,732*	*15,849*	*15,964*	*16,078*	*16,189*
Applications:												
Investment programme net of land transactions	0	0	0	0	0	0	0	0	0	0	0	0
Furniture & Fixtures	0	0	0	0	0	0	0	0	0	0	0	0
Professional fees & uplift	0	0	0	0	0	0	0	0	0	0	0	0
Loan repayments - Senior Debt	4,351	4,598	4,858	5,134	5,425	5,732	6,057	6,401	6,764	7,147	7,553	7,981
Interest payments - Senior Debt	6,760	6,513	6,253	5,977	5,686	5,379	5,054	4,710	4,347	3,964	3,559	3,130
Loan repayments - Sub debt	231	260	292	329	370	416	468	526	592	666	749	843
Interest payments - Sub debt	1,692	1,663	1,630	1,594	1,553	1,507	1,455	1,396	1,330	1,256	1,173	1,080
Interest payments - overdraft	0	0	0	0	0	0	0	0	0	0	0	0
Setup Costs	0	0	0	0	0	0	0	0	0	0	0	0
Arrangement fees - senior debt	0	0	0	0	0	0	0	0	0	0	0	0
Commitment fees - senior debt	0	0	0	0	0	0	0	0	0	0	0	0
Arrangement fees - sub debt	0	0	0	0	0	0	0	0	0	0	0	0
Commitment fees - sub debt	0	0	0	0	0	0	0	0	0	0	0	0
Insurance costs during construction	0	0	0	0	0	0	0	0	0	0	0	0
Pre-funded Reserve Account	0	0	0	0	0	0	0	0	0	0	0	0
Corporate taxation paid	367	399	432	464	497	531	565	599	634	670	707	745
Dividends paid	852	927	1,002	1,078	1,155	1,233	1,311	1,391	1,473	1,556	1,642	1,730
Transfer to (from) debt reserve account	0	0	0	0	0	0	0	0	0	0	0	0
Change in cash balances	635	650	664	677	688	697	704	707	708	704	695	680
Total applications:	*14,888*	*15,010*	*15,132*	*15,253*	*15,374*	*15,494*	*15,613*	*15,732*	*15,849*	*15,964*	*16,078*	*16,189*

FYs beginning April 5th	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Profit & loss account:												
Escalation factor applying to unitary charge	1.204	1.220	1.235	1.250	1.266	1.282	1.298	1.314	1.330	1.347	1.364	1.381
% of unitary charge calculation	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Total service payments by The Highland Council	22,019	22,294	22,573	22,855	23,140	23,430	23,722	24,019	24,319	24,623	24,931	25,243
Of which:												
Part repayment of finance debtor	-5,105	-5,394	-5,700	-6,024	-6,365	-6,726	-7,107	-7,510	-7,936	-8,386	-8,862	-9,364
Operating income to Project Co from non-D&B services	16,914	16,899	16,872	16,831	16,775	16,704	16,615	16,509	16,383	16,237	16,069	15,879
Property revenue (FM) costs	3,770	3,864	3,961	4,060	4,161	4,265	4,372	4,481	4,593	4,708	4,826	4,946
Life cycle maintenance provision	1,870	1,916	1,964	2,013	2,064	2,115	2,168	2,222	2,278	2,335	2,393	2,453
Rates	758	777	797	816	837	858	879	901	924	947	971	995
Insurance costs	551	565	579	594	609	624	639	655	672	689	706	723
Annual agency fee for loan monitoring	30	30	31	31	32	32	32	33	33	34	34	35
Annual costs of SPV administration	602	610	617	625	633	641	649	657	665	673	682	690
Operating surplus:	9,332	9,136	8,923	8,691	8,440	8,169	7,875	7,559	7,218	6,852	6,458	6,036
Interest earned on positive cash balances	450	479	508	538	569	600	631	663	694	726	758	789
Interest charges on debt servicing	8,452	8,176	7,883	7,571	7,239	6,885	6,508	6,106	5,678	5,220	4,732	4,210
Profit before tax:	1,331	1,439	1,548	1,658	1,770	1,883	1,998	2,115	2,235	2,358	2,484	2,615
Corporation tax payable	399	432	464	497	531	565	599	634	670	707	745	785
Profit after tax:	931	1,007	1,084	1,161	1,239	1,318	1,398	1,480	1,564	1,650	1,739	1,831
Dividends declared	927	1,002	1,078	1,155	1,233	1,311	1,391	1,473	1,556	1,642	1,730	1,822
Retained profits for the year	5	5	5	6	6	7	7	7	8	8	9	9
Retained profits brought forward	14,292	14,297	14,302	14,307	14,313	14,319	14,326	14,333	14,340	14,348	14,356	14,365
Retained profits carried forward:	14,297	14,302	14,307	14,313	14,319	14,326	14,333	14,340	14,348	14,356	14,365	14,374
Balance Sheet:												
Non-current asset: contract debtor	134,788	129,394	123,693	117,670	111,305	104,579	97,471	89,961	82,025	73,639	64,777	55,413
Debt Reserve Account	6,517	6,517	6,517	6,517	6,517	6,517	6,517	6,517	6,517	6,517	6,517	6,517
Cash	4,126	4,776	5,441	6,118	6,806	7,503	8,206	8,914	9,621	10,325	11,020	11,700
less: Corporation tax payable	-399	-432	-464	-497	-531	-565	-599	-634	-670	-707	-745	-785
Dividends payable	-927	-1,002	-1,078	-1,155	-1,233	-1,311	-1,391	-1,473	-1,556	-1,642	-1,730	-1,822
Net current assets	2,800	3,342	3,898	4,465	5,042	5,626	6,216	6,806	7,394	7,976	8,544	9,094
Total assets :	**144,105**	**139,253**	**134,108**	**128,652**	**122,864**	**116,722**	**110,204**	**103,284**	**95,936**	**88,131**	**79,838**	**71,023**
Financed by:												
Share capital	1,629	1,629	1,629	1,629	1,629	1,629	1,629	1,629	1,629	1,629	1,629	1,629
Retained profits	14,297	14,302	14,307	14,313	14,319	14,326	14,333	14,340	14,348	14,356	14,365	14,374
Sub-ordinated debt	13,303	13,043	12,751	12,423	12,053	11,637	11,170	10,643	10,051	9,385	8,636	7,793
Sub-total, equity:	29,229	28,974	28,688	28,365	28,001	27,592	27,132	26,613	26,029	25,371	24,630	23,796
Senior Debt	114,876	110,279	105,421	100,287	94,862	89,130	83,072	76,671	69,908	62,760	55,208	47,227
Total financing:	**144,105**	**139,253**	**134,108**	**128,652**	**122,864**	**116,722**	**110,204**	**103,284**	**95,936**	**88,131**	**79,838**	**71,023**

FYs beginning April 5th	2030	2031	2032	2033	2034	2035	2036	2037
Project Years	25	26	27	28	29	30	31	32
Capital Required								
Capital Costs (net of land transactions)	0	0	0	0	0	0	0	0
Setup Costs								
Arrangement fees - senior debt								
Commitment fees - senior debt	0	0	0	0	0	0	0	0
Arrangement fees - sub debt								
Commitment fees - sub debt	0	0	0	0	0	0	0	0
Pre-funded Reserve Account								
Total Costs to be Funded	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Funded by:								
Senior Debt	0	0	0	0	0	0	0	0
Equity	0	0	0	0	0	0	0	0
Sub-ordinated debt	0	0	0	0	0	0	0	0
Step - up Unitary Charge								
Total Funding	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Source & Application of Funds:								
Equity Subscriptions	0	0	0	0	0	0	0	0
Sub-ordinated debt drawdowns	0	0	0	0	0	0	0	0
Senior Debt Drawdown	0	0	0	0	0	0	0	0
Part payment of contract debtor	9,895	10,456	11,049	11,675	12,337	0	0	0
Interest earned on positive cash balances	820	849	878	904	964	1,041	1,597	1,211
Operating surplus	5,584	5,099	4,581	4,811	5,416	18,601	9,188	75
Total sources:	*16,298*	*16,405*	*16,508*	*17,390*	*18,717*	*19,642*	*10,785*	*1,287*
Applications:								
Investment programme net of land transactions	0	0	0	0	0	0	0	0
Furniture & Fixtures	0	0	0	0	0	0	0	0
Professional fees & uplift	0	0	0	0	0	0	0	0
Loan repayments - Senior Debt	8,433	8,911	9,417	9,951	10,515	0	0	0
Interest payments - Senior Debt	2,678	2,200	1,694	1,160	596	0	0	0
Loan repayments - Sub debt	948	1,067	1,200	1,350	1,519	1,709	-	-
Interest payments - Sub debt	974	856	722	572	403	214	-	-
Interest payments - overdraft	0	0	0	0	0	0	0	0
Setup Costs	0	0	0	0	0	0	0	0
Arrangement fees - senior debt	0	0	0	0	0	0	0	0
Commitment fees - senior debt	0	0	0	0	0	0	0	0
Arrangement fees - sub debt	0	0	0	0	0	0	0	0
Commitment fees - sub debt	0	0	0	0	0	0	0	0
Insurance costs during construction	0	0	0	0	0	0	0	0
Pre-funded Reserve Account	0	0	0	0	0	0	0	0
Corporate taxation paid	785	825	868	913	1,195	1,614	5,829	3,236
Dividends paid	1,822	1,916	2,015	2,119	2,774	3,747	13,532	7,512
Transfer to (from) debt reserve account	0	0	0	0	0	0	-5,556	-961
Change in cash balances	659	629	591	1,325	1,715	12,359	-3,020	-8,500
Total applications:	*16,298*	*16,405*	*16,508*	*17,390*	*18,717*	*19,642*	*10,785*	*1,287*

FYs beginning April 5th	2030	2031	2032	2033	2034	2035	2036	2037
Profit & loss account:								
Escalation factor applying to unitary charge	1.398	1.416	1.433	1.451	1.469	1.488	1.506	1.525
% of unitary charge calculation	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	50.0%	0.0%
Total service payments by The Highland Council	25,558	25,878	26,201	26,529	26,860	27,196	13,768	0
Of which:								
Part repayment of finance debtor	-9,895	-10,456	-11,049	-11,675	-12,337	0	0	0
Operating income to Project Co from non-D&B services	15,663	15,422	15,152	14,853	14,523	27,196	13,768	0
Property revenue (FM) costs	5,070	5,197	5,326	5,460	5,596	5,736	2,940	0
Life cycle maintenance provision	2,515	2,577	2,642	1,925	796	85	-206	-75
Rates	1,020	1,045	1,071	1,098	1,126	1,154	591	0
Insurance costs	742	760	779	799	819	839	860	0
Annual agency fee for loan monitoring	35	35	36	36	37	37	19	0
Annual costs of SPV administration	699	708	717	726	735	744	377	0
Operating surplus:	5,584	5,099	4,581	4,811	5,416	18,601	9,188	75
Interest earned on positive cash balances	820	849	878	904	964	1,041	1,597	1,211
Interest charges on debt servicing	3,652	3,055	2,417	1,733	1,000	214	0	0
Profit before tax:	2,751	2,893	3,042	3,982	5,380	19,429	10,785	1,287
Corporation tax payable	825	868	913	1,195	1,614	5,829	3,236	386
Profit after tax:	1,926	2,025	2,129	2,788	3,766	13,600	7,550	901
Dividends declared	1,916	2,015	2,119	2,774	3,747	13,532	7,512	896
Retained profits for the year	10	10	11	14	19	68	38	5
Retained profits brought forward	14,374	14,384	14,394	14,405	14,419	14,437	14,505	14,543
Retained profits carried forward:	14,384	14,394	14,405	14,419	14,437	14,505	14,543	14,548
Balance Sheet:								
Non-current asset: contract debtor	45,518	35,062	24,013	12,337	0	0	0	0
Debt Reserve Account	6,517	6,517	6,517	6,517	6,517	6,517	961	-
Cash	12,358	12,988	13,579	14,904	16,619	28,978	25,958	17,459
less: Corporation tax payable	-825	-868	-913	-1,195	-1,614	-5,829	-3,236	-386
Dividends payable	-1,916	-2,015	-2,119	-2,774	-3,747	-13,532	-7,512	-896
Net current assets	9,617	10,105	10,547	10,936	11,258	9,618	15,211	16,177
Total assets :	**61,651**	**51,683**	**41,077**	**29,790**	**17,775**	**16,134**	**16,172**	**16,177**
Financed by:								
Share capital	1,629	1,629	1,629	1,629	1,629	1,629	1,629	1,629
Retained profits	14,384	14,394	14,405	14,419	14,437	14,505	14,543	14,548
Sub-ordinated debt	6,845	5,778	4,578	3,228	1,709	0	0	0
Sub-total, equity:	22,858	21,801	20,612	19,275	17,775	16,134	16,172	16,177
Senior Debt	38,794	29,882	20,466	10,515	0	0	0	0
Total financing:	**61,651**	**51,683**	**41,077**	**29,790**	**17,775**	**16,134**	**16,172**	**16,177**

The Highland Council

A Report on the Risk and Optimism Bias Factors Applying to the Council's Schools PPP2 Project

August 2005

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1 Introduction

1.1 Purpose and basis of the report

The purpose of this report is to assess the risk and Optimism Bias factors that would apply to The Highland Council's proposed Schools' Partnership.

The analysis has been undertaken in accordance with the Treasury Green Book *Appraisal and Evaluation in Central Government* and in particular the Supplementary Guidance contained therein on Optimism Bias.

1.2 Approach and Methodology

Technical Risk Factors

Detailed Technical Risk Appraisals have been undertaken during the procurement to assess the likelihood and impact of cost overruns on design, construction, Life Cycle Maintenance (LCM) and Facilities Management (FM) costs. The analysis and results of these appraisals were set out in two Risk Evaluation Reports, respectively dated May 2004 and September 2004. They were updated in the *Report on the Risk and Optimism Bias Factors Applying to the Council's Schools PPP2 Project* dated April 2005.

The methodology applied to complete the technical risk evaluations involved the following tasks:

1. Preparing a risk matrix identifying each of the risks associated with the delivery of the services, which provided a framework for the evaluation.

2. Mapping this matrix onto Risk Evaluation worksheets that compute the absolute and percentage risk associated with each asset to be procured under the PSC. This mapping exercise ensured that the Risk Evaluation worksheets included all the relevant risks that should be taken into account in the financial model.

3. Assessing each risk specified in the Risk Evaluation worksheets during the workshop. For each identified risk factor, values were sought for the three variables in the formula:

   RV = B V * PV*

   Where:

   RV = the estimated risk value (£)
   B = the unadjusted value of the parameter under consideration (£)
   V = the estimated median financial impact of the risk event were it to occur (expressed as a % of B)

PV = the probability (%) of the risk event occurring.

4. The monetary values estimated by applying the formula to each category of risk were then summed up to derive a single valuation of the risk associated with each major class of asset that would need to be procured to deliver the services as specified in the PSC. These valuations were subsequently fed into the Council's project financial model as percentages of the non-risk adjusted values to arrive at risk-adjusted estimates for the costs of the PSC.

The technical risk evaluation was updated at a workshop held in Inverness on April 27th 2005 attended by the Council's procurement team and its financial advisers, Caledonian Economics Ltd., and subsequently reviewed at a workshop held in Perth on August 9th 2005. The purpose of the review was not to undertake a completely new risk evaluation, but rather to update the earlier 2004 assessment in the light of information received since then, and to confirm that there was no double-counting between the technical risk factors and the allowance for Optimism Bias contained in the financial model, particularly in the light of observations made by the Council's auditors, Audit Scotland, that the combined risk and Optimism Bias adjustment contained in the financial model appeared high in relation to other Scottish Schools PPPs.

Optimism Bias

The primary purpose of the April 27th Workshop and subsequent August 9th workshop was to assess the likely Optimism Bias associated with the Schools Partnership, following the methodology set out in the 2003 edition of the Treasury guidance on *Appraisal and Evaluation in Central Government* (the Green Book). The 2003 Green Book observes that:

"There is a demonstrated, systematic, tendency for project appraisers to be overly optimistic. This is a worldwide phenomenon that affects both the private and public sectors. Many project parameters are affected by optimism – appraisers tend to overstate benefits, and understate timings and costs, both capital and operational."

To redress this tendency, the Green Book requires appraisers to make explicit adjustments for this bias. These adjustments should take the form of increasing estimates of the costs and where appropriate decreasing, and delaying the receipt of, estimated benefits. The Green Book also recommends that sensitivity analysis should be used to test assumptions about operating costs and expected benefits.

The Guidance is set out in Table A1.4, which provides upper (U) and lower (L) bound optimism bias levels for capital expenditure and works duration to be used when carrying out project appraisals. These U and L bound levels should be used for both traditional and privately funded projects, as both types of procurement are considered as alternatives at the Outline Business

Case stage, and therefore require effective risk management to reduce optimism bias.

Table 1.1 (Table A1.4 of the Green Book)
Optimism Bias Factors

Project Type	Optimism Bias (%) [2]			
	Works Duration		CAPEX	
	U	L	U	L
Non-standard Buildings	39	2	51	4
Standard Buildings	4	1	24	2
Non-standard Civil Engineering	25	3	66	6
Standard Civil Engineering	20	1	44	3
Equipment/Development	54	10	200	10
Outsourcing	N/A	N/A	41*	0*

Source: Treasury Guidance

An important point to note is that although various figures for optimism bias are provided by the new Guidance, these should be used only in the case where no local evidence is available. The adjustment for optimism bias is designed to complement and encourage, rather than replace, existing good practice in terms of calculating project specific risk adjustments. In the absence of specific data, Treasury provide a methodology for estimating optimism bias as follows:

- **Step One**: with reference to the Table, decide which type of project to use. For ease of determining project type for a building project, it should be considered "non standard" if it satisfied any of the following conditions: a) it is innovative; b) it has mostly unique characteristics; c) construction involves a high degree of complexity and/or difficulty;

- **Step Two**: always start with the Upper Bound for the relevant project type;

- **Step Three**: consider whether the Optimism Bias factor can be reduced.

- **Step Four**: apply the Optimism Bias factor;

- **Step Five**: Review the Optimism Bias adjustment as the project progresses and as clear and tangible evidence of the success of strategies to mitigate the various contributory factors emerges.

We would assess that the Highland Schools PPP2 Project should be considered as a Standard Building for the purposes of calculating the Optimism Bias. The Upper Bound for a Standard Building project is 24%

according to the guidance. The guidance suggests a methodology that takes a range of ‘contributory factors’, identifies their individual contribution to the optimism bias, and then allocates ‘mitigation factors’ to the individual contributions according to the extent to which they are being managed. These include such factors as contractor capabilities, design complexity, inaccuracies in the business case, poor project intelligence and site characteristics.

Caveats on the Methodology

In applying the Treasury’s Optimism Bias (OB) methodology, the following caveats should be borne in mind:

- Optimism Bias is assessed for a direct procurement option, under which the Council would commission the design for the new schools, tender and supervise the works contract, and accept maintenance risks thereafter. However, the Council has not worked up designs for a direct procurement option beyond concept stage. The effective choice facing the Council in August 2005 is therefore between a notional direct procurement option – the Public Sector Comparator (PSC) – and an alternative PPP option with Alpha Schools, whose design has been worked up in detail and whose costs are being rigorously analysed and negotiated by the Council against established market benchmarks;

- Were the PPP to be cancelled, the view of the Council is that there would be few contractors in the Highland region capable of undertaking a contract of this size under a direct procurement route other than AWG / Morrison and Tulloch Construction – the two main contractors within the Alpha Schools consortium;

- As with any Optimism Bias appraisal, there is inevitably a degree of subjectivity in the assignment of applicable factors, because OB by its nature applies to factors which are inherently uncertain.

Subject to these caveats, the Council and its advisers have sought to provide an objective assessment of plausible levels of optimism bias to be entered into the public-sector comparator, in a form that is transparent and auditable.

The next section of this report sets out the results of the August 9th workshop. Section 3 summarises the rationale behind each score. Section 4 summarises the revised evaluation of the technical risk factors.

2 Results of the Optimism Bias Workshop

As set out in the Supplementary Green Book Guidance on Optimism Bias, optimism with respect to actual outturn costs on a major public sector procurement can arise as a result of several factors, which are classified into five areas for the purposes of the analysis:

- Procurement-related issues, e.g. related to the complexity of the contract structure, contractor capabilities and potential for disputes and claims;

- Project-specific issues, e.g. relating to the complexity and degree of innovation in the design;

- Client-specific issues, of which the most important are the adequacy of the client's Business Case, the number of stakeholders who need to be consulted, and the availability of funding for the project;

- Environmental issues, relating to the impacts of the project on the environment, and the permits and consents required to mitigate them;

- External influences, including political opposition and economic factors.

The August 2005 Workshop assessed each of these areas in turn, and the results are summarised in the Table 2.1 below.

Table 2.1:
Assessed OB Factors for the Highland Schools PPP2 Project, August 2005

		Standard Buildings (1)					
		Wks Dur'n			CapEx		
Contributory factors to Upper Bound Optimism Bias (%)		4	Mitigation Factor		24	Mitigation Factor	
Procurement Stage							
Complexity of Contract Structure	1	1	0.2	0.2	0	0.0	0
Late Contractor Involvement in Design	2	3	1.0	3	2	1.0	2
Poor Contractor Capabilities	3	4	0.5	2	9	0.5	4.5
Government Guidelines	4	0	0.0	0	0	0.0	0
Dispute and Claims Occurred	5	4	0.2	0.8	29	0.5	14.5
Information management	6	0	0.0	0	0	0.0	0
Other (specify)	7	0	0.0	0	0	0.0	0
Project Specific							
Design Complexity	8	3	0.4	1.2	1	0.4	0.4
Degree of Innovation	9	1	0.1	0.1	4	0.4	1.6
Environmental Impact	10	0	0.0	0	0	0.0	0
Other (specify)	11	0	0.0	0	0	0.0	0
Client Specific							
Inadequacy of the Business Case	12	31	0.5	15.5	34	1.0	34
Large Number of Stakeholders	13	6	0.1	0.6	0	0.0	0
Funding Availability	14	8	0.1	0.8	0	0.0	0
Project Management Team	15	0	0.0	0	1	0.5	0.5
Poor Project Intelligence	16	6	0.7	4.2	2	0.7	1.4
Other (specify)	17	0	0.0	0	1	0.0	0
Environment							
Public Relations	18	8	0.5	4	2	0.5	1
Site Characteristics	19	5	0.2	1	2	0.2	0.4
Permits / Consents / Approvals	20	9	0.1	0.9	0	0.0	0
Other (specify)	21	0	0.0	0	0	0.0	0
External Influences							
Political	22	0	0.0	0	0	0.0	0
Economic	23	0	0.0	0	11	0.3	3.3
Legislation / Regulations	24	9	0.2	1.8	3	0.4	1.2
Technology	25	0	0.0	0	0	0.0	0
Other (specify)	26	0	0.0	0	0	0.0	0
					101		64.8
Upper Limit Duration OB %				4.00			
Amount by which Duration OB should be reduced (% of UL)				36.10			
Resultant Duration OB %				2.56			
Lower Limit Duration OB %				1.00			
Amount of Duration OB to be applied to Financial Model				**2.56**			
Upper Limit Capex OB %				24.00			
Amount by which Capex OB should be reduced (% of UL)				64.80			
Resultant Capex OB %				8.45			
Lower Limit Capex OB %				2.00			
Amount of Capex OB to be applied to Financial Model				**8.45**			

Source: Optimism Bias Workshop, August 9th 2005

In summary, the Workshop concluded that the Optimism Bias factor that should be applied to Works Duration should be 2.56%, and to capital expenditure 8.45%, compared to 13.39% estimated in April 2005.

After discussion with Audit Scotland it was agreed that the Treasury Lower Limit values of 2% and 1% should be applied in the model as the Capital and Duration optimism bias factors.

In the next section, the rationale behind the scores given to each factor is set out.

3 Rationale behind the OB Factors

For ease of reference, the rationale behind each of the OB factors given in Section 2 of this report is given in tabular form, with the structure of the Table following the format of the Table given in the Supplementary Green Book Guidance on Optimism Bias, as follows:

- The rows are classified according to the contributory factors to OB as specified in the Guidance, distinguishing between procurement-related, project-specific, client-specific, environmental and external influences;

- The columns distinguish between Works Duration and Capital Expenditure.

		Works Duration	Capital Expenditure
Procurement Stage			
1.	***Complexity***	If the Highland schools procurement were to be implemented under a direct Council contract, the Council would need to use the Major Contract Form, for the first time. This would apply to the Secondaries even if the procurement was divided into separate contracts, although the Council has greater experience of managing contracts of the scale of the Primaries. OB mitigation factor on works duration = 0.2.	The use of an unfamiliar contract form, for a scale of procurement well above the maximum for previous Council procurements, means that the OB factor with respect to capital expenditure arising from contractual complexity has not been mitigated at all. OB mitigation factor on capex = 0.0.
2.	***Late Contractor Involvement in Design***	Under traditional procurement, the Council would retain design responsibility, and there would be no requirement for contractor involvement. OB mitigation factor on works duration = 1.0.	As for works duration. OB mitigation factor on capex = 1.0.
3.	***Poor 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. There are currently very real resource constraints on contractor capacity in the Highlands, and realistically very few contractors would have capacity to tender for a contract of this size. Under PPP they take the risk of time overruns because of resource constraints; under a traditional procurement the Council would be directly exposed to skills shortages. OB mitigation factor on works duration = 0.5.	As for works duration, this source of OB is estimated to be only 50% mitigated. There is a risk that lack of contractor capacity and skills shortages in the construction industry could generate high tender prices in a conventional procurement. OB mitigation factor on capex = 0.5.

		Works Duration	Capital Expenditure
4.	N/A		
5.	***Disputes & Claims Occurred***	The possibility of disputes and claims was regarded as a real possibility under a direct procurement, which could only partially mitigated for following reasons: • the design function would have to be contracted out, at least for the larger Secondaries, because of the limitations on the Council's in-house resources; • there is evidence that external design practices are overstretched; • therefore there would be a risk of face high risk of delays in implementation. OB mitigation factor on works duration = 0.2.	Taking account of the Council's likely reliance on an external design and supervisory team in a traditional procurement, which would almost certainly be located outside the Highlands, there would be an ongoing risk that design and structural engineering information could be received late, and / or not clearly communicated to the works contractors, giving rise to the potential for disputes & claims during implementation. If a traditional procurement were progressed, the Council could consider buying the Keppie designs for the new schools, which would mitigate the uncertainties relating to disputes and claims as they have been worked up in detail. OB mitigation factor on capex = 0.5.
Project Specific			
1.	***Design Complexity***	The design of the schools is not inherently complex, but there are potential difficulties in fitting these designs into the existing sites. In particular, at Dingwall and Kinlochleven, schools would need to be built on existing sites with children present; in Portree, the school will be built in a residential area; and in several schools there are issues around ground conditions (see below). OB mitigation factor on works duration = 0.4.	The same issues around the design would apply as for works duration, and have only partially been mitigated by surveys, as the PSC design has not been worked up beyond concept stage. OB mitigation factor on capex = 0.4.
2.	***Degree of innovation***	The innovation connected to the project relates specifically to site conditions. While condition surveys have been completed, the Council has done nothing to mitigate the innovation risk with regard to the site conditions, having not worked up a detailed design for schools and package. OB mitigation factor on works	Since April, neighbour issues with respect to the sites have been dealt with, and detailed plans developed, although there are still uncertainties with respect to site characteristics. OB mitigation factor on capex = 0.4.

		Works Duration	Capital Expenditure
		duration = 0.1.	
Client Specific			
1.	***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, financing within the Prudential Borrowing regime. To prepare a Business Case for a traditional procurement would have a considerable unknown impact on works duration, which would only be partially mitigated by the work done on the PPP procurement to date. OB mitigation factor on works duration = 0.5.	Under a direct procurement, the scope of the schools programme and specification of each of the schools in the programme would need to be revisited, but on the assumption that the Council would take over the Keppie designs, the Business Case risk has now been completely mitigated, with the appraisal of options completed, the scope of the schools package fully defined, sites identified and planning consents secured. OB mitigation factor on capex = 1.0.
2.	***Large number of stakeholders***	A particular factor within the Highlands. Although the statutory consultation process has been completed for the PPP, there would need to be an extensive consultation in the event that a PPP procurement was halted and a direct procurement alternative re-initiated, leading to delays. OB mitigation factor on works duration = 0.1.	N/A
3.	***Funding Availability***	This risk has been mitigated under the PPP alternative, but in the event that a direct procurement alternative was recommenced, there would be delays: • firstly, there is lack of available funding in the form of prudential borrowing capacity; • secondly, abandonment of the PPP could give rise to a political debate over the allocation of direct Council funding. OB mitigation factor on works duration = 0.1.	N/A
4.	***Project Management Team***	NA	The Highland Council team is unique in Scotland in being the only local authority team with substantially the same personnel in place for PPP2 as for PPP1. However, it cannot be assumed that the project

		Works Duration	Capital Expenditure
			team would be the same for a conventional procurement, and the skills requirements would be slightly different for a conventional procurement than for a PPP. OB mitigation factor on capex = 0.5.
5.	***Poor Project Intelligence***	Is being managed through site investigations and existing conditions surveys, although there are no ground condition surveys of existing schools. Some outstanding issues remain with SEPA, although agreement is close, & Scottish Water approvals may need to be sought. OB mitigation factor on works duration = 0.7.	As for works duration. OB mitigation factor on capex = 0.7.
6.	***Other client specific***	N/A	N/A
Environment			
1.	***Public Relations***	The Council has only undertaken limited public consultation for the project, as under the PPP responsibility for PR and communications has transferred to Alpha Schools as prospective partner. Therefore PR would be required in the event that the PPP was abandoned and a direct procurement option was preferred, with potentially some impact on works duration and capex. OB mitigation factor on works duration = 0.5.	As for works duration. OB mitigation factor on capex = 0.5.
2.	***Site Characteristics***	Potentially difficult in that the larger Secondaries are within residential areas (Portree, Milburn and Dingwall), & little has been done to mitigate site specific risks, although archaeological surveys have commenced. A further uncertainty relates to the transportation of heavy equipment and materials over narrow Highland roads. OB mitigation factor on works duration = 0.2.	As for works duration. OB mitigation factor on capex = 0.2.
3.	***Permits, Consents &***	While planning approval is being pursued for the schools in PPP	N/A

		Works Duration	Capital Expenditure
	approvals	package, there would be the risk that these would not apply should a direct procurement alternative be initiated, as the Council would need to prepare new designs, and potentially re-examine the schools within the package. OB mitigation factor on works duration = 0.1.	
External Influences			
1.	***Economic***	N/A	The Council has no control over external economic factors, such as interest and inflation rates. If implementation were delayed, there is a risk of construction costs escalating more rapidly than anticipated, particularly as a switch to conventional procurement could realistically be expected to delay implementation by at least two years. However, as the project approaches financial close the uncertainties relating to future inflation and interest rate movements are diminishing, although fluctuations in the BCIS construction price indices indicate continuing uncertainties in future trends in tender prices. OB mitigation factor on capex = 0.3.
2.	***Legislation / regulations***	This risk has only partly been mitigated. New building and planning regulations, e.g. with regard to sustainability, have been taken into account in the development of the PPP project to date, but would need to be revisited if the PPP procurement were cancelled in favour of a direct procurement. OB mitigation factor on works duration = 0.2.	Since April, the OB mitigation factor on capex with regard to regulatory risk has increased to reflect the fact that the design proposals have now secured planning consent. OB mitigation factor on capex = 0.4.

Conclusions

The general point emerging from the Risk and OB Workshops was that, if the PPP procurement were abandoned, it could not be assumed that the same project would proceed on the same timetable. On the contrary, the most likely scenario is that project implementation would be considerably delayed by the need for extensive consultation and political debate over the scope, design and affordability of a conventionally procured schools package. Direct Council and stakeholder involvement in detailed schools design issues are being avoided through the PPP route, as responsibility for designing schools to meet the Council's functional educational requirements has transferred to the private sector partner.

4 The Technical Risk Evaluation Revisited

4.1 Scope of the evaluation

The September 2004 technical risk evaluation was updated in April and August 2005 to take account of the latest intelligence on risk factors, and the findings of the OB Workshop, to confirm that there is no double-counting in the financial model.

4.2 Design and Construction Phase Changes since September 2004

The principal changes in risk factors that have occurred since September 2004 are as follows:

Design Phase

1. *Fitness for purpose*. Emerging evidence from PPP1 indicates that this risk may have been underestimated. Costs have been incurred by the PPP1 Project Co to meet remediation costs to address issues such as playing fields not fit for purpose; inadequate dust extraction in technical rooms within two Secondaries; an inadequate supervisors' office; leaking roofs; and inadequate acoustics in two Primary School halls.

2. *Detailed planning*. In April 2005, there was a planning risk associated with the three large Secondaries which form the core of the PPP2 procurement. The planning risk has since been mitigated by progress since then, although there remains the risk of a Judicial Review, and there is a risk of cost consequences in meeting the planning conditions. Overall, the probability of significant cost implications arising as a result of planning requirements is assessed as having fallen from 50% in April to 20% in August 2005, with the expected value of costs being 2.5% of the estimated base cost.

3. *Council errors/modifications*. The risk associated with this aspect has reduced since 2004 as the Council has developed and tightened the output specification during the procurement process. Therefore the probability of this risk arising was assessed as having reduced from 95% to 50%.

4. *Fees*. If the PPP procurement were abandoned, the Council would face the risk of having to meet increased design fee costs, as the most likely scenario would be that it would enter into negotiations with Alpha’s architects, Keppie, to acquire their plans for the new schools. Based on the Fife precedent, where there was a change in the Preferred Bidder late in the procurement process, the fee cost of this option could be considerable. The August 2005 workshop assessed that there was a one-in-twenty (5%) risk of this scenario occurring, and, if it did, it could add

10% to the overall cost of the project – being an estimate of the professional design and supervision fees that would cystallise.

Construction Phase

1. *Difficult ground conditions* potentially apply to half the schools within the PPP package, as follows:

    - Portree: bedrock near the surface on site may impact on the construction programme;

    - Kinlochleven: may need groundwater pumps to prepare the site for development;

    - Dingwall: tidal influences – the site contains alluvial clay, so piling may be required;

    - Cullicudden: bedrock near the surface and the depth of topsoil is unknown;

    - Cawdor: bedrock near the surface and the depth of topsoil is unknown;

    - Milburn: tidal influences – the site contains alluvial clay, so piling may be required.

2. *Council errors/modifications*. The risk associated with this aspect has fallen since 2004, as Council has developed and tightened the output specification during the procurement process. Therefore the probability of this risk arising was assessed as having reduced from 95% to 20%.

3. *Durability/latent defects*. Recent evidence has emerged from the Eden Court Theatre, where a failure in brickwork costed the Council £1.5 million to remediate, even though the failure was due to proven design and construction faults when the Theatre was built 30 years ago. This suggests that the risk factors associated with construction quality failures should be adjusted slightly upwards compared to the September estimate, particularly given the site conditions highlighted under (1) above which give rise to a risk of settlement and cracks in schools buildings.

4. *Protestor action / vandalism/ costs and delays*. A specific risk has arisen since 2004 with respect to the Dingwall Academy, where a protest group is objecting to the development of a new school on the Academy's existing playing fields. The August 2005 workshop assessed a 40% probability of this risk crystalling, and, if it did so, it could add a third to the construction cost of the Dingwall Academy. This reflects the fact that the alternative to a new building on the playing fields would be to

decant the entire school to temporary premises, then demolish and replace the existing Academy on its current site.

5. *Receivership default, costs and delays*. Recent experience of construction contracts in Scotland suggests that this remains a risk. In the event that a contractor went into default, the reality is that there might be a very limited market of alternative contractors whom the Council could retain to complete the works. This is recognised by Alpha and more particularly their funders, who are asking for an amendment to the liquid market provisions of the SSSC to secure greater protection in the event of default. The August 2005 assessment was that the valuation of this risk is approximately £5.15 million, or 4% of the base value of the project, reflecting the costs of delays in finding an alternative contractor, and the premium any alternative contractor would be likely to charge, in an environment where the Highland construction industry is likely to be operating close to full capacity.

6. *Insurance risk.* The risk of significant insurance cost overruns is now reduced, as the cost estimate is based on a firm insurance quote. In addition, under the new drafting for risk sharing under the SSSC, this risk is likely to be shared between the Council and Project Co.

7. *Inflation risk*. This risk remains, with construction escalation ahead of retail price inflation, and the actual experience of contracts in implementation in Highland suggesting that delays in construction can have a considerable impact on outturn costs of projects.

The revised estimates of design and construction risks are given in Table 4.1.

Table 4.1:
Revised estimates of design and construction risks

	A	D	E	F	G	H
2	**August 9, 2005**					
3	New Build Capital Costs (£M)			**18.03%**		
4						
5						
6			*Expected*	*Probability*	*Base*	*Risk*
7	**Design phase risks**		*Value %*	*%*	*Value*	*Value*
8	Fit for purpose		2%	10%	£129	£0.26
9	Planning consent - outline		0%	0%	£129	£0.00
10	Planning consent - detailed		2.5%	20%	£129	£0.64
11	Programme delays/time overruns incl cost to education		1.5%	20%	£129	£0.39
12	Errors / modifications / resolutions incl fees		2%	50%	£129	£1.29
13	Fees		10%	5%	£129	£0.64
14						
15	**Construction phase risks impacting on timescales**					
16	Land acquisition - cost & availability		0%	0%	£129	£0.00
17	Costs - archaeological & ecological discoveries		0.57%	75%	£129	£0.55
18	Costs - difficult ground conditions		7.5%	50%	£129	£4.83
19	Delays & unexpected site conditions incl weather		0.60%	33%	£129	£0.26
20						
21	**Construction phase risks impacting on quality**					
22	Spec probs due to poor Proj Mgt, comms with contractor		0%	0%	£129	£0.00
23	Reworking (during construction) due to council changes, lack of info, late info		3%	20%	£129	£0.77
24	Latent defects in existing assets, unforeseen works		5%	5%	£129	£0.32
25	Productivity/delays on site /site safety: construction costs (contractors cost)		5%	10%	£129	£0.64
26			0%	0%	£129	£0.00
27	Durability / obsolescence / latent defects during operation		5%	5%	£129	£0.32
28						
29	**Construction management & third party risks**					
30	Third party action		0%	0%	£129	£0.00
31	Industrial action affecting supply		0%	0%	£129	£0.00
32	Protestor action / vandalism / costs & delays		8%	40%	£129	£3.86
33	Statutory undertakings / costs & delays		1%	25%	£129	£0.32
34	Receivership/default / costs & delays		20%	20%	£129	£5.15
35	Insurance cover		1%	50%	£129	£0.64
36	Construction inflation risk		4%	45%	£129	£2.32
37						
38					**Total value of risks:**	**£23.22**
39					**Risk value as a % of base cost:**	**18.0%**

Source: Risk and Optimism Bias Workshop, Inverness, April 27th 2005

4.3 Operational Phase Changes since September 2004

Only minor changes have occurred in the operational phase since September 2004, with the key changes being:

- A reduction in the general change in law risk, reflecting the lapse of time and greater information now available on likely changes in law over the forthcoming five years;
- the risk of financial default by a sub-contractor on the FM contract has been reduced to reflect the Council's view that the interface between the FM and construction arms of the AWG / Morrison Alpha consortium is tighter than between Gleesons and MITIE on PPP1;
- conversely, the risk of unitary charge deductions has increased slightly in the light of the Council's actual experience on PPP1;

- a risk factor has been assigned to the possibility of cost overruns on water and utilities;

- the risk factor applying to operational insurance has been reduced, reflecting the greater robustness of current insurance cost estimates, and the risk-sharing formula applying to insurance embodied in the draft changes to the SSSC.

Taking all these changes into account, VFM risk factor is now assessed as 14.88% on the FM element of the costs, as shown in Table 4.2.

Table 4.2:
Revised estimates of FM and LCM risks

August 9, 2005				
Operating Phase				
Operating Costs New Build	£ m-2			
Grounds Maintenance	0.53			
Repairs & Maintenance	6.31			
Rates	0			
Water & Utilities	7.93			
Cleaning	9.5			
Janitorial Services	5.26			
FM Management	3.68			
January 0, 1900	0			
Life Cycle Maintenance	24.17			
Total	57.38			
New Build '000m2	64,344.00		14.88%	
	Expected Value %	*Probability %*	*Base Value*	*Risk Value*
General legislative changes to SPV incl tax chgs	8%	100%	**£3,692,059**	£295,364.70
Grounds Maintenance	10%	5%	*£34,102*	£170.51
Repairs & Maintenance	10%	5%	*£406,011*	£2,030.05
Rates	0%	0%	£0	£0.00
Water & Utilities	1%	5%	*£510,248*	£255.12
Cleaning	12%	12%	*£611,268*	£8,802.26
Janitorial Services	10%	10%	*£338,449*	£3,384.49
FM Management	10%	10%	*£236,786*	£2,367.86
0	0%	0%	£0	£0.00
Life Cycle Maintenance	5%	20%	*£1,555,194*	£15,551.94
Insurance (property, employer, 3rd pty, fire, flood storm)	2%	100%	***£3,692,059***	£73,841.17
Additional op costs due to poor design (incl pitches)	5%	25%	**£3,692,059**	£46,150.73
Financial default by sub-contractor	10%	10%	**£3,692,059**	£36,920.59
Additional 3rd party claims, TUPE, employee	3%	25%	**£3,692,059**	£27,690.44
	0%	0%	£0	£0.00
UC deductions to due availability & performance penalties	5%	20%	**£3,692,059**	£36,920.59
Total operating FM and LC cost		check	£3,692,059	
		check	£3,692,059	
			Total value of Operating risks:	**£549,450**
			k value as a % of base operating cost:	**14.88%**

Source: Risk and Optimism Bias Workshop, Inverness, April 27th 2005 and Perth, August 9th 2005

Appendix: Workshop Participants

Attendees at the April 2005 Optimism Bias Workshop

Dr Alister Coutts:	Highland Council Project Director
Sandy Young:	Highland Council Property Department
Michael Fraser:	Highland Council Finance Department
Alan Simpson:	Highland Council Legal Department
Ken Allan:	Highland Council Education Department
Martin Finnigan:	Caledonian Economics – facilitator
Michael Nevin:	Caledonian Economics

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Hugh Fraser:	Highland Council Education Department
Martin Finnigan:	Caledonian Economics – facilitator
Michael Nevin:	Caledonian Economics
Evelyn McDowall:	Turner Townsend Project Management

PSC

construction starts 05/06		yr		2006/2007	2007/2008	2008/2009	2009/2010	2010/2011	2011/2012	2012/2013	2013/2014	2014/2015	2015/2016	2016/2017	2017/2018	2018/2019	2019/2020	2020/2021	2021/2022
		mid	01/04/06	30/09/06	30/09/07	30/09/08	30/09/09	30/09/10	30/09/11	30/09/12	30/09/13	30/09/14	30/09/15	30/09/16	30/09/17	30/09/18	30/09/19	30/09/20	30/09/21
		XNPV	0	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
Base capital		**0**	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Base Capital (nominal)		**125,600**	0	43,546	54,501	36,699	2,191	0	0	0	0	0	0	0	0	0	0	0	0
Construction Cost Risk	**18.03%**	**22,646**	0	7,851	9,826	6,617	395	0	0	0	0	0	0	0	0	0	0	0	0
		148,246	0	51,397	64,327	43,316	2,586	0	0	0	0	0	0	0	0	0	0	0	0
check npvs up and across		TRUE																	
		148,246	0	51,397	64,327	43,316	2,586	0	0	0	0	0	0	0	0	0	0	0	0
optimism bias		**4,447**	0	1,542	1,930	1,299	78	0	0	0	0	0	0	0	0	0	0	0	0
Captial per model		**152,694**	0	52,939	66,257	44,615	2,664	0	0	0	0	0	0	0	0	0	0	0	0
check npvs up and across		TRUE																	
FM		**44,853**	0.00	0.00	316.04	588.98	2,626.10	3,093.97	3,171.32	3,250.60	3,331.87	3,415.17	3,500.54	3,588.06	3,677.76	3,769.70	3,863.95	3,960.55	4,059.56
Rates		**9,021**	0.00	0.00	63.56	118.46	528.17	622.27	637.83	653.78	670.12	686.87	704.05	721.65	739.69	758.18	777.14	796.56	816.48
Admin		**2,939**	0.00	256.25	262.66	269.22	275.95	147.08	150.76	154.53	158.39	162.35	166.41	170.57	174.84	179.21	183.69	188.28	192.99
Insurance		**7,148**	0.00	256.25	262.66	269.22	275.95	452.56	463.88	475.47	487.36	499.55	512.03	524.83	537.96	551.40	565.19	579.32	593.80
		63,961	0.00	512.50	904.91	1,245.88	3,706.18	4,315.89	4,423.79	4,534.38	4,647.74	4,763.94	4,883.04	5,005.11	5,130.24	5,258.50	5,389.96	5,524.71	5,662.82
check npvs up and across		TRUE																	
Risk adjustment per CE excl rates		**8,175**	0.00	76.26	125.19	167.76	472.89	549.61	563.35	577.43	591.87	606.67	621.83	637.38	653.31	669.65	686.39	703.55	721.14
OB adjustment		**1,546**	0.00	0.00	10.89	20.30	90.51	106.63	109.30	112.03	114.83	117.70	120.64	123.66	126.75	129.92	133.17	136.50	139.91
FM etc Risk and OB adjusted		**73,682**	0.00	588.76	1,041.00	1,433.94	4,269.58	4,972.13	5,096.44	5,223.85	5,354.44	5,488.30	5,625.51	5,766.15	5,910.30	6,058.06	6,209.51	6,364.75	6,523.87
LCM unadjusted		**23,904**	0.00	0	168	314	1,400	1,649	1,690	1,732	1,776	1,820	1,866	1,912	1,960	2,009	2,059	2,111	2,164
LCM risk adjustment		**3,557**	0	0	25.06222411	46.70687221	208.2542664	245.3570381	251.490964	257.7782381	264.2226941	270.8282614	277.5989679	284.5389421	291.6524157	298.9437261	306.4173192	314.0777522	321.929696
LCM Provision Risk adjusted		**27,461**	0.00	0.00	193.49	360.60	1,607.81	1,894.26	1,941.62	1,990.16	2,039.91	2,090.91	2,143.18	2,196.76	2,251.68	2,307.97	2,365.67	2,424.82	2,485.44
check npvs up and across		TRUE																	
LCM Optimism Bias		**549**	0.00	0	4	7	32	38	39	40	41	42	43	44	45	46	47	48	50
		101,692	0.00	588.76	1,238.36	1,801.75	5,909.55	6,904.28	7,076.89	7,253.81	7,435.15	7,621.03	7,811.56	8,006.85	8,207.02	8,412.20	8,622.50	8,838.06	9,059.01
check npvs up and across		TRUE																	

NPV without Risk Adjustment	**213,465**
Tax adjustment	**10,673**
NPV of Risk and OB adjustments	**40,920**
Total Risk Adjusted NPV of PSC	**265,058**

		01-Apr-06	31-Jul-07	31-Jan-08	31-Jul-08	31-Jan-09	31-Jul-09	31-Jan-10	31-Jul-10	31-Jan-11	31-Jul-11	31-Jan-12	31-Jul-12	31-Jan-13	31-Jul-13	31-Jan-14	31-Jul-14	31-Jan-15
			0	*1*	*2*	*3*	*4*	*5*	*6*	*7*	*8*	*9*	*10*	*11*	*12*	*13*	*14*	*15*
Unadjusted cashflows (from Contract debtors e74) (120206 **model**)	620,803,649	0	662,833	1,550,385	2,950,663	7,705,131	8,831,203	9,157,263	9,230,521	9,267,150	9,341,287	9,378,356	9,453,383	9,490,896	9,566,823	9,604,787	9,681,625	9,720,044

NPV of UC Payment Stream	**246,723,136**

Value for money margin	(%)	7.43%
	(£k)	18,335

2022/2023	2023/2024	2024/2025	2025/2026	2026/2027	2027/2028	2028/2029	2029/2030	2030/2031	2031/2032	2032/2033	2033/2034	2034/2035	2035/2036	2036/2037	2037/2038	2038/2039	2039/2040	2040/2041	2041/2042	2042/2043	2043/2044
30/09/22	30/09/23	30/09/24	30/09/25	30/09/26	30/09/27	30/09/28	30/09/29	30/09/30	30/09/31	30/09/32	30/09/33	30/09/34	30/09/35	30/09/36	30/09/37	30/09/38	30/09/39	30/09/40	30/09/41	30/09/42	30/09/43
17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	34	35	36	37	38
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
4,161.05	4,265.07	4,371.70	4,480.99	4,593.02	4,707.84	4,825.54	4,946.18	5,069.83	5,196.58	5,326.49	5,459.66	5,596.15	5,736.05	2,939.73	0	0	0	0	0	0	0
836.89	857.81	879.26	901.24	923.77	946.86	970.54	994.80	1,019.67	1,045.16	1,071.29	1,098.07	1,125.52	1,153.66	591.25	0	0	0	0	0	0	0
197.81	202.76	207.82	213.02	218.35	223.80	229.40	235.13	241.01	247.04	253.21	259.54	266.03	272.68	139.75	0	0	0	0	0	0	0
608.65	623.86	639.46	655.45	671.83	688.63	705.84	723.49	741.58	760.12	779.12	798.60	818.56	839.03	860.00	0	0	0	0	0	0	0
5,804.40	5,949.51	6,098.24	6,250.70	6,406.97	6,567.14	6,731.32	6,899.60	7,072.09	7,248.89	7,430.12	7,615.87	7,806.27	8,001.42	4,530.73	0	0	0	0	0	0	0
739.16	757.64	776.59	796.00	815.90	836.30	857.20	878.63	900.60	923.12	946.19	969.85	994.09	1018.95	586.19	0	0	0	0	0	0	0
143.41	146.99	150.67	154.43	158.29	162.25	166.31	170.47	174.73	179.09	183.57	188.16	192.87	197.69	101.31	0	0	0	0	0	0	0
6,686.97	6,854.14	7,025.49	7,201.13	7,381.16	7,565.69	7,754.83	7,948.70	8,147.42	8,351.10	8,559.88	8,773.88	8,993.23	9,218.06	5,218.24	0	0	0	0	0	0	0
2,218	2,273	2,330	2,388	2,448	2,509	2,572	2,636	2,702	2,769	2,839	2,910	2,982	3,057	1,567	0	0	0	0	0	0	0
329.9779384	338.2273869	346.6830716	355.3501484	364.2339021	373.3397496	382.6732434	392.2400744	402.0460763	412.0972282	422.3996589	432.9596504	443.7836416	454.8782327	233.1250943	0	0	0	0	0	0	0
2,547.57	2,611.26	2,676.54	2,743.46	2,812.04	2,882.34	2,954.40	3,028.26	3,103.97	3,181.57	3,261.11	3,342.63	3,426.20	3,511.86	1,799.83	0.00	0.00	0.00	0.00	0.00	0.00	0.00
51	52	54	55	56	58	59	61	62	64	65	67	69	70	36	0.00	0.00	0.00	0.00	0.00	0.00	0.00
9,285.49	9,517.63	9,755.57	9,999.46	10,249.44	10,505.68	10,768.32	11,037.53	11,313.47	11,596.30	11,886.21	12,183.37	12,487.95	12,800.15	7,054.06	0.00	0.00	0.00	0.00	0.00	0.00	0.00

31-Jul-15	31-Jan-16	31-Jul-16	31-Jan-17	31-Jul-17	31-Jan-18	31-Jul-18	31-Jan-19	31-Jul-19	31-Jan-20	31-Jul-20	31-Jan-21	31-Jul-21	31-Jan-22	31-Jul-22	31-Jan-23	31-Jul-23	31-Jan-24	31-Jul-24	31-Jan-25	31-Jul-25	31-Jan-26	31-Jul-26	31-Jan-27	31-Jul-27
16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	34	35	36	37	38	39	40
9,797,805	9,836,685	9,915,378	9,954,725	10,034,363	10,074,182	10,154,775	10,195,072	10,276,633	10,317,413	10,399,952	10,441,222	10,524,752	10,566,517	10,651,049	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######

31-Jan-28	31-Jul-28	31-Jan-29	31-Jul-29	31-Jan-30	31-Jul-30	31-Jan-31	31-Jul-31	31-Jan-32	31-Jul-32	31-Jan-33	31-Jul-33	31-Jan-34	31-Jul-34	31-Jan-35	31-Jul-35	31-Jan-36	31-Jul-36	31-Jan-37	31-Jul-37
41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60
#######	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######	#######

PSC

		yr		2006/2007	2007/2008	2008/2009	2009/2010	2010/2011	2011/2012	2012/2013	2013/2014	2014/2015	2015/2016	2016/2017	2017/2018	2018/2019	2019/2020	2020/2021	2021/2022
		mid	01/04/06	30/09/06	30/09/07	30/09/08	30/09/09	30/09/10	30/09/11	30/09/12	30/09/13	30/09/14	30/09/15	30/09/16	30/09/17	30/09/18	30/09/19	30/09/20	30/09/21
		XNPV	0	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
Base capital		**0**	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Base Capital (nominal)		**125,600**	0	43,546	54,501	36,699	2,191	0	0	0	0	0	0	0	0	0	0	0	0
Construction Cost Risk	**18.03%**	**22,646**	0	7,851	9,826	6,617	395	0	0	0	0	0	0	0	0	0	0	0	0
		148,246	0	51,397	64,327	43,316	2,586	0	0	0	0	0	0	0	0	0	0	0	0
check npvs up and across		TRUE																	
		148,246	0	51,397	64,327	43,316	2,586	0	0	0	0	0	0	0	0	0	0	0	0
optimism bias		**4,447**	0	1,542	1,930	1,299	78	0	0	0	0	0	0	0	0	0	0	0	0
Captial per model		**152,694**	0	52,939	66,257	44,615	2,664	0	0	0	0	0	0	0	0	0	0	0	0
check npvs up and across		TRUE																	
FM		**44,853**	0.00	0.00	316.04	588.98	2,626.10	3,093.97	3,171.32	3,250.60	3,331.87	3,415.17	3,500.54	3,588.06	3,677.76	3,769.70	3,863.95	3,960.55	4,059.56
Rates		**9,021**	0.00	0.00	63.56	118.46	528.17	622.27	637.83	653.78	670.12	686.87	704.05	721.65	739.69	758.18	777.14	796.56	816.48
Admin		**2,939**	0.00	256.25	262.66	269.22	275.95	147.08	150.76	154.53	158.39	162.35	166.41	170.57	174.84	179.21	183.69	188.28	192.99
Insurance		**7,148**	0.00	256.25	262.66	269.22	275.95	452.56	463.88	475.47	487.36	499.55	512.03	524.83	537.96	551.40	565.19	579.32	593.80
		63,961	0.00	512.50	904.91	1,245.88	3,706.18	4,315.89	4,423.79	4,534.38	4,647.74	4,763.94	4,883.04	5,005.11	5,130.24	5,258.50	5,389.96	5,524.71	5,662.82
check npvs up and across		TRUE																	
Risk adjustment per CE excl rates		**8,175**	0.00	76.26	125.19	167.76	472.89	549.61	563.35	577.43	591.87	606.67	621.83	637.38	653.31	669.65	686.39	703.55	721.14
OB adjustment		**1,546**	0.00	0.00	10.89	20.30	90.51	106.63	109.30	112.03	114.83	117.70	120.64	123.66	126.75	129.92	133.17	136.50	139.91
FM etc Risk and OB adjusted		**73,682**	0.00	588.76	1,041.00	1,433.94	4,269.58	4,972.13	5,096.44	5,223.85	5,354.44	5,488.30	5,625.51	5,766.15	5,910.30	6,058.06	6,209.51	6,364.75	6,523.87
LCM unadjusted		**23,904**	0.00	0	168	314	1,400	1,649	1,690	1,732	1,776	1,820	1,866	1,912	1,960	2,009	2,059	2,111	2,164
LCM risk adjustment		**3,557**	0	0	25.06222411	46.70687221	208.2542664	245.3570381	251.490964	257.7782381	264.2226941	270.8282614	277.5989679	284.5389421	291.6524157	298.9437261	306.4173192	314.0777522	321.929696
LCM Provision Risk adjusted		**27,461**	0.00	0.00	193.49	360.60	1,607.81	1,894.26	1,941.62	1,990.16	2,039.91	2,090.91	2,143.18	2,196.76	2,251.68	2,307.97	2,365.67	2,424.82	2,485.44
check npvs up and across		TRUE																	
LCM Optimism Bias		**549**	0.00	0	4	7	32	38	39	40	41	42	43	44	45	46	47	48	50
		101,692	0.00	588.76	1,238.36	1,801.75	5,909.55	6,904.28	7,076.89	7,253.81	7,435.15	7,621.03	7,811.56	8,006.85	8,207.02	8,412.20	8,622.50	8,838.06	9,059.01
check npvs up and across		TRUE																	

NPV without Risk Adjustment	**213,465**
Tax adjustment	**10,673**
NPV of Risk and OB adjustments	**40,920**
Total Risk Adjusted NPV of PSC	**265,058**

		01-Apr-06	31-Jul-07	31-Jan-08	31-Jul-08	31-Jan-09	31-Jul-09	31-Jan-10	31-Jul-10	31-Jan-11	31-Jul-11	31-Jan-12	31-Jul-12	31-Jan-13	31-Jul-13	31-Jan-14	31-Jul-14	31-Jan-15
			0	***1***	***2***	***3***	***4***	***5***	***6***	***7***	***8***	***9***	***10***	***11***	***12***	***13***	***14***	***15***
Unadjusted cashflows (from Contract debtors e74) (120206 **model**)	620,803,649	0	662,833	1,550,385	2,950,663	7,705,131	8,831,203	9,157,263	9,230,521	9,267,150	9,341,287	9,378,356	9,453,383	9,490,896	9,566,823	9,604,787	9,681,625	9,720,044

NPV of UC Payment Stream	**246,723,136**

Value for money margin	(%)	7.43%
	(£k)	18,335

2022/2023	2023/2024	2024/2025	2025/2026	2026/2027	2027/2028	2028/2029	2029/2030	2030/2031	2031/2032	2032/2033	2033/2034	2034/2035	2035/2036	2036/2037	2037/2038	2038/2039	2039/2040	2040/2041	2041/2042	2042/2043	2043/2044
30/09/22	30/09/23	30/09/24	30/09/25	30/09/26	30/09/27	30/09/28	30/09/29	30/09/30	30/09/31	30/09/32	30/09/33	30/09/34	30/09/35	30/09/36	30/09/37	30/09/38	30/09/39	30/09/40	30/09/41	30/09/42	30/09/43
17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	34	35	36	37	38
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
4,161.05	4,265.07	4,371.70	4,480.99	4,593.02	4,707.84	4,825.54	4,946.18	5,069.83	5,196.58	5,326.49	5,459.66	5,596.15	5,736.05	2,939.73	0	0	0	0	0	0	0
836.89	857.81	879.26	901.24	923.77	946.86	970.54	994.80	1,019.67	1,045.16	1,071.29	1,098.07	1,125.52	1,153.66	591.25	0	0	0	0	0	0	0
197.81	202.76	207.82	213.02	218.35	223.80	229.40	235.13	241.01	247.04	253.21	259.54	266.03	272.68	139.75	0	0	0	0	0	0	0
608.65	623.86	639.46	655.45	671.83	688.63	705.84	723.49	741.58	760.12	779.12	798.60	818.56	839.03	860.00	0	0	0	0	0	0	0
5,804.40	5,949.51	6,098.24	6,250.70	6,406.97	6,567.14	6,731.32	6,899.60	7,072.09	7,248.89	7,430.12	7,615.87	7,806.27	8,001.42	4,530.73	0	0	0	0	0	0	0
739.16	757.64	776.59	796.00	815.90	836.30	857.20	878.63	900.60	923.12	946.19	969.85	994.09	1018.95	586.19	0	0	0	0	0	0	0
143.41	146.99	150.67	154.43	158.29	162.25	166.31	170.47	174.73	179.09	183.57	188.16	192.87	197.69	101.31	0	0	0	0	0	0	0
6,686.97	6,854.14	7,025.49	7,201.13	7,381.16	7,565.69	7,754.83	7,948.70	8,147.42	8,351.10	8,559.88	8,773.88	8,993.23	9,218.06	5,218.24	0	0	0	0	0	0	0
2,218	2,273	2,330	2,388	2,448	2,509	2,572	2,636	2,702	2,769	2,839	2,910	2,982	3,057	1,567	0	0	0	0	0	0	0
329.9779384	338.2273869	346.6830716	355.3501484	364.2339021	373.3397496	382.6732434	392.2400744	402.0460763	412.0972282	422.3996589	432.9596504	443.7836416	454.8782327	233.1250943	0	0	0	0	0	0	0
2,547.57	2,611.26	2,676.54	2,743.46	2,812.04	2,882.34	2,954.40	3,028.26	3,103.97	3,181.57	3,261.11	3,342.63	3,426.20	3,511.86	1,799.83	0.00	0.00	0.00	0.00	0.00	0.00	0.00
51	52	54	55	56	58	59	61	62	64	65	67	69	70	36	0.00	0.00	0.00	0.00	0.00	0.00	0.00
9,285.49	9,517.63	9,755.57	9,999.46	10,249.44	10,505.68	10,768.32	11,037.53	11,313.47	11,596.30	11,886.21	12,183.37	12,487.95	12,800.15	7,054.06	0.00	0.00	0.00	0.00	0.00	0.00	0.00

31-Jul-15	31-Jan-16	31-Jul-16	31-Jan-17	31-Jul-17	31-Jan-18	31-Jul-18	31-Jan-19	31-Jul-19	31-Jan-20	31-Jul-20	31-Jan-21	31-Jul-21	31-Jan-22	31-Jul-22	31-Jan-23	31-Jul-23	31-Jan-24	31-Jul-24	31-Jan-25	31-Jul-25	31-Jan-26	31-Jul-26
16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	34	35	36	37	38
9,797,805	9,836,685	9,915,378	9,954,725	10,034,363	10,074,182	10,154,775	10,195,072	10,276,633	10,317,413	10,399,952	10,441,222	10,524,752	10,566,517	10,651,049	#######	#######	#######	#######	#######	#######	#######	#######

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7 October 2005

Mr Alan Geddes
Director of Finance
The Highland Council
Glen Urquhart Road
Inverness
IV3 5NX

Dear Alan

Schools PPP2 Project
Final Judgment on Proposed Accounting Treatment

In response to the request from the Director of Property & Architectural Services & PPP Projects Director, dated 28 September 2005, for my comments on the final judgement on the accounting treatment of the Schools PPP2 project, I include my comments on its reasonableness and summarise the context in which they are given.

Responsibilities of the audited body and the external auditor

The Highland Council is accountable to the public for the stewardship of funds under its control. It is for the body alone to take decisions about the most appropriate accounting treatment for any transactions it is considering entering into, after taking whatever advice it deems necessary.

It is the external auditor's role to form an independent view on how the body has discharged its stewardship of public funds. It is not part of the auditor's role to provide accounting advice or to act as an accounting advisor. The public sector audit regime requires that auditors should not, nor appear to, compromise their independence.

Audit Scotland's Code of Audit Practice sets out clearly the nature of public sector audit and the general duties of external auditors operating under that audit regime. The Statement of Responsibilities of Auditors and of Audited Bodies provides further clarification of the respective roles of both parties.

The Treasury Taskforce Technical Note 1 (revised) - 'How to Account for PFI Transactions' (TTF 1) summarises the relative responsibilities of the purchaser and auditor and recommends that the following outputs are obtained at progressive stages of the procurement process.

Audited body	Auditor
Provides an **initial view** on the proposed accounting treatment based on Outline Business Case information.	Comments on whether the purchaser's initial view on the proposed accounting treatment is reasonable.
Updates initial view to provide a **provisional judgment** on the proposed accounting treatment based on the design solution/financial models of the preferred bidder.	Comments on whether the purchaser's provisional judgment on the proposed accounting treatment is reasonable.
Provides a **final judgment** on the accounting treatment by weighing up all the relevant indicators of which party has an asset of the property.	Comments on whether the purchaser's final judgment on the accounting treatment is reasonable.

Status of audit view

The purpose of this letter is to provide The Highland Council with my comments on the reasonableness of the final judgment on the accounting treatment of the project from the perspective of the external auditor. The views are expressed in my capacity as external auditor and should not be regarded as advice. The letter is provided to inform you of my views at this stage as external auditor and for no other purpose. In particular, no responsibility is accepted towards any other organisation or individual who may seek to place reliance on its contents.

Changing circumstances

The views set out in this letter are based upon the information presented to me as at 30 September 2005 in the documents listed in the annex. If circumstances change, or further information becomes available, then my views may have to be reconsidered.

The financial advisor indicates that the financial model, used as a basis of the analysis, has yet to be agreed by the Council and its advisors. However, the financial advisor does not expect any subsequent changes to alter the conclusions reached by them on the accounting treatment.

The views are also expressed in recognition of the current underlying guidance which is Application Note F to FRS 5-Reporting the substance of transactions: Private Finance Initiative and similar contracts (which provides clarification of how the principles and requirements of FRS 5 should apply to transactions conducted under the UK Government's Private Finance Initiative), as supplemented by Treasury Taskforce Technical Note No. 1 (Revised)-How to Account for PFI Transactions.

Comments on reasonableness of final view on accounting treatment

In your capacity as Director of Finance, you have confirmed to me that your final judgement on the accounting treatment is that the transaction should be accounted for as off The Highland Council's balance sheet.

The identification and evaluation of the key risks by the Council's officers and professional advisors is based on their technical analysis, and their subjective judgements on the likelihood of various events occurring. The quantitative analysis is substantially based on the contractor's financial model.

The Council appointed Caledonian Economics Ltd as its financial advisor in respect of this scheme. As part of their remit, they have provided the body with advice on whether the transaction should be accounted for as on or off the Council's balance sheet. Caledonian Economic's draft audit opinion (Pre-financial close version), dated 27 September 2005, is that the transaction should be accounted for as off the Council's balance sheet. This is supported by their qualitative analysis and their analysis of quantitative risks, which allocates 54% of identified risk to the provider and 46% to the purchaser (The Highland Council).

I note their conclusions and comment as follows:

Separability

I concur with the assessment of the separable elements of the property identified in the financial advisor's report. In the report, cleaning services and insurance costs are considered separable due to the potential for renegotiation due to benchmarking, and business rates costs are considered separable as any increases are passed directly to the Council (pass-through cost). In addition, I note that advisor has treated utility costs as separable in the financial analysis, although this is not reflected in the advisor's report.

Advisor's quantified analysis of risks

The total quantum of risk identified by the financial advisor (£6.2 million) is consistent with our modelled total of £5.6 million.

The financial advisor identifies the relative share of the risks being borne by each party (at 90% confidence limits) as:

- ♦ Contractor £3.4 million (54%); and
- ♦ Council £2.9 million (46%).

My conclusion from modelling the contract is that the contractor bears a risk of £2.84 million and the risk borne by the Council is £2.78 million (51% vs. 49%). The outcome of the quantified assessment is tight, but the contractor bears the majority risk.

I do not have any adverse comment on the advisor's quantified analysis or modelling methodology

Demand risk

Application Note F to FRS 5 makes clear that demand risk, where significant, will normally give the clearest evidence of who should record an asset of the property. The Council does not consider this to be a significant risk given the locations of the schools and the fact they have been designed to accommodate the forecast demand within the area.

The Council estimates that demand can by accurately predicted for Dingwall Academy on the basis of known birth rates until 2019/2020. Thereafter the increasing uncertainty in the spread of forecast demand is based on whether existing levels of house building in the Inner Moray Firth area continues or ceases. The Council have estimated the potential variation in demand until 2033/2034. This represents substantially the term of the PPP contract. The cost of each pupil place, for the purposes of quantifying demand risk, is approximately £5,000 (per annum NPV) based on the unitary charge and the number of pupils.

The potential variation in demand for Dingwall Academy and Millburn Academy is considered, by the Council, to be similar and as these two schools represent 60% of the PPP2 school roll. This analysis is expected to reasonably reflect the proportionate demand risk in the project as a whole.
Some of the schools within the project occupy a significant position within the local community they serve, being the only education establishments with alternatives being impractically distant. This fact

tends to assure their continued use for the foreseeable future (while education of primary and secondary age children continues to depend on their physical presence at a local property).

Residual value risk

The financial advisor has modelled residual value risk on the basis of the eventual value varying between 1.27 and 1.40 times that expected, based on cost and remaining useful life. This is based on an analysis of the 30-year movement in historic building price index movement since 1971. It is noted that the residual value calculation used by the financial advisor is based on a life of the PPP2 properties of 60 years.

Unavailability deductions

Unavailability and performance deduction estimates, contained within the financial advisor's report are that performance deductions are likely to be more extensive in the first operational year and then, for the remainder of the contract, deductions will vary between 0.5% and 2.1%. This is based on The Highland Council's experience of deductions in the existing PP1 schools' contract.

Third party revenues

The advisor has noted that "third party revenue opportunities tend to be limited and operator Alpha Schools have not included any third party revenue within their financial model". These are not considered as significant in this analysis.

Design risk

Modelling of design risk generally includes two main components. The first of these is related to initial design failures, for example when temperature ranges cannot be maintained due to unplanned solar gains or inadequate insulation or heating provision. These are considered as resulting in one-off rectification costs and will probably arise early in the concession period. The second element is due to variations in the volume and extent of maintenance and lifecycle costs throughout the contract.

If design leads to higher volumes of maintenance in year 1, then it is likely that this will be reproduced in later years unless additional expenditure is used to redesign the factor resulting in higher costs. If higher volumes are due to under/over estimates in the initial model then this too is likely to recur throughout the contract.

The financial advisor's modelling takes into account the cost of initial design failures and ongoing maintenance volumes as it uses the capital and lifecycle maintenance costs as a basis for evaluating the risk.

Potential changes in costs

This risk represents where costs incurred by the contractor in delivering the agreed outcomes are greater (or less) than the general inflation estimates used. The advisor has modelled this on the basis of BCIS building cost indexation movements relative to RPI, based on data from 1970 onwards.

Risk of obsolescence

The advisor has indicated that "within a schools PPP, this risk is considered low compared to projects such as IT systems". The advisor has therefore not quantified this risk.

Qualitative indicators

In addition to the quantified analysis of risk, I have considered the following qualitative indicators:

- Termination for operator default;
- Nature of the operator’s financing; and
- Who determines the nature of the property

The assessment of these issues contained within the financial advisor’s accounting opinion appears to be appropriate.

Symmetrical accounting treatment

Where a purchaser adopts an off balance sheet treatment of a PPP asset, there is persuasive evidence of the appropriateness of this approach if the contractor, conversely, recognises the asset on its balance sheet. The provider’s financial model indicates that it intends to include a contract debtor on its balance sheet. It is, of course, for the provider to determine its own accounting treatment in conjunction with its auditors, however, the occurrence of “off/off” balance sheet treatments has been a source of concern for public sector auditors considering PPP and related arrangements, particularly where this may derive from the purchaser and provider having different perceptions of the allocation of risk.

I am concerned that the asset is not likely to appear on either public or private sector balance sheets, as a fixed asset. I accept that future changes in International Accounting Standards may address the accounting treatment for PFI projects, resulting in most Scottish PFI contracts appearing on public sector balance sheets.

Overall conclusion

In my view, and in the context of my preceding remarks:

- the process followed to determine whether the body should account for the transaction on or off its balance sheet was in accordance with the current underlying guidance; and
- your final judgment on the accounting treatment is reasonable subject to my reservations covering the tight outcome of the quantitative analysis and the potential for fixed assets not to be recognised on either the balance sheet of the purchaser or the contractor.

The proposed project is a major development for The Highland Council and I will continue to take an interest as part of the audit process.

Yours sincerely

G Stevenson

Gavin Stevenson
Director of Audit (Local Government)

cc Dr Alister Coutts, Director of Property & Architectural Services

ANNEX

Nature of document	Prepared by	Date
Project Agreement Highland Council Schools PPP 2: Pb Draft 7 23/09/05	MacRoberts	23 September 2005
Review of Accounting Treatment for Highland Council Schools PPP2 Pre financial close version	Caledonian Economics Ltd	27 September 2005
Accounting Analysis_190905	Caledonian Economics Ltd	19 September 2005
Preferred Bidders Financial Model [Copy of Model submitted to THC 26 Sep 2005.xls]	Grant Thornton	26 September 2005
Dingwall values no housing post 2020.xls	Fujitsu Services	September 2005
Dingwall values to 2034 with housing.xls	Fujitsu Services	September 2005

HIGHLAND SCHOOLS PPP2 PROJECT AGREEMENT

TABLE OF AMENDMENTS

The following table identifies changes to the proposed Highland Council Project Agreement version 11 dated 3 February 2006 recently submitted to the Scottish Executive (**the PA**), namely those clauses in which amendments have been made (and changes to Clause 1.1 definitions), compared to the previous draft submitted to the Scottish Executive (draft version 9 dated 25 November).

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
1.1	**Definitions**				
	Additional Rights	**Additional Rights** means the rights set out in Section B of Schedule Part 16;	New definition inserted for incorporation of the provisions of Schedule Part 16 which the Parties have agreed should apply in relation to certain Site and School-specific matters (access during construction period etc.)	Accept that these are project specific, but council must not dilute normal responsibilities expected of contractor.	
	Affiliate	**Affiliate** means : (i) in relation to any person, any holding company or subsidiary of that person or any subsidiary of such holding company and "holding company" and "subsidiary" shall have the meaning given to them in section 736 of the Companies Act 1985; (ii) in relation to Northern Infrastructure Investments LLP (or any successor thereto), any unit trust, investment fund, partnership, other fund or entity of which Northern Infrastructure Investments LLP (or its successor) is either the general partner, trustee or principal manager (directly or indirectly); and ; and	Definition changed to reflect project specific requirements of one of the Shareholder's (Northern Infrastructure Investments LLP) legal status as a limited liability partnership rather than a limited company	Accepted as project specific on basis of council's legal advice. Possible typo of repeated "and" at end of limb (ii)?	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		(iii) partners or limited partners in Northern Infrastructure Investments LLP (or its successor) or any partnership referred to in paragraph (ii) of this definition, but only to the extent that such partners become holders of shares as a result of a transfer in specie to them which is a distribution on winding up out of the assets of the partnership (or limited liability partnership) in question;			
	Ambac	~~**Ambac** means [•][4];~~ **Ambac** has the meaning given in the Master Definitions Schedule;	Correction of cross-reference	Acceptable	
	Ambac Bond Guarantee	**Ambac Bond Guarantee** has the meaning given to "Bond Guarantee" in the Master Definitions Schedule	Correction of cross-reference	Acceptable	
	Ancillary Rights	**Ancillary Rights** means the [Additional Rights] and (a) a non exclusive~~,~~ right to enter and remain on each of the Project Facilities ~~and~~, (b) rights to connect into all utilities and services located in the Project Facilities and to use, maintain, repair and renew all such utilities and services, (c) during the Works Period only the right to occupy the areas shown coloured blue on the Phasing Drawings on an exclusive basis during the period shown on the	Reflects Additional Rights (see comment above in relation to Additional Rights, and below in relation to Clause 8.1) and extent of access rights. Reference to the Execution Date is subject to final agreement in relation to the point in time at which property searches are to be obtained.	Accept project specific approach, but see comments above on 'Additional rights'. This drafting tightens definition of which areas of the sites that it can occupy exclusively/non-exclusively (SSSC is "non-exclusive right to enter and remain"). Council to check composite tax treatment?	This definition has now been finally agreed as set out in the following row:

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		relevant Phasing Drawing. (d) during the Works Period only the right to occupy the areas shown coloured red on the Phasing Drawings on a non-exclusive basis during the period shown on the relevant Phasing Drawing. in each case to the extent required only for the purpose of implementing the Works, performing the Services and fulfilling the Contractor's rights and obligations under this Agreement [but only insofar as such right is capable of being granted by the Authority ~~and provided that during the Works Period such rights granted in paragraphs (a) and (b) may only be exercised over the areas shown [ ] on the [Phasing Plans] on the dates corresponding to the relevant areas as detailed [on the Phasing Plans/a table to be agreed].~~as at the Execution Date];			
	Final agreed drafting -17 03 06	**Ancillary Rights** means the ~~[~~Additional Rights~~]~~ and (a) a non exclusive right to enter and remain on each of the Project Facilities with effect from the Service Availability Date (other than in respect of the External Works including the Grass Playing Fields) and/or the External			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Works Availability Date (in respect of the areas forming the External Works and/or the Grass Playing Fields), as appropriate, (b) rights to connect into all utilities and services located in the Project Facilities and to use, maintain, repair and renew all such utilities and services, (c) during the Works Period only the right to occupy the areas shown coloured blue on the Phasing Drawings on an exclusive basis during the period shown on the relevant Phasing Drawing, and (d) during the Works Period only the right to occupy the areas shown coloured red on the Phasing Drawings on a non-			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		exclusive basis during the period shown on the relevant Phasing Drawing. in each case to the extent required only for the purpose of implementing the Works, performing the Services and fulfilling the Contractor's rights and obligations under this Agreement ~~[~~but, save as provided in Section B of Schedule Part 16, only insofar as such right is capable of being granted by the Authority as at the ~~Execution Date]~~date to which the searches referred to in Section A of Schedule Part 16 are brought down;			
	Applicable Standards	means any generally recognised industry or service standard or code of practice (including British and European Standards and Codes of Practice) which relates to services of a type similar to the Services or to goods, equipment or materials required in the provision of the Services or to works of a similar nature as the Works but specifically excluding ~~[excluded matters to be agreed following discussions on~~the standards and codes which it is stated in the Authority's Requirements~~– **Alpha to provide list for agreement**] which the parties have agreed~~ shall not apply to the Works and/or the Services;	Reflects agreed position now reached on this issue (which was previously advised) that the agreed list of exclusions is to be set out expressly under Authority's Requirements	Acceptable	
	Base Senior Debt	…*(Force Majeure Compensation)* and 47 *(Compensation on Termination for Corrupt*	Reflects amendments to funding documentation	To be updated per agreement on instalments	….”any amounts which are payable in

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
	Termination Amount	*Gifts and Fraud and Breach of Refinancing*) [Condition 9(~~c)(i)(C)]~~[11]e), at sub-paragraph (3) of the definition of "Spens Acceleration Event"][4] or [Condition 9(~~c)(ii)~~e), at paragraph (iii) of the definition of "Default Amount"] of the Bonds (as the case may be) or for the purposes of Clause 46 *(Compensation on Termination for Authority Default/Voluntary Termination by the Authority)*, ~~Conditions 9(c)(i)(A) and 9(c)(i)(B)~~[Condition 9(e), at sub-paragraphs (1) and (2) of the definition of "Spens Acceleration Event"]		on contractor default / no re-tendering	respect of the Bonds and in respect of Permitted Borrowings calculated in accordance with~~, for the purposes of Clauses 44 (Force Majeure Compensation) and 47 (Compensation on Termination for Corrupt Gifts and Fraud and Breach of Refinancing) [Condition 9(c)(i)(C)]~~[11] ~~or Condition 9(c)(ii) of the Bonds (as the case may be) or for the purposes of Clause 46 (Compensation on Termination for Authority Default/Voluntary Termination by the Authority), Conditions 9(c)(i)(A) and 9(c)(i)(B~~ the definition of "Default Amount" at Condition 9(e) of the Bonds,…."
	Building Sub-Contractor	**Building Sub-Contractor** means a principal sub-contractor appointed by the Building Contractor to undertake (i) the building of the whole ~~or a material part~~ of any single New Project Facility ~~as listed in the Contractor's Proposals~~or (ii) works to a value in excess of £10,000,000 in connection with the Works;	The Parties have agreed this definition of Building Sub-Contractor by reference to and based on the terms of the Contractor's Proposals	What contract provision(s) cover building works below £10M?	
	CDT Equipment	**CDT Equipment** means the Portree CDT Equipment, the Dingwall CDT Equipment, the Millburn CDT Equipment and the Kinlochleven CDT Equipment all as defined in Schedule Part 22;	New definition required as part of the Authority's Requirements	Acceptable	
	Certificate of Service Availability	means a certificate stating the satisfaction in relation to a New Project Facility (excluding the External Works and/or the Grass Playing	Amendment to reflect the agreed position on Phasing in relation to Construction, Availability and	Acceptable	

~~11~~4 Note: Subject to discussion between Alpha/THC and SE. Note cross references to the terms and conditions of the Bonds will need to be updated to reflect the outcome of Contractor Default discussions and final form Bond T&Cs.

~~11 Note: Subject to discussion between Alpha/THC.~~

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Fields as appropriate) of the Service Availability Requirements in the form as set out in Schedule Part 20 Section A *(Certificate of Service Availability)*;	Certificates (see below in relation to Clause 21)		
	Certificate of External Works Availability	[**Certificate of External Works Availability** means a certificate stating the satisfaction in relation to a New Project Facility (excluding the Grass Playing Fields) of any External Works Availability Requirements for that New Project Facility in the form as set out in Schedule Part 20 Section B *(Certificate of External Works Availability)*;]	Amendment to reflect the agreed position on Phasing in relation to Construction, Availability and Certificates (see below in relation to Clause 21)	Acceptable	
	Change of Control	**Change of Control** means (other than in respect of transfers to Affiliates ~~or to any of~~ ~~[●] **[Note: list of acceptable group companies to be completed by Alpha]**~~of any Shareholder) the change in the direct or indirect legal or beneficial ownership of more than [~~●~~50%][18] of the issued share capital or (if it is convertible into shares), of the loan capital of the Contractor and/or the HoldCo;	Reflects agreed position in relation to Alpha's shareholding structure	Acceptable	
	Cleaning	**Cleaning** means the cleaning services provided by the Contractor identified in Section [B.5.8] of the Operational Services Specification.	Definition cross-refers to the Operational Services Specification for the purposes of benchmarking and market testing provisions in Clause 28.	Acceptable	
	Committed Standby Facility	~~**Committed Standby Facility** means [ ];~~[21]	Deleted as not required – there is to be no Committed Standby Facility under the funding arrangements for the Project	Acceptable	
	Contingent Funding Liabilities	**Contingent Funding Liabilities** means any contingent ~~liability~~liabilities of the Shareholders ~~and the Issuer~~ in respect of financial obligations owed to the Contractor and/or Senior Lenders under the Funding	Reflects position under funding and subcontract documentation. New drafting at end of Clause is clarificatory and reflects standard form principles	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Agreements in relation to the Project which are triggered as a result of or in relation to the termination of this Agreement, including (without limitation) guarantees or letters of credit in respect of deferred equity or Loan Note Commitments (as defined in the Equity Subscription Agreement)[23] but excluding any guarantees or letters of credit issued in support of sub-contractors' obligations under the relevant sub-contracts;			
	Credit	**Credit** has the meaning given to it in the EIB Loan Agreement;	Reflects position under funding documentation	Acceptable	
	Culbokie Primary School	**Culbokie Primary School** means the New Project Facility numbered [●] in Section B of Schedule Part 4 (*New Project Facilities*);	New definition required for Clause 22A	Acceptable	
	Culbokie Application	**Culbokie Application** means the application for detailed planning permission in respect of Culbokie Primary School submitted to The Highland Council Department of Development on [●] 2005 under reference number [●]; **[Note: MCSL to confirm details]**	New definition required for Clause 22A	Accepted as project specific.	
	Curricular Equipment List	~~**Curricular Equipment List** means, in respect of a New Project Facility, a list of equipment to be specified by the Authority, and to be installed prior to the Service Availability Date, such list to be delivered to the Contractor not less than 6 months before the Target Service Availability Date, or such later date as may be estimated from time to time for the obtaining of the Certificate of Service Availability in the Construction~~	Deleted as not required	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		~~Programme;~~			
	Date of Possession	**Date of Possession** means, in respect of each Phasing Drawing, the dates set out in Schedule Part 23; **[Drafting note: This definition will be used on the Phasing Drawings.]**	Definition required for construction Phasing provisions	Accepted as project specific	
	Dingwall Academy	**Dingwall Academy** means the New Project Facility numbered [●] in Section B of Schedule Part 4 (*New Project Facilities*);	New definition required for Clause 22A	Acceptable	
	Dingwall Permission	**Dingwall Permission** means the detailed planning permission number [●] issued by the [Planning Department] of The Highland Council on [●] 2005 in respect of Dingwall Academy; **[Note: MCSL to confirm details]**	New definition required for Clause 22A	Accepted as project specific	
	Disclosed Data	(b) the ITN dated ~~19 December 2003~~February 2004 and associated amendments and clarifications issued by or on behalf of the Authority to the Contractor; (c) all information in the Data Room at the Execution Date under exception of ~~Warranted Data~~the information contained in Schedule Part 12 (*Employment Cost Data*);	Definition conformed to position in relation to Disclosed Data and cross-reference corrected	Acceptable	
	Distribution Account	~~**Distribution Account** has the meaning given in the Master Definition Schedule~~	Deleted as duplication of definition	Acceptable	
	Educational Functionality	~~(e) the location and relationship of equipment, furniture and fittings~~	Limb (e) will be re-inserted if THC receive sufficient information from MCSL as to the location and relationship of equipment, furniture and fittings.	Expect to see limb (e) re-inserted	Alpha accept that the design has not been sufficiently developed to allow THC to provide this confirmation - 17 03 06

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
	Equity Subscription Agreement	**Equity Subscription Agreement** means the ~~agreement~~Funding Agreement with that name dated on or around the Execution Date and entered into by [~~Noble Fund Managers], Morrison Education (Highland) Limited, the Contractor, and HoldCo, in respect of the subscription for loan notes in HoldCo and the Contractor,~~●] as amended or varied from time to time in accordance with the provisions of this Agreement	Reflects position under funding documentation	Acceptable	
	Estimated Change in Project Costs	(a) in the case of works to be undertaken at a Project Facility, (i) prior to the Service Availability Date or relevant External Works Availability Date (where the works relate to the External Works other than the Grass Playing Fields) or the relevant Grass Playing Fields Availability Date (where the works relate to the Grass Playing Fields) for that Project Facility; or	Definition amended as required for construction Phasing provisions	Acceptable	
	External Works	[**External Works** ~~means~~has the ~~Works specified in [Section [●] of the Contractor's Proposals~~meaning given to that term in Section A of Schedule Part 5 (*Service Availability Requirements*)];	Cross-reference corrected	Acceptable	
	External Works Availability Date	**External Works Availability Date** means, in relation to External Works (other than the Grass Playing Fields) at a New Project Facility the date of issue of an Acceptance Certificate in respect of such External Works (other than the Grass Playing Fields) or the	Definition amended for construction Phasing provisions	Acceptable as project specific	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		date determined as the date on which External Works Availability occurred in relation to such External Works (other than the Grass Playing Fields) under the Dispute Resolution Procedure;			
	Growing Month	**Growing Month** means each and all of April, May, June, July, August, and/or September;	Reflects the Parties' agreed position on Phasing in relation to Construction and landscaping of grassed areas (with reference to Growing Months reflecting practicalities of completion with regard to the seasonal nature of turfing)	Acceptable as project specific	
	Helpdesk	**Helpdesk** means the helpdesk facilities established by the Contractor pursuant to the Operational Services Specification and as defined in Part 1 of Section A of Schedule Part 7 *(Payment Mechanism)*;		Acceptable	
	Judicial Review	"**Judicial Review**" means judicial review under Chapter 58 of the Rules of the Court of Session or any statutory challenge or appeal against the Authority or the Scottish Executive which proceeds on principles similar to judicial review, which concerns the legality of any grant of planning permission.	Definition moved from Clause 22A	Acceptable	
	Master Definitions Schedule	**Master Definitions Schedule** means the document of that name~~, dated on or about the Execution Date [a copy of which is contained within Appendix [•] of this Agreement];~~[39] in the Agreed Form;	Reflects use of Agreed Form documentation	Acceptable	
	Original	(a) the ~~[~~gross Bond proceeds~~]~~	Conforms to funding	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
	Senior Commitment	excluding the proceeds of the Variation Bonds to be raised under the Senior Funding Agreements; and (b) the amount committed under the Senior Funding Agreements other than the ~~[~~gross Bond proceeds~~]~~ and the proceeds of the Variation Bonds, being the Credit from EIB ~~loan~~,~~[40]~~[12]	documentation. The reference to "gross Bond proceeds" is intended to include amounts that are raised from the Bond issue and immediately used to fund fees and expenses. However it should be clear that this excludes the proceeds of the Variation Bonds (since the treatment of the Variation Bonds is that they are sold to RBC and immediately re-purchased by the Issuer).		
	Permitted Borrowing	**Permitted Borrowing** means, without double counting, any:[13] (a) advance to the Contractor under the Senior Funding Agreements ~~[, provided that such advance is not made under any Committed Standby Facility]~~; (b) Additional Permitted Borrowing; (c) ~~an advance to the Contractor under the Committed Stand-by Facility which is made solely for the purpose of funding any cost overruns, increased expenses or loss of revenue which the~~	Conforms to funding documentation. There is no Committed Standby Facility.	Acceptable	

[12] Note: Subject to review of bond documentation.
[13] Note: subject to review of bond documentation.

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		~~Contractor incurs, provided that such funds are not used in substitution for other sources of committed funding designated for those purposes~~not used; and			
	Phasing Drawings	**Phasing Drawings** means [●];	New definition required to reflect the Parties agreed position on Phasing in relation to Construction	Acceptable as project specific	
	Portree High School	**Portree High School** means the New Project Facility ~~identified as such~~numbered [●] in Section B of Schedule Part 4 (*New Project Facilities*);	Cross-reference completed	Acceptable	
	Portree Permission	**"Portree Permission"** means the detailed planning permission number [●] issued by the [Planning Department] of The Highland Council on [●] 2005 in respect of Portree High School; ***[MCSL to confirm details]***	New definition required for Clause 22A	Acceptable as project specific	
	Qualifying Bank Transaction	pursuant to Council Directive ~~2001~~2000/12/EC	Statutory reference corrected	Acceptable	
	Qualifying Institution (b)	(ii) any institution which is recognised or permitted under the law of any member state of the EEA to carry on the business of a credit institution pursuant to Council Directive ~~2001~~2000/12/EC relating to the taking up and pursuit of the business of credit institutions or which is otherwise permitted to accept deposits in the United Kingdom or any other EEA member state	Statutory reference corrected	Acceptable	
	Reimbursement and Indemnity Agreement	~~[~~**Reimbursement and Indemnity Agreement** has the meaning given in the Master Definitions Schedule~~]~~;	Square brackets removed	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
	Relevant Judicial Review	**Relevant Judicial Review** means Judicial Review which has not arisen on the grounds of failure by the Contractor or any Contractor Related Party to comply with statutory procedure or on the grounds of commission of any unlawful act or acts by the Contractor or any Contractor Related Party;	New definition required for Clause 22A to reflect requirements of FPU in relation to judicial review as a result of acts of the Contractor not giving rise to any relief for the Contractor.	Acceptable	
	Relief Event	~~[~~(h) an application for Relevant Judicial Review ~~of the relevant detailed planning permission~~in relation to the Dingwall Permission and/or the Portree Permission made within the period of three months from the Effective Date including, without prejudice to the foregoing generality, the issue of a decision revoking, quashing or withdrawing a planning permission following such an application for Judicial Review,~~]~~ ~~**[Note: to be updated following commercial agreement and FPU sign off – Alpha to revert.]**~~	Amendment to limb of definition required for Clause 22A to reflect requirements of FPU in relation to judicial review as a result of acts of the Contractor not giving rise to any relief for the Contractor, and to further restrict the scope of comfort being provided to the Contractor in respect of the two specific project facilities where there is an identified concern in relation to judicial review.	Acceptable	
	Reserved Rights	**Reserved Rights** means (1) ~~the~~ rights of pedestrian and vehicular access to and egress ~~from land~~(provided that during the Works Period this is to the extent practicable given the stage of the Works at the relevant time and without the Contractor requiring to incur additional costs) from land currently in the ownership of the Authority adjoining the Sites of Millburn Academy, Portree High School, Drummond Special School and Kinlochleven Campus along ~~the routes shown [~~, in the case of Millburn Academy, Portree High School and Kinlochleven Campus such reasonable route designated by the Contractor from time to time and in	Development of definition required to reflect more fully detailed Works, access and land arrangements and to allow the Council to ensure continuity of access to certain areas in the vicinity of certain of the Sites.	Acceptable as project specific and at council's risk	Note that final terms of the Reserved Rights have now been agreed as set out in the row below: 17 03 06

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		the case of Drummond Special Schools, along the route shown hatched ~~in~~ black~~]~~ on the relative Site ~~Plans;~~Plan and (2) the rights of the owner, tenants and occupiers of the area of ground shown ~~[~~outlined in blue~~]~~ on the Site Plan of Portree High School, currently known as Elgin Hostel, to park six cars in the car parking spaces ~~included~~existing from time to time in the area ~~shown [hatched in black] on the relative Site Plan~~surrounding Elgin Hostel and (3) any public rights of way over the Sites; **[Drafting note: We understand that the Site plan for Portree currently shows the Site as a whole and the Elgin Hostel outlined in red. Can Mark Garland please arrange for this to amended so that the Elgin Hostel is outlined in blue. The definition of the Portree Site will also have to amended to refer to the area outlined in red with the exception of the area outlined in blue. Same applies to the Pavillion at Millburn Academy]**			
	Final agreed drafting -17 03 06	**Reserved Rights** means (1) rights of pedestrian and (save in respect of (c) below) vehicular access ~~to and egress (provided that during the Works Period this is to the extent practicable given the stage of the Works at the relevant time and without the Contractor requiring to incur additional costs) from land currently in the ownership of the Authority adjoining the Sites of Millburn Academy, Portree High School,~~and egress over the Site of (a) Millburn Academy by the Authority or Authority Related Parties to the area shown			As above.

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		edged in blue on the Millburn Academy Site Plan (b) Portree High School to the area shown edged in blue on the Portree High School Site Plan (c) Drummond Special School ~~and Kinlochleven Campus along, in the case of Millburn Academy, Portree High School and Kinlochleven Campus~~for the purpose of access to and egress from adjoining land currently owned by Authority (such access to be pedestrian only during the Works Period) and (d) Kinlochleven Campus by the Authority or Authority Related Parties to the land adjoining the River Leven for the purposes of carrying out works on or to the same as authorised by the Authority along such reasonable route designated by the Contractor from time to time and ~~in the case of Drummond Special Schools, along the route shown hatched black on the relative Site Plan and~~ (2) the rights of the owner, tenants and occupiers of the area of ground shown outlined in blue on the Site Plan of Portree High School, currently known as Elgin Hostel, to park six cars in the car parking spaces existing from time to time in the area surrounding Elgin Hostel and (3) ~~any~~the existing public ~~rights~~right of way exercisable over the ~~Sites; **[Drafting note: We understand that the Site plan for Portree currently shows the Site as a whole and the Elgin Hostel outlined in red. Can Mark**~~			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		~~Garland please arrange for this to amended so that the Elgin Hostel is outlined in blue. The definition of the Portree Site will also have to amended to refer to the area outlined in red with the exception of the area outlined in blue. Same applies to the Pavillion at Millburn Academy]~~Site of Portree High School;			
	Revised Senior Debt Termination Amount (c)	*(Force Majeure Compensation)* and 47 (*Compensation on Termination for Corrupt Gifts and Fraud and breach of Refinancing*) [Condition 9(~~c)(i)(C)]~~[43]e), at sub-paragraph (3) of the definition of "Spens Acceleration Event"][15] or [Condition 9(~~c)(ii)~~e), at paragraph (iii) of the definition of "Default Amount"] of the Bonds (as the case may be) or for the purposes of Clause 46 *(Compensation on Termination for Authority Default/Voluntary Termination by the Authority)*, ~~Conditions 9(c)(i)(A) and 9(c)(i)(B)~~[Condition 9(e) at sub-paragraphs (1) and (2) of the definition of "Spens Acceleration Event"] of the Bonds	Reflects amendments to funding documentation.	To be revised post instalments agreement MacRoberts to confirm impact of SOPC3 update taken account of (where it refers to this definition)	"…any amounts which are payable in respect of the Bonds and in respect of Permitted Borrowings calculated in accordance with~~, for the purposes of Clauses 44 *(Force Majeure Compensation)* and 47 *(Compensation on Termination for Corrupt Gifts and Fraud and breach of Refinancing)* [Condition 9(c)(i)(C)]~~[43] ~~or Condition 9(c)(ii) of the Bonds (as the case may be) or for the purposes of Clause 46 *(Compensation on Termination for Authority Default/Voluntary Termination by the Authority)*, Conditions 9(c)(i)(A) and 9(c)(i)(B~~ the definition of "Default Amount" at Condition 9(e)) of the Bonds,…"
	Senior Funding Agreements	**Senior Funding Agreements** means the agreements listed in Part 1 of Section ~~2A~~B of Schedule Part 6 (*Transaction Documents*) in the Agreed Form or as amended in	Cross-reference corrected	Acceptable	

~~43~~15 Note: Subject to discussion between Alpha/THC and SE. Note cross references to the terms and conditions of the Bonds will need to be updated to reflect any additional condition in relation to compensation on termination for Contractor Default No Retendering in the final form bond T&Cs.

~~43 Note: Subject to discussion between Alpha/THC.~~

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		accordance with Clause 7.2 *(Changes to Funding Agreements)*;			
	Service Availability Date	means the date of issue of an Acceptance Certificate in respect of the relevant New Project Facility (other than the External Works) or the date determined under the Dispute Resolution Procedure as the date on which Service Availability occurred;	Change to definition reflecting the agreed position on Phasing in and distinction in relation to External Works Availability	Acceptable as project specific	
	Services Compensation Event	(e) The existence of [~~INSERT DETAILS OF EXISTING CONTAMINATION ISSUES AND POTENTIAL MIGRATION~~benzo(a)pyrene], Japanese knotweed and/or nickel contamination] at the Kinlochleven Site after the [Date for Possession]; ~~[to be discussed – await specific wording]~~ (f) The exercise of the Reserved Rights in breach of the conditions contained in Clause 19.4 hereof; (g) ~~(f)~~ The occurrence of any Title Compensation Event;	Development of definition required to reflect more fully the extent of this Project-specific Service Compensation Event (contamination that has been identified at Kinlochleven, which the Council has agreed to remove) and, re Reserved Rights	Acceptable as project specific on basis of council's legal advice	
	Site - 17 03 06	**Site** means the area edged [red] on the relevant Site Plan for each Project Facility (under exception of any area edged blue thereon) together with the buildings and other erections in and upon the same and the service ducts and media for all utilities and services serving such buildings and erections;			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
	Snagging Works	(a) the Section A Snagging Works (as defined in Paragraph 2 of Section A of Schedule Part 5 *(Service Availability Requirements)*); ~~and/or~~ (b) the Section B Snagging Works (as defined in Paragraph 2 of Section B of Schedule Part 5 (*External Works Availability Requirements*)); and/ or (c) the Section C Snagging Works (as defined in paragraph 2 of Section C of Schedule Part 5 (Grass Playing Fields Availability Requirements);	Change to definition reflecting the agreed position on Phasing and Grass Playing Fields, and distinction in relation to Availability Requirements	Acceptable as project specific	
	Subordinated Funding Agreements	means the agreements listed in Part 2 of Section ~~2~~B of Schedule Part 6 (*Transaction Documents*) in the Agreed Form, as amended or replaced from time to time in accordance with this Agreement;	Cross-reference corrected	Acceptable	
	Target Grass Playing Fields Availability Date	means, in relation to each New Project Facility, the date shown as the Target Grass Playing Fields Availability Date in Section B of Schedule Part 4 (*New Project Facilities*) or such later date as may be allowed in accordance with the terms of this Agreement;	Amendment to reflect the agreed position on Phasing in relation to Construction and Target Availability Dates (see below in relation to Clause 21)	Acceptable	
	Title Compensation Events	**Title Compensation Events** means notwithstanding any other provisions of this Agreement (a) any third party exercising or asserting any right of ownership over the Inches Site (or any part or parts thereof or any part of the initial access [road (referred to in Schedule Part 22A sub paragraph 3)] thereto);	Development of definition required to reflect more fully detailed access and land arrangements	(a) – Acceptable (b) – Not acceptable; SSSC drafting should be used. (c) – Acceptable (d) – Acceptable (e) – Please explain change from “Site” to “site.” (f) – Acceptable (g) - Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		(b) the exercise by any third party of any right ~~other than the Reserved Rights~~ which is (a) not disclosed in the Title Deeds or (b) is not otherwise ascertainable from an inspection of the Sites ~~provided that such rights do not~~other than (i) the Reserved Rights and/or (ii) those rights which relate to public water, sewerage, drainage, electricity, gas service media or telephone communication cables or service media existing as at the Execution Date; (c) the exercise by the party entitled thereto of the right to widen the road on the west side of the Cullicudden site shown [green/blue] on the Site Plan relative thereto; (d) the exercise by the party entitled thereto of the right to substitute the route of either the access road leading to or a servicing connected with the Cawdor Site; (e) the exercise by the former agricultural tenant of part of the Cawdor Site of any right of access over that part hereof shown [●] on the ~~Site~~site Plan relative thereto; (f) the exercise of the right to buy the Cawdor Site which becomes exercisable by virtue of (a) the construction of the new school not having materially commenced			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		within 5 years of the date of entry of the Authority's acquisition of the Cawdor Site or (b) the Authority using the Cawdor Site or obtaining consent to use it for any purpose other than educational and community purposes ; ~~(g) [non-compliance by the Authority with a planning condition number [●] contained in the Planning Consent in respect of the Interest Site]~~ ~~**[This is to be discussed further, the road is to be adopted and thereafter the contractors to comply with the Planning Permission.**]~~ (g) any third party exercising or asserting any right of ownership over that part of the Portree Site shown shaded [●] on the Site Plan relative thereto.			
	Works	means all the works described in the Authority's Requirements and Section [A] of the Contractor's Proposals including the design, construction, fitting out, equipping, testing and commissioning of the whole works to be undertaken at each Project Facility to achieve Service Availability and External Works Availability and works necessary for obtaining access to the Sites to be undertaken in accordance with this Agreement;	Cross-reference corrected	Acceptable	
	Works Compensation Event	(e) The existence of [~~INSERT DETAILS OF EXISTING CONTAMINATION ISSUES AND POTENTIAL~~	Development of definition required to reflect more fully the extent of this Project-specific Works Compensation Event	Acceptable as project specific on basis of council's legal advice	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		~~MIGRATION] at the Kinlochleven Site; [to be discussed]~~benzo(a)pyrene], Japanese knotweed and/or nickel contamination at the Kinlochleven Site after the [Date for Possession]; (f) The exercise of the Reserved Rights in breach of the conditions contained in Clause 19.4 hereof; (g) ~~(f)~~ The occurrence of any Title Compensation Event;	(contamination that has been identified at Kinlochleven, which the Council has agreed to remove) and, re Reserved Rights		
4.1	Conditionality [additional clause referred to]	This Agreement (other than the provisions of Clauses 1, 2, 3, 4, 40.2, 59, 67, 70, 71, 72, 74, 75, 80.1, 80.2.3, 80.3, 80.4, 82, 84 and 88) is conditional on the satisfaction of the Conditions Precedent.	Extends protection of this Clause to 80 .3 (invocation of rights under Clause 80 by either Party for minor infringements)	Not acceptable - use SSSC drafting.	
6.1	No warranty by Authority	~~Subject to Clause 6.5, the~~The Authority does not give any warranty or undertaking as to the relevance, completeness, accuracy or fitness for any purpose of any of the Disclosed Data.	Reflects that Clause 6.5 is not used	Acceptable	
8.1	Ancillary Rights	Subject to Clause 19.4 from the Effective Date until the Termination Date or the Expiry Date, whichever is the earlier, the Authority will afford the Ancillary Rights to the Contractor and Contractor Related Parties. The Additional Rights shall be exercised subject to the conditions set out in Section B of Schedule Part 16.	Reflects the provisions of Schedule Part 16 which the Parties have agreed should apply in relation to the exercise by the Contractor of Additional Rights (of access etc.)	Accepted as project specific	
8.12	Access during Operations	Subject to the provisions of this Agreement, with effect from the Service Availability Date for a New Project Facility, the Authority shall permit the Contractor and Contractor Related Parties reasonable access to and egress	Corrects position as correct defined term to be referred to here is New Project Facility	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		from that New Project Facility for the purpose of carrying out its obligations under the Agreement provided that the Contractor (subject to Clause 24.4) shall only be entitled to have access to an Area which is being used by the Authority for Educational Services or Community Educational Use with the prior consent of the relevant School Representative.			
10.1 and 10.1.1 & 4	Obligation to Carry Out	The Contractor shall or shall procure that the Building Contractor shall (subject to the Authority's obligations set out in Clause 22B and Schedule Part 22) secure the Necessary Consents and carry out the Works so that: 10.1.1 as set out in the Construction Programme (subject only to the terms of this Agreement) each New Project Facility shall achieve Service Availability on the Target Service Availability Date for that New Project Facility ~~and the External Works~~, the External Works at each New Project Facility shall achieve External Works Availability by the relevant Target External Works Availability Date and the Grass Playing Fields at each New Project Facility shall achieve ~~External Works~~Grass Playing Fields	Reflects the provisions of Schedule Part 22 which the Parties have agreed should operate in relation to certain Project/Site specific matters	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Availability by the relevant Target ~~External Works~~Grass Playing Fields Availability Date or, in the case of delay beyond the Target Service Availability Date ~~or~~, Target External Works Availability Date or Target Grass Playing Fields Availability Date (as the case may be), as soon as reasonably practicable thereafter; 10.1.4 new materials only will be included in any parts of the Works which comprise new build (unless ~~specified otherwise in [Appendix ● to Part ●][48] of the Contractor's Proposals or~~ the Authority agrees otherwise in writing with specific reference to this Clause). All goods used or included in the Works will be of satisfactory quality and no Prohibited Materials will be used or included in the Works;			
11.1.2 & 3	Contractor to follow Construction Programme	11.1.2 to produce and submit to the Authority's Representative in accordance with the Review Procedure a revised Construction Programme showing the manner in which the Works will be carried out and (if possible) the periods	Reflects the Parties' agreed position on Phasing in relation to Construction and the use of a Target Grass Playing Fields Availability Date, in addition to a Target External Works Availability Date and a Target Service	Acceptable as project specific	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		necessary to ensure completion of the Works at the relevant Project Facility by the relevant Target Service Availability Date ~~or~~, Target External Works Availability Date or Target Grass Playing Fields Availability Date, as the case may be; or 11.1.3 to produce and submit to the Authority's Representative in accordance with the Review Procedure a revised Construction Programme showing the steps which the Contractor intends to take to eliminate or reduce any delay in reaching the relevant Target Service Availability Date ~~or~~, Target External Works Availability Date or Target Grass Playing Fields Availability Date, as the case may be.	Availability Date		
16.2	Limitation	The Contractor will not be entitled to propose a variation to the Contractor's Proposals or to the Key Dates in the Construction Programme (other than where necessitated by a Specific Change in Law, a Discriminatory Change in Law or as a direct consequence of a variation to the Contractor's Proposals or to the Key Dates in the Construction Programme which is implemented at the request of the Authority) which would delay the Target Service Availability Date ~~or~~, Target External Works Availability Date or Target Grass Playing Fields Availability Date of the New Project Facility in question or would lead to an increase in the Unitary Charge.	Reflects the Parties' agreed position on Phasing in relation to Construction and the use of a Target Grass Playing Fields Availability Date, in addition to a Target External Works Availability Date and a Target Service Availability Date	Acceptable as project specific	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
17.6.1	Procedure for relief	as soon as practicable, and in any event within 20 Business Days after it becomes aware that the Works Compensation Event has caused or is likely to cause delay, breach of an obligation under this Agreement or the Contractor to incur costs or lose revenue, give to the Authority a notice of its claim for an extension of time to the Target Service Availability Date, Target External Works Availability Date~~,~~ and/or Target Grass Playing Fields Availability Date and/or the Deadline Dates, payment of compensation under Part 3 of this Agreement and/or relief from its obligations under this Agreement.	Minor typo clarifying application to each Target Availability Date and the Deadline Dates	Acceptable as project specific	
17.7.1	Giving of relief	the relevant part of the Construction Programme, Target Service Availability Dates, Target External Works Availability Dates~~,~~ Target Grass Playing Fields Availability ~~Date~~Dates and/or Deadline Dates shall be postponed by such time as shall be reasonable for such a Works Compensation Event, taking into account the likely effect of delay;	Minor typo clarifying there is more than one Target Availability Date	Acceptable as project specific	
19.2.1.3	Use of Sites	subject only to Paragraph 1.4 of Schedule Part 16 *(Property Agreements and Title Provisions)*, the rights exercisable over or in relation to the Sites (to the extent as disclosed in or would be reasonably obtainable ~~form~~from a due and diligent inspection of the Title Deeds or the Sites;	Minor typo	Acceptable	
	Final agreed drafting - 17 03 06	The Contractor is deemed: 19.2.1 to have satisfied itself in relation to: 19.2.1.1 means of access to and through the Sites, the			Drafting reflects agreed form of Schedule Part 16 which does not contain any proviso to this deeming provision. Change from "obtainable" reflects previous typo.

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		possibility of interference by any person with such access and the times and methods of working necessary to prevent any nuisance whether public or private to any third party; 19.2.1.2 the boundaries of the Sites; 19.2.1.3 ~~subject only to Paragraph 1.4 of Schedule Part 16 *(Property Agreements and Title Provisions)*,~~ the rights exercisable over or in relation to the Sites (to the extent ~~as~~ disclosed in or ~~would be~~ reasonably ~~obtainable~~ascertainable from a due and diligent inspection of the Title Deeds or the Sites; 19.2.1.4 the information disclosed in the Data Room in respect of the Sites; 19.2.1.5 the extent and nature of work and materials necessary for conducting and completing the Works;			
19.4	Third Party Rights and Reserved Rights	**19.4 Third Party Rights** and Reserved Rights 19.4.1 The Contractor shall observe and comply with	Clarifies the division between Contractor rights of occupation and Authority access by reference to Phasing Drawings, and makes provision in relation to Elgin	Acceptable as project specific on basis of council's legal advice	For information, final agreed drafting in relation to this clause is set out in the following row: 17 03 06

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		any third party rights (including public rights) which may exist from time to time in respect of land comprising and adjoining the Sites including the Reserved Rights, and the Contractor shall ensure that the Works are carried out in such a way as not to interfere with access to and use and occupation of public or private roads or footpaths by any person who is entitled to any such access, use or occupation.[~~51~~19] 19.4.2 The Contractor shall observe and comply with the Reserved Rights. Declaring, however, that in respect of those areas shown coloured blue on the relevant Phasing Drawing and that during the period shown on the relevant Phasing Drawing (being areas in respect of which the Contractor is entitled to exclusive occupation of the relevant Site for the said period) the Authority (or owner tenant or occupier as appropriate) shall not be entitled to	Hostel (Project-specific)		

[~~51~~19] Note: the exercise of a right not disclosed in the Title Deeds is a Compensation Event so this should be acceptable

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		exercise the Reserved Rights save with the prior written consent of the Contractor (such consent to be in the discretion of the Contractor acting reasonably provided that the Contractor shall ensure that access to the property currently know as Elgin Hostel is available through Portree High Schools at all times) and at such time or times as shall be agreed by the Contractor save in case of emergency when prior consent shall not be required. In all cases the exercise of the Reserved Rights shall be subject to the Authority (or such owner tenant or occupier as appropriate):- 19.4.2.1 complying with the Contractor's reasonable requirements regarding Site management and any applicable Legislation including health and safety requirements and site rules; 19.4.2.2 interfering with,			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		delaying or otherwise affecting the carrying out of the Works; and 19.4.2.3 not damaging the Works or any materials in the exercise of the Reserved Rights. [The Authority shall be responsible for the actions of Authority Related Parties and the said owners, tenants and occupiers of the Elgin Hostel while such Authority Related Parties, owners, tenants and/or occupiers are on the relevant Site as a consequence of the Reserved Rights and such actions shall be deemed to be actions of the Authority for the purposes of Works Compensation Events.]			
	Final agreed drafting - 17 03 06	19.4.1 The Contractor shall observe and comply with any third party rights (including public rights) which may exist from time to time in respect of land comprising and adjoining the Sites~~ including the Reserved Rights~~, and the Contractor shall ensure that the Works are carried out in such a way as not			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		to interfere with access to and use and occupation of public or private roads or footpaths by any person who is entitled to any such access, use or occupation.~~19~~20 19.4.2 The Contractor shall ~~observe and comply with~~not obstruct the exercise of the Reserved Rights~~. Declaring, however,~~ provided that, (1) in respect of those areas shown coloured blue on the relevant Phasing Drawing and that during the period shown on the relevant Phasing Drawing (being areas in respect of which the Contractor is entitled to exclusive occupation of the relevant Site for the said period) the ~~Authority (or owner tenant or occupier as appropriate) shall not be entitled to exercise the Reserved Rights save with the prior written consent of the Contractor (such consent to be in the discretion of the Contractor acting reasonably~~Reserved Rights in respect thereof shall only be exercisable by the party or			

~~19~~20 Note: the exercise of a right not disclosed in the Title Deeds is a Compensation Event so this should be acceptable

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		parties entitled thereto on their giving at least 48 hours verbal or written notification to the Contractor of their intention to exercise these rights save in the case of emergency provided that the Contractor shall ensure that access to the property currently ~~know~~ known as Elgin Hostel is available over a route through the Site of Portree High ~~Schools at all times) and at such time or times as shall be agreed by the Contractor save in case of emergency when prior consent shall not be required. In all cases~~School at all times and pedestrian access to the land adjoining Drummond Special Schools is available at all times (2) in all cases except in respect of the exercise of the public right of way (other than by the Authority or any Authority Related Party) presently exercisable over the Site of Portree High School the exercise of the Reserved Rights shall be subject to the Authority (or such owner tenant or occupier or other party exercising such Reserved Rights as appropriate):- 19.4.2.1 complying with the			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Contractor's reasonable requirements regarding Site management and any applicable Legislation including health and safety requirements and site rules; 19.4.2.2 not interfering with, delaying or otherwise adversely affecting the carrying out of the Works or the Services; ~~and~~ 19.4.2.3 not damaging the Works, the Project Facilities or any materials thereon in the exercise of the Reserved Rights. **~~[The Authority shall be responsible for the actions of Authority Related Parties and the said owners, tenants and occupiers of the Elgin Hostel while such Authority Related Parties, owners, tenants and/or occupiers are on the relevant Site as a consequence of the Reserved Rights and such actions shall be deemed to be actions of~~**			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		~~**the Authority for the purposes of Works Compensation Events.] Is this agreed?**~~ **Notwithstanding the foregoing, nothing in this Clause shall place responsibility on the Authority for the actions of any parties exercising the Reserved Rights in respect of either the Site of Portree high School or the Site of Drummond Special School to the extent that such parties are not authorised (whether specifically or impliedly) by the Authority to exercise them.**			
19.5	Safety, Security and Cleaning	The Contractor shall procure that at all times prior to the issue of an Acceptance Certificate in respect of a New Project Facility that the Works Area in question is maintained in an orderly, safe and secure state and without prejudice to such generality in accordance with the requirements of Section ~~[●]~~2, Section C.3 of the Authority's Requirements provided that no act or omission on the part of the Authority shall result in the Contractor being in breach of the provisions of this Clause.	Completes reference to Authority's Requirements	Acceptable	
21.1	Inspection of a Project Facility	The Contractor shall give the Authority and the Technical Adviser not less than 5 Business Days' notice of the date when it proposes to inspect a New Project Facility with a view to issuing a Certificate of Service Availability, a Certificate of External Works Availability or a Certificate of ~~External Works~~Grass Playing Fields Availability (as	Reflects the Parties' agreed position on Phasing in relation to Construction and the use of a Certificate of Grass Playing Fields Availability, in addition to a Certificate of External Works Availability and a Certificate of Service Availability	Acceptable as project specific	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		the case may be) in respect of that New Project Facility and representatives from the Authority and the Technical Adviser shall make a joint inspection with the Contractor.			
21.3	Authority Representations	The Contractor shall have due and proper regard to any representations made by the Authority or the Technical Adviser regarding the condition of the New Project Facility in respect of which a Certificate of Service Availability ~~or~~, a Certificate of External Works Availability or a Certificate of Grass Playing Fields Availability is proposed to be issued by the Contractor and any defects or items to be included on a Snagging List.	Reflects the Parties' agreed position on Phasing in relation to Construction and the use of a Certificate of Grass Playing Fields Availability, in addition to a Certificate of External Works Availability and a Certificate of Service Availability	Acceptable	
21.4	Issue of Statement	Immediately following the issue of any Certificate of Service Availability, Certificate of External Works Availability or Certificate of ~~External Works~~Grass Playing Fields Availability, the Contractor shall send a true and complete certified copy of such certificate and the Snagging List (if relevant) to the Authority and the Technical Adviser.	Reflects the Parties' agreed position on Phasing in relation to Construction and the use of a Certificate of Grass Playing Fields Availability, in addition to a Certificate of External Works Availability and a Certificate of Service Availability	Acceptable	
21.5	Issue of an Acceptance Certificate	**21.5 Issue of an Acceptance Certificate** 21.5.1 Following receipt of the certified copy of the Certificate of Service Availability and/or Certificate of External Works Availability and/or Certificate of Grass Playing Fields Availability pursuant to Clause 21.4 and provided that the Technical Adviser acting reasonably	Reflects the Parties' agreed position on Phasing in relation to Construction and the use of a Certificate of Grass Playing Fields Availability, in addition to a Certificate of External Works Availability and a Certificate of Service Availability	Acceptable as project specific	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		is satisfied that: 21.5.1.1 in relation to the relevant New Project Facility, the Service Availability Requirements ~~or~~, External Works Availability Requirements or Grass Playing Fields Availability Requirements (as the case may be) have been met; and 21.5.1.2 all outstanding Works detailed in the Snagging List are capable of being carried out within 20 Business Days (or such longer period as the Technical Adviser may agree in writing, having regard to the lead time in respect of the relevant items) of the date of the Acceptance Certificate save that the 20 Business Day period shall not	Reflects the Parties' agreed position on Phasing in relation to Construction and landscaping of grassed areas		

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		apply to any landscaping grassed areas or playing fields which have not been turfed at that stage or in respect of which the turf has not been laid for 6 full Growing Months due to the growing season, then the Technical Adviser shall within 5 Business Days issue an Acceptance Certificate in respect of the relevant New Project Facility or the relevant External Works or Grass Playing Fields (as the case may be). If the Technical Adviser declines to issue an Acceptance Certificate, and unless the parties agree within a further 5 Business Days to repeat the procedure set out in Clause 21.5.1 and so advise the Technical Adviser, the matter shall be determined under the Dispute Resolution Procedure. 21.5.2 The issue of an Acceptance Certificate and any identification of any outstanding Works detailed			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		in the Snagging List shall not relieve the Contractor of liability for Deductions in terms of Schedule Part 7 (*Payment Mechanism*) or otherwise diminish the obligations of the Contractor under this Agreement in accordance with the terms of this Agreement. Subject to the operation of the provisions of Schedule Part 7 (*Payment Mechanism*) and without affording any relief to the Contractor from meeting the requirements of the Operational Services Specification or from liability for Deductions in terms of Schedule Part 7 (*Payment Mechanism*), the Authority shall not be entitled to, and shall be deemed to have waived any right to claim that there has been a breach by the Contractor of its obligations under Clause 15.7 *(Rectification of Contractor's Proposals)* which should have been apparent from any detailed visual inspection of the Works following the issue of the relevant Acceptance Certificate but not otherwise, unless the claim intimating the same is			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		made prior to the second anniversary of the relevant Service Availability Date ~~or~~, External Works Availability Date or Grass Playing Fields Availability Date, as the case may be.			
21.8.1,2 & 8	Completion of Works detailed in the Snagging List	21.8.1 Unless otherwise agreed pursuant to Clause 21.8.7 and Clause 21.8.8 below, the Contractor shall carry out all outstanding Works detailed in the Snagging List annexed to the relevant Certificate of Service Availability, Certificate of External Works Availability or Certificate of ~~External Works~~Grass Playing Fields Availability (as the case may be) to the reasonable satisfaction of the Technical Adviser (acting in accordance with the Technical Adviser's Deed of Appointment) within 20 Business Days of the date of the issue of the Acceptance Certificate. 21.8.2 Subject to Clause ~~21.8.7,~~21.8.7 and Clause 21.8.8, if 20 Business Days after the date of issue of any Acceptance Certificate, 21.8.8 If the outstanding work detailed on the Snagging List is landscaping grassed areas or playing fields which have not been turfed at that stage or in respect of which the turf has not been laid for 6 full Growing Months due to the growing season then the Contractor shall be obliged	Reflects the Parties' agreed position on Phasing in relation to Construction and the use of a Certificate of Grass Playing Fields Availability, in addition to a Certificate of External Works Availability and a Certificate of Service Availability Reflects the Parties' agreed position on Phasing in relation to Construction and landscaping of grassed areas (with reference to Growing Months reflecting practicalities of completion with regard to the seasonal nature of turfing)	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		to lay the turf in the next appropriate growing season (where it has not already been laid) and to achieve the Service Availability Requirements or External Works Availability Requirements (as the case may be) in respect of the relevant areas of turf when the relevant area of turf has been laid for 6 full Growing Months			
22A	JUDICIAL REVIEW	~~**[22A JUDICIAL REVIEW – [Note: as advised, the FPU have rejected the position on judicial review as drafted below. This clause will be updated once a new commercial position is agreed and FPU sign off achieved. Alpha to revert.]**~~ ~~"**Judicial Review**" means judicial review under Chapter 58 of the Rules of the Court of Session or any statutory challenge or appeal against the Authority or the Scottish Executive which proceeds on principles similar to judicial review, which concerns the legality of any grant of planning permission.~~ **22A JUDICIAL REVIEW** 22A.1 Where any application for Judicial Review is made, the Authority shall notify the Contractor as soon as it becomes aware of such application and:-			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		22A.1.1 for the avoidance of doubt, the Authority shall be entitled to defend, compromise or take any other step in relation to such application as it shall think fit; 22A.1.2 the Contractor shall at the written request of the Authority: (a) provide to the Authority all such relevant evidence and information as is available to the Contractor; and (b) co-operate in the provision of witnesses, which is or are necessary and (in the case of (a) above) may be lawfully disclosed to the Authority and employed by it for the effective defence of the Judicial Review proceedings. The Authority shall reimburse the Contractor's proper and reasonable costs of	Clarifies that the impact of such suspension is that it should not automatically be considered as a Relief Event – that should be restricted to amended limb (h) of the definition of relief Event Reflects revised position in line with previous SE comments (time-limit to relief and relief restricted only to certain of the Project Facilities)		

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		compliance with this Clause 22A.1.2; and 22A.1.3 the Contractor may be required by order of the court to suspend the Works in whole or part for such period or periods as may from time to time be notified to the Contractor~~ and any such suspension shall constitute a Relief Event~~. In the absence of such a requirement, the Contractor shall be entitled to continue with the Works as if no application for Judicial Review had been made. 22A.2 Subject to Clause 22A.3 if ~~a~~an application for Relevant Judicial Review made within the period of three months from the Effective Date results in the revocation, quashing or withdrawal of ~~any of the planning permissions granted in relation to the Project, ~~the Dingwall Permission and/or the Portree Permission: 22A.2.1 the Authority shall elect within 20 Business Days to either: ~~22A.2.1~~(a) serve an Authority Notice of Change on the	Clarifies Contractor right to continue with Works etc. pending agreement of change Deletion of provisions that required automatic termination of the Project Agreement, in line with previous SE comments.		

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Contractor under Clause 56.1: (~~a~~i) varying the Authority's Requirements by the removal of the affected Project Facility from the Project; or (~~b~~ii) instructing the Contractor to proceed with a new planning application in respect of the Project Facility(ies) affected by the Judicial	Clarifies Authority to issue notice to proceed to ensure procedures designed to offer proportionate protection to the Contractor are not able to be frustrated by Authority failure to do so. Reflects revised position in line with previous SE comments (time-limit to relief) – further changes clarify application of Compensation Event arrangements		

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Review; or ~~22A.2.2~~ (b) exercise its rights of appeal against the decision revoking, quashing or withdrawing the relevant planning permission~~; or~~, and if the Contractor is not notified of any such election within the said period of 20 Business Days, the Authority shall be deemed to have elected in accordance with Clause 22A.2.1(a)(i); and 22A.2.2 save to the extent that to do so would be a breach of Legislation, Guidance or any Necessary Consent, or an order of the court ordering suspension of the Works, the Contractor will be entitled to continue the Works at the affected Project Facility(ies) pending agreement of any Authority Notice of Change issued or deemed to have been issued pursuant to			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Clause 22A.2.1(a) in accordance with Clause 56 or the resolution of any appeal (as the case may be). ~~22A.2.3 terminate this Agreement, in which case the Authority shall forthwith serve notice pursuant to Clause 35.2.2.~~ For the avoidance of doubt the Authority shall issue an instruction to proceed with the agreed or determined Estimate issued in relation to any Authority Notice of Change served or deemed to be served under Clause 22A.2.1(a) pursuant to Clause 56.1.4A.2 and any such Authority Notice of Change shall not be capable of withdrawal notwithstanding Clause 56.1.9.2 and 56.1.10 (but subject always to Clause 56.1.16A). 22A.3 If the Contractor is required by order of the court following an application for Relevant Judicial Review made within the period of three months from the Effective Date in relation to the Portree Permission and/or the Dingwall Permission to suspend the Works in	Project-specific amendment to reflect necessary changes that would require to be made to Authority's Requirements in the event planning permission in respect of a change of design requested by the Council for Culbokie is not obtained in sufficient time to allow the Contractor to start the works on site by the scheduled commencement date.		

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		relation to either Portree High School or Dingwall Academy for a period in excess of ten (10 ~~months, the Authority shall be deemed to have exercised its rights pursuant to Clause 22A.2.3 with effect from the date falling 10 months after the date of suspension unless, prior to such date the Authority has confirmed an Estimate or an Estimate has been deemed to be agreed pursuant to Clause 56.1 in respect of an Authority Notice of Change served on the Contractor varying the Authority's Requirements by the removal of the affected Project Facility from the Project~~) months at either New Project Facility, any such period of suspension at such New Project Facility in excess of ten (10) months shall be deemed to be a Works Compensation Event and a Services Compensation Event. For the avoidance of doubt, all costs, losses			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		and/or expenses relating to the suspension of Works during such 10 month period shall be borne by the Contractor and shall not be recoverable from the Authority in any circumstances.~~]~~ 22A.4 In the event that the Authority elects to exercise its rights pursuant to: 22A.4.1 Clause 22A.2.1(a)(ii) and a new detailed planning permission in respect of the affected Project Facility has not been obtained by the expiry of the period of ten (10) months after the date of notification to the Contractor of the Authority's election (subject always to the Contractor having complied with its obligations under Clause 56.1 in respect of the relevant Authority Notice of			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Change); and/or 22A.4.2 Clause 22A.2.1(b) and no final decision in relation to such appeal has been given in favour of the Authority so that the planning permission that was the subject of the Relevant Judicial Review remains in full force and effect by the date falling ten (10) months after the date of notification to the Contractor of the Authority's election, any period of delay between the date falling ten (10) months after the date of such notification referred to in Clauses 22A.4.1 or 22A.4.2 above (as the case may be) and the date of grant of a new detailed planning permission in respect of the affected Project Facility or final decision (as the case may be) shall be deemed to be a Works Compensation Event and a Services Compensation Event but only in so far as the acts or omissions of the Contractor or any Contractor			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Related Party have not contributed to any such delay. For the avoidance of doubt, all costs, losses and/or expenses incurred by the Contractor prior to such ten (10) month period shall be borne by the Contractor and shall not be recoverable from the Authority in any circumstances 22A.5 In the event that: 22A.5.1 grant of detailed planning permission in respect of the Culbokie Application has not been obtained on or before [*the date falling two months prior to the start on Site date for Culbokie to be inserted*]; or 22A.5.2 any application for Relevant Judicial Review in respect of any detailed planning permission granted pursuant to the Culbokie Application made in the period ending *[on the start on Site date for Culbokie to be*			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		inserted] either results in the revoking, quashing or withdrawal of such planning permission prior to such date or has not been finally determined in favour of the Authority prior to such date, the parties agree that, with effect from [*the date falling two months prior to the start on Site date for Culbokie to be inserted]* where Clause 22A.5.1 applies or [*the start on Site date for Culbokie to be inserted]* where Clause 22A.5.2 applies (as the case may be): (a) the Authority's Requirements shall be amended by the substitution of [*MCSL/THC to identify where in the AR's the "default position will be set out*] for [*the section of the Authority's Requirements setting out the revised Culbokie requirements*];			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		(b) [the Unitary Charge shall be adjusted in accordance with Section B of Schedule Part 7 *(Unitary Charge Adjustment)* to reflect [*details to be inserted*]] *or* [the Contractor shall pay to the Authority within 30 days the sum of £[*to be inserted*]][*Alpha to confirm agreed position with funders on financial treatment of any savings*].			
23.1	Provision of Services	The Contractor shall provide to the Authority or procure the provision to the Authority of the Operational Services at each New Project Facility on the terms of this Agreement with effect from the Service Availability Date for that New Project Facility or, in respect of External Works, the relevant External Works Availability Date or, in respect of Grass Playing Fields, the relevant Grass Playing Fields Availability Date.	Reflects the Parties' agreed position on Phasing in relation to Construction and the use of a Target Grass Playing Fields Availability Date, in addition to a Target External Works Availability Date and a Target Service Availability Date	Acceptable as project specific	
23.2A1	Inconsistency between Operational Services	If the Authority or the Contractor finds there is any inconsistency ~~of~~or contradiction between the Operational Services Specification and the Operation and	Correction of minor typo	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
	Specification and Operation and Maintenance Proposals	Maintenance Proposals it shall give notice to the other specifying the inconsistency or contradiction			
23.3	Services Compensation Event	If, as a direct result of the occurrence of a Services Compensation Event, the Contractor is unable or will be unable to comply with its obligations under this Agreement and/or the Contractor incurs or may incur costs or loses or may lose revenue in excess of ~~[~~£150~~]~~ (Indexed) per event or ~~[~~£5,000~~]~~ (Indexed) in aggregate in any Contract Year (**Relief Amount**) then, subject to Clause 23.6, the Contractor shall be entitled to claim compensation under this Part 4 of the Agreement and or relief from its obligations under this Agreement.	Square brackets removed	Acceptable (Green issue)	
24.4.5.1	Maintenance Programme	~~save~~ in the case of Urgent need, then in accordance with Clause 24.4.6	Correction of minor typo	Acceptable	
28.1.2(i)	Benchmarking	the standards and prices of the relevant Operational Services element as detailed in the relevant sub contract and the costs of the provision thereof by the FM Contractor (or of the relevant sub-contractor of the FM Contractor if a sub-contractor is delivering the Operational Services in question) as identified in the Financial Model (as such element may have been adjusted as a result of being Indexed or as a result of previous adjustments made pursuant to ~~this Clauses~~Clause 17 (*Extension of Time*), Clause 23, Clause 28, or the Change Procedure (**Base Cost**);	Correction of minor typo	Acceptable	
28.1.5	Benchmarking	TD~~, SU~~ and ~~SUSF~~SU are as defined in Schedule Part 7 (*Payment Mechanism*).	Correction of cross-reference to Payment Mechanism – SUSF is not used on this Project	FPU comment asap	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
28.1.6	Benchmarking	TD~~, SU~~ and ~~SUSF~~SU are as defined in Schedule Part 7 (*Payment Mechanism*).	As for Clause 28.1.5	FPU comment asap	
28.5.1	Adjustments to Unitary Charge	TD~~, SU~~ and ~~SUSF~~SU are as defined in Schedule Part 7 (*Payment Mechanism*).	As for Clause 28.1.5	FPU comment asap	
28.5.2	Adjustments to Unitary Charge	Where P_s = Successful ~~tenderer~~Tenderer's tender price P_A has meaning given to it in Clause 28.1.5 and TD~~, SU~~ and ~~SUSF~~SU are as defined in Schedule Part 7 (*Payment Mechanism*).	As for Clause 28.1.5	FPU comment asap	
30.2.2.2	Contractor Responsibilities	procure that each Relevant Employee who is a member of the Local Government Scheme at the date of the Relevant Transfer will be entitled, during the whole period that the Relevant Employee is involved in the provision of the Services, to remain a member of the Local Government Scheme on substantially the same terms as those offered to him whilst employed by the Authority and that his service under the Local Government Scheme is treated as continuous, or in the case of a Relevant Employee who is not a member of the Local Government Scheme at the date of the Relevant Transfer but was entitled to become such a member procure that such Relevant Employees are entitled to become members of the Local Government Scheme on substantially the same terms as those offered to those Relevant Employees who were members of the Local Government	Clarification/correction to the effect that application of pensions provisions is to be by reference to date of the Relevant Transfer not the Commencement Date (which term has been deleted from the Project Agreement previously)	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Scheme at the ~~Commencement Date~~date of the Relevant Transfer;			
30.4A.1	Costs of Employment	As at the Execution Date, Part 12 of the Schedule (~~Warranted~~*Employment Cost Data*) ("**the Employees List**") represents the Authority's estimate, acting reasonably and in good faith, of those persons (including persons who will be appointed to positions marked as vacancies) who will be Relevant Employees at the relevant New Project Facility by the Service Availability Date and the Authority confirms that the information detailed in the Employees' List is complete and accurate in all respects.	Correction of cross-reference	Acceptable	
30.4A.4	Costs of Employment	The Contractor shall notify the Authority of the annual costs of employment of the Assigned Employees at each New Project Facility within ~~[~~30~~]~~ days of the parties' agreement (or of determination under the Dispute Resolution Procedure) of the Final Employees List for that New Project Facility.	Removal of square brackets	Acceptable (Green)	
31.9.1	Authority Notice	The Authority may in circumstances where information is received under the terms of Clause 31.8, in its absolute discretion, instruct the Contractor by way of a written notice not to employ or continue to employ (or procure that the Employer does not employ or continue to employ) that person in connection with the provision of the Services and to remove or procure the removal of that person from the Sites and/or the New Project Facilities. The decision of the Authority to issue such a notice shall be final and conclusive.	Insertion of bracket	Acceptable	
35.1.11	Contractor Event of	the Contractor receives a total number of five or more Warning Notices in any period of 12	THC and Alpha have agreed this Contractor Event of Default	Up to council under SSSC, but FPU considers that this	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
	Default Termination	consecutive months ending on or before the first Service Availability Date, six or more Warning Notices in any period of 12 consecutive months commencing on or after the first Service Availability Date or five or more Warning Notices in any period of 12 consecutive months commencing after the last External Works Availability Date; and/or	Termination as part of final negotiations, considering that the appropriate level of Warning Notices during the latter stages of the construction period of this project (while there is service provision under the Operating Agreement and Works continue under the Building Contract) should be six to reflect the requirements to pass down this termination trigger to Alpha's main Sub-Contractors. This avoids the risk that the project is forced to suffer the effects of termination of sub-contractors at a relatively early stage.	is a generous approach and weakens its contractual position	
43	DEFINITIONS				
	Adjusted Estimated Fair Value	(g) any Post Termination Service Amounts (if a negative number) which have not been set off in accordance with Clause ~~45.2.6~~45.2.8 prior to the Compensation Date	Correction of cross-reference	Acceptable	
	Adjusted Highest Compliant Tender Price	(g) (g) any Post Termination Service Amounts (if a negative number) which have not been set off in accordance with Clause ~~45.2.6~~45.2.8 prior to the Compensation Date	Correction of cross-reference	Acceptable	
	Breakage Costs	…including costs of early termination of the Guaranteed Investment Contract and ~~an~~any other interest hedging arrangements and any other breakage or termination costs	Correction of minor typo	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		calculated in accordance with the terms of the Senior Funding Agreements, subject to the Contractor and the Senior Lenders mitigating any such costs to the extent reasonably possible (unless the amount, the method or the formula for determining the amount of such costs are fixed in advance under the terms of the relevant Senior Funding Agreements			
	Senior Debt Interest Rate	~~[~~**Senior Debt Interest Rate** means in respect of the Bonds the interest rate (not being the default rate) that applies to the Bonds in terms of the Conditions and in respect of the ~~[EIB Loan]~~Credit , the rate (not being the default rate) that applies under the EIB Loan Agreement; ~~[Note: clause reference to be confirmed once the EIB Loan Agreement is circulated]~~	Amendment to conform with new definition inserted (making reference to definition in funding documentation).	Acceptable	
44.4	Distributions	If a Distribution is made whilst any Additional Permitted Borrowing is outstanding and the Contractor has wilfully, or through gross negligence, failed to comply with its obligations under Clause [~~10~~12(d)(iv)(a)] of the Direct Agreement then in addition to the deduction of the Distribution referred to in paragraph (v) of the definition of Revised Senior Debt Termination Amount , the Authority shall be entitled to set off the value of that Distribution a second time against the Force Majeure Termination Sum, provided that the amount of the Force Majeure Termination Sum will never be less than the Revised Senior Debt Termination Amount .	Reference to Direct Agreement corrected	Acceptable	
44.5	Overstatement of Balances	If the Contractor has wilfully or through gross negligence failed to comply with its obligations under Clause [~~10~~12(d)(iv)(b)] of		Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		the Direct Agreement and there has been an overstatement of the cash balances by the Contractor as at that date which has caused the Authority to reasonably believe that it would be required to pay a lesser sum at the Termination Date than it actually is required to pay under the terms of this Clause 44, then the Force Majeure Termination Sum, shall be reduced by the amount of such overstatement (to the extent such overstatement is still applicable at the Termination Date), provided that the amount of the Force Majeure Termination Sum will never be less than the Revised Senior Debt Termination Amount .			
44.6.1	Payment	~~[~~The compensation payable pursuant to Clause 44 shall be paid in accordance with Clause 47A.~~]~~	Square brackets removed	Acceptable	
45.1	Retendering Election	~~The~~On termination of this Agreement under Clause 35.1 (*Contractor Event of Default Termination*), the Authority shall be entitled to retender the provision of the Works and the Services or the Services in accordance with Clause 45.2 *(Retendering)* and the provisions of Clause 45.2 shall apply if:	Clarification of when entitlement to retender arises	No – use SSSC	THC would wish that its proposed derogation be re-considered further to correspondence today involving the FPU (Ben King) on the issue.
45.2.11	Retendering Election	…interest on such part shall be at the Senior Debt Default Interest Rate………… and thereafter at the Senior Debt Default Interest Rate	The parties agreed previously that this is the appropriate interest rate to apply in the relevant circumstances (default on payment). Typo correction.	Acceptable	
45.3.5 & 45.4 & 5	No Retendering	[45.3.5 The Authority shall pay to the Contractor an amount equal to the Adjusted Estimated Fair Value of the Agreement either as by	Reflects the Parties' agreed position as to lump sum payment of compensation on Contractor Default (No Retendering). Clause links in Project–specific drafting on	FPU have accepted principles related to the instalment arrangements for all compensation scenarios.	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		way of a lump sum payment (in accordance with Clause 47A.3) on the date falling [28] days after the date on which the Adjusted Estimated Fair Value of the Agreement has been agreed or determined in accordance with this Clause 45.3 ~~or, at its election, either: [Note: this definition will be updated to reflect the principles set out in the Scottish Executive letter of 12th February 2004. Scottish Executive drafting awaited].~~[23], either: 45.3.5.1 in instalments in accordance with the provisions of ~~Clauses 45.4 and 45.5 save where the Authority is in material breach~~	Clause 47A.		

[23] Note: time period to tie in with Clause 45.3.

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		~~of its obligation to pay in instalments in which case the outstanding amount of the compensation shall become due and payable within three months of such material breach~~Clause 47A; or 45.3.5.2 as the parties may otherwise agree; 45.4 The ~~Authority shall be entitled to pay the compensation payable in [•] equal instalments by serving notice on the Contractor within forty [40] Business Days of the Termination Date, in which case the provision of Clause 45.5 shall apply.~~			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		~~45.5 In the event that the Authority elects to pay the compensation in instalments pursuant to Clause 45.4 then:~~ ~~45.5.1 the first such instalment (together with interest therein calculated pursuant to 45.5.2 below) shall be due on the first Business Day occurring [•] months after the date of the Authority's notice served pursuant to 45.4 above and the remaining instalments (together with interest therein calculated pursuant to 45.5.2 below) shall be due, respectively, on the first Business Day occurring [•], [•], [•], [•] etc months after the date of such notice;~~ ~~45.5.2 the Authority shall pay interest on the compensation (or any part of such compensation that remains outstanding) from the Termination Date until the date of payment at the [•]; 45.5.3 The~~ discharge by the Authority of its obligation in Clause 45.3.5 is in full and final settlement of all the Contractor's claims and rights against the Authority for breaches and/or			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		termination of this Agreement or other Project Documents whether in contract, delict, restitution or otherwise, including in relation to any Post Termination Service Amount which has fallen due pursuant to Clause 45.3.1 but not yet been paid save for any liability which arose prior to the Termination Date (but not from the termination itself) which has not been taken into account in determining the Adjusted Estimated Fair Value of the Agreement. ~~45.5.4~~45.5 To the extent that the Adjusted Estimated Fair Value of the Agreement is less than zero, an amount equal to the sum by which the Adjusted Estimated Fair Value of the Agreement falls below zero shall be due and payable by the Contractor to the Authority on the Compensation Date.]			
46.1.7	Adjustment of Authority Default Termination	failed to comply with its obligations under Clause ~~10~~[12(d)(iv)(a)]	Reference to Direct Agreement corrected	Acceptable	
46.1.8	Adjustment of Authority Default Termination	failed to comply with its obligations under Clause ~~10~~[12(d)(iv)(b)]	Reference to Direct Agreement corrected	Acceptable	
46.2	Method of	~~[~~The compensation payable pursuant to this	Square brackets removed	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
	Payment	Clause 46 shall be paid in accordance with clauses 47A.1.1 and 47A.3 or Clause 47A.1.3.~~]~~			
47.2	Method of Payment	~~[~~The compensation payable pursuant to Clause 47.1 shall be paid in accordance with Clause 47A.~~]~~	Square brackets removed	Acceptable	
47A.1.1& 3	PAYMENT	**47A.1** The compensation payable pursuant to ~~[~~Clauses ~~44~~44, 45.3 and 47~~]~~ shall at the Authority's discretion be paid either: 47A.1.1 in a lump sum in accordance with Clause 47A.3 provided that, in the case of Clauses 44 and 47 only, the Base Senior Debt Termination Amount	Note: Clause 47A subject to outcome of SE discussions. Correction of Clause references and clarificatory amendments.	To be updated	"47A.1.1 in a lump sum, and (i) in the case of compensation payable pursuant to Clause 45.3 in accordance with Clause 45.3.5.1; and (ii) in the case of compensation payable pursuant to Clauses 44 and 47 only in accordance with Clause 47A.3 provided that, the Base Senior Debt Termination Amount or, where Additional Permitted Borrowings ...."
47A.1.2	PAYMENT	the relevant compensation amount shall not, subject to Clause 47A.2.6, be subject to the deduction of the balance standing to the credit	See comment in relation to Clause 47A.1.1&3. Clarificatory amendment.	To be updated	in respect of the amounts of compensation other than compensation payable pursuant to Clauses 44.1.4 (which shall be payable in lump sum in accordance with Clause 47A.1.1 above) in instalments, by serving notice (the "**Instalment Notice**") on the Contractor within ~~[20]~~(i) in the case of compensation payable pursuant to Clauses 44 and 47, 20 Business Days of the Termination Date ~~in which case~~ ; and (ii) in the case of compensation payable pursuant to Clause 45.3, 10 Business Days of the Adjusted Estimated Fair Value being agreed or

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
					determined, whereupon (other than in the case of compensation payable pursuant to Clauses 44.1.2 and 44.1.3, where payment shall be made pursuant to Clause 47A.4) the provisions of Clause 47A.2 shall apply (the "**Instalment Option**") save where the Authority is in breach of its obligations under Clause 47A.2 in which case the outstanding amount of the compensation will become due and payable immediately, provided that for the purposes of the Instalment Option, the relevant compensation amount shall not, subject to Clause 47A.2.6, be subject to the deduction of the balance standing to the credit of the Debt Service Reserve Account. All other credit balances on any bank accounts (but excluding the Joint Insurance Account and the ~~Distribution~~Distributions Account) held by or on behalf of the Contractor on the Termination Date, shall be deducted on a pound for pound basis against the first payment of principal and interest due and payable by the Authority under Clause 47A.2 and against each subsequent such payment until those credit balances have been reduced to zero;"
47A.2.1	PAYMENT	it shall, subject to ~~Clause~~Clauses 47A.~~2.6,~~2.6 and 47A.2.8, unconditionally and irrevocably: …………… Subject to ~~Clause~~Clauses 47A.~~2.6,~~2.6 and 47A.2.8, if any of the above	Correction of cross-references.	To be updated	…."~~it shall, subject to Clause 47A.2.6,~~subject to Clauses 47A.2.6 and 47A.2.8, it shall, in the case of

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		conditions remain unsatisfied after a period of forty five (45) days has elapsed from the date of the Instalment Notice			compensation payable pursuant to Clauses 44 and 47 only, unconditionally and irrevocably: (i) make all payments of interest and principal due under the Senior Funding Agreements and (ii) make all other payments due under any Senior Funding Agreement or, in the case of compensation payable pursuant to Clause 45.3, make all payments due under Clause 47A.2.8 during the Condition Satisfaction Period and thereafter, in ~~each case~~the case of compensation payable pursuant to Clauses 44 and 47 only, on the due date for payment set out in the relevant Senior Funding Agreement ~~provided that~~(prior to any acceleration) or in the case of compensation payable pursuant to Clause 45.3 on the due date for payment set out in Clause 47A.2.8, provided that, in each case, for any such payments to be made after the Condition Satisfaction Period the following conditions are satisfied (in each case, to the reasonable satisfaction of the Credit Provider and the Bond Trustee): 47A.2.1.1 each instalment of principal and interest payable under the Senior Funding Agreements is paid to the Contractor not less than ten (10) Business Days prior to the date on which

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
					such amount is due to be paid (prior to any acceleration) by the Contractor under the relevant Senior Funding Agreement or in the case of compensation payable pursuant to Clause 45.3 on the due date for payment set out in Clause 47A.2.8; "
47A.2.1.2	PAYMENT	all amounts due to ~~[~~Ambac~~]~~ under the Reimbursement and Indemnity Agreement and the Ambac Fee Letter are paid by the Authority to ~~[~~Ambac~~]~~ within [fifteen (15)] Business Days of demand	Square brackets removed	Acceptable	
47A.2.1.4	PAYMENT	"….the Authority pays all necessary costs and expenses of the Contractor, HoldCo, the Issuer and the Senior Lenders in respect of the ongoing operations of the Contractor to include (without limitation) the Contractor maintaining the arrangements contemplated by this Clause 47A.2.1, maintaining an underlying rating of the Bonds and maintaining the Debt Service Reserve Account at the level required by the Collateral Deed and the Accounts Agreement and that within [(15) Business Days] of such amounts being agreed or determined; "			
4/A.2.1.5	PAYMENT	"…In the case of compensation payable pursuant to Clauses 44 and 47 only, the Authority has paid any Breakage Costs			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		for which it is liable under paragraph (b) of the definition of Base Senior Debt Termination Amount or paragraph (c) of the definition of Revised Senior Debt Termination Amount (whichever is relevant); "			
47A.2.1.7	PAYMENT	"…the Authority, the Senior Lenders and the Contractor (acting reasonably) agreeing the terms of a new agreement to give effect to the instalment arrangements ~~and~~, based on the provisions of this Part ~~7 (including the amount and timing of the payments referred to in Clause 47A.2.1.1 above)~~7, and such agreement has been executed by all the parties thereto and is in full force and effect and any required amendments to existing documents and/or the execution of any new documents have been completed;"			
47A.2.2	PAYMENT	The Contractor and the Senior Lenders will be required to take such reasonable steps as are necessary to mitigate the costs and expenses incurred pursuant to paragraphs 47A.2.1.3 and 47A.2.1.4 and will be required to provide reasonable supporting evidence in respect of the amounts due under paragraphs 47A.~~1.2~~1.2, 47A.2.1.3 and 47A.2.1.4.	Correction of cross-reference	Acceptable	
47A.2.3	PAYMENT	In such case the Authority shall, subject to Clause 47A.2.8 pay to the Contractor the Base Senior Debt Termination Amount or the Revised Senior Debt Termination Amount	Clarificatory amendment.	Accepted	…."Where the Authority has exercised the Instalment Option in accordance with Clause 47A.2 and has satisfied the

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
					relevant conditions, the Authority may (in the case of compensation payable pursuant to Clauses 44 and 47 only) at any time thereafter, by (20) Business Days notice in writing to the Contractor and the Security Trustee (the "Election Notice") elect to discontinue the Instalment Option."
47A.2.4	PAYMENT	Subject to Clause 47A.~~2.6,~~2.7 and 47A.2.8, where the Authority has exercised the Instalment Option in accordance with Clause 47A.2	Correction of cross-references	Accepted	"…47.2.4.2………~~The~~In the case of compensation payable pursuant to Clauses 44 and 47 only, the Authority shall be required to pay Breakage Costs pursuant to this Clause 47A.2.4 notwithstanding that the Authority is also required to pay Breakage Costs pursuant to paragraph (b) of the definition of Base Senior Debt Termination Amount or paragraph (c) of the definition of Revised Senior Debt Termination Amount (as the case may be), provided there shall be no double counting."
47A.2.7	PAYMENT	The Authority may elect not to continue with the Instalment Option at any time ~~following~~from the date of the Instalment Notice ~~prior~~ to the earlier of (i) the end of the Condition Satisfaction Period and (ii) the date on which the agreement referred to in Clause 47A.2.1.7 is in full force and effect. In the event that the Authority exercises such an election compensation will be payable in accordance with Clause 47A.1.1 or Clause 47A.1.3. For the purposes of this Clause 47A.~~2.6~~2.7 and the time for payment under Clause 47A.3, the Termination Date for the purposes of the calculation of the Base	Correction of minor typos and cross-references	Typos – no. Cross-references – yes.	"…~~The~~In the case of compensation payable pursuant to Clauses 44 and 47 only, the Authority may elect not to continue with the Instalment Option at any time following the date of the Instalment Notice prior to the earlier of (i) the end of the Condition Satisfaction Period and (ii) the date on which the agreement referred to in Clause 47A.2.1.7 is in full force and effect. "

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Senior Debt Termination Amount or the Revised Senior Debt Termination Amount (as the case may be) shall be the date of the Authority's election pursuant to this Clause 47A.~~2.6.~~2.7.			
47A.2.8	PAYMENT		See comment in relation to Clause 47A.1.1&3. Please see separate submission paper.	To be updated	"Where compensation is payable by the Authority under Clause 45.3, and the Authority has elected to pay such compensation in instalments in accordance with Clauses 45.3.5.2 and 47A.1.2, the Authority shall pay an amount equal to the Adjusted Estimated Fair Value of the Agreement to the Contractor in equal instalments on the date 10 Business Days before each [Scheduled Payment Date][26] (as scheduled prior to any acceleration under the Senior Funding Agreements) during the Instalment Period and all amounts due under Clause 47A.2.1, provided that the obligations of the Authority to make payment to the Contractor under each of Clauses 47A.2.1, 47A.2.1.1 to 47A.2.1.4 and 47A.2.3 and 47A.2.4 shall be to pay the proportion of amounts due under such Clauses that the (a) Adjusted Estimated Fair Value of the Agreement bears to (b) the Base Senior Debt Termination Amount, or where Additional Permitted Borrowings have been advanced in accordance with the terms of this

[26] Note: "Payment Date" in the MDS refer to the Conditions but does not appear to be defined in the Conditions?

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
					Agreement, the Revised Senior Debt Termination Amount (in each case excluding any prepayment, breakage or similar costs,) "
47A.3	PAYMENT	In the event that the Authority elects to pay the compensation in a lump sum pursuant to Clause 47A.1 and in respect of compensation payable pursuant to Clauses ~~44.1.2, 44.1.3~~44, 45.3.5, 46 and ~~44.1.4 and 46~~47 then	Correction of cross-references	Acceptable	
47.A.3.2	PAYMENT				"….it shall pay the outstanding amount of the lump sum in full within six months of the Termination Date with interest at the Senior Debt Interest Rate accruing from the Termination Date until the date falling six months after the Termination Date and to the extent such lump sum has not been paid in full by the date falling six months after the Termination Date, interest at the Senior Debt Default Interest Rate accruing from the date falling six months after the Termination Date until paid in full"
47A.4	PAYMENT				
49.1	Maintenance of Accounts	The accounts of the Contractor shall be maintained as foreseen in the Financial Model, in particular, and without limiting the generality of the obligation contained in this Clause, the Contractor shall ensure that it is at all times possible to determine the balances of the [Debt Service Reserve Account] and the [Major Maintenance Reserve Account]			

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
53.1	Liaison Committee	The Authority and the Contractor shall establish and maintain the Liaison Committee with effect from the ~~Commencement~~Effective Date throughout the Contract Period.	The Liaison Committee is to operate as from the Effective Date	Acceptable	
54.2.3.2	Relief	To obtain relief, the Contractor must: 54.2.1 as soon as practicable, and in any event within 10 Business Days after it becomes aware that the Relief Event has caused or is likely to cause delay and/or adversely affect the ability of the Contractor to perform its other obligations give to the Authority a notice of its claim for relief from its obligations under this Agreement, including full details of the nature of the Relief Event, the date of occurrence and its likely duration; 54.2.2within 5 Business Days of receipt by the Authority of the notice referred to in Clause 54.2.1, give full details of the relief claimed; and 54.2.3 demonstrate to the reasonable satisfaction of the Authority that: 54.2.3.1 the Contractor and its sub-contractors could not have avoided the occurrence or consequences of the relevant Relief Event by steps which they might reasonably be expected to have taken, without incurring material expenditure; 54.2.3.2 the Relief Event directly will	Drafting change reflecting that Clause 54.2.1 includes the words "likely to cause delay *and/or adversely affect the ability of the Contractor to perform*", while Clause 54.2.3.2 referred to delay to performance which may not be the appropriate test – the parties have agreed these additional words to ensure that adverse effect on performance is duly taken into account throughout the clause.	Unacceptable – unless two precedents of exactly same wording in close deal	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		cause or has caused the delay to the achievement of the Service Availability Date by the relevant Target Service Availability Date and/or External Works Availability Date by the relevant Target External Works Availability Date or ~~to~~ the adverse effect on performance by the Contractor of any of its obligations under this Agreement;			
55.1.3	Change in Law	whether relief from compliance with obligations is required, including the obligation of the Contractor to achieve the Target Service Availability Date and/or any Target External Works Availability Date and/or any Target Grass Playing Fields Availability Date in relation to a New Project Facility and/or meet the Operational Services Specification during the implementation of any relevant Qualifying Change in Law	Correction of cross-reference	Acceptable	
56.1.4A. 1.3	Authority Changes	in the case of an Authority Change requested prior to any of the Service Availability Dates and/or External Works Availability Dates, and/or Grass Playing Fields Availability Dates~~,~~ the impact (if any) on the Target Service Availability Dates and/or Target External Works Availability Dates and/or ~~Target~~ Grass Playing Fields Availability Dates	Correction of minor typo	Acceptable	
57A.2	IMPLEMENTATION OF CHANGES	In the event of a conflict between the requirements of Clauses 57.A.1.1 to 57A.1.6 the requirements shall have precedence in the numerical order in Clause 57A.1, provided always that where such further	Correction of cross-reference to Contractor proposals	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		Contractor proposals provide greater benefit to the Authority, of which the Authority shall be sole judge, there shall be deemed to be no conflict (unless and to the extent the ~~Operational and Maintenance Proposals~~further Contractor proposals are inconsistent with Legislation and/or the Necessary Consents).			
60.2.2	Authority not responsible	any claim made under Clause 60.1.2 in respect of loss of or damage to property to the extent in excess of £~~25~~50 million~~[72]~~ or such greater sum as this liability is insured against.	This conforms the position under this Clause with the insurance levels in the Project Insurances	Acceptable	
61.10	Premiums	Subject to Clause ~~61A,~~61.13, the insurance premiums referred to in this Clause shall be the responsibility of the Contractor.	Correction of cross-reference	Acceptable	
69.2	Restrictions on Transfer of Shares	**69.2 ~~Restrictions on Transfer of Shares~~[Not Used]** ~~The Contractor shall not register the transfer of any shares or loan capital or any interest in any share or loan capital of the Contractor and the Contractor shall procure that the HoldCo shall not register the transfer of any shares or loan capital or any interest in any share or loan capital of the HoldCo (other than pursuant to the Financing Documents) prior to the second anniversary of the last Service Availability Date, save where such transfer is:~~ ~~69.2.1 to an Affiliate and on the basis that on any Affiliate~~	Not Used – as per SSSCv3.	Acceptable	

~~[72] Note: references to "Indexed" in Clauses 60.2.2 and 60.5.1 deleted as neither the Council nor the Contractor's insurance policies will be Indexed.~~

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		~~ceasing to be an Affiliate such shares or loan capital or interest in shares or loan capital are immediately re-transferred to the Contractor and/or HoldCo (as the case may be); or~~ ~~69.2.2 with the prior written consent of the Authority, which shall not be unreasonably withheld or delayed.~~ ~~Subject to the foregoing, the Contractor may register the transfer of any share or loan capital or any interest in the share or loan capital of the Contractor at any time.~~			
72.1	Notice Requirements	Director of Corporate Services Highland Council, Glenurquhart Road, Inverness, IV3 5NX Fax No: ~~[●]~~01463 702182	Authority contact details for written notice	Acceptable	
72.2	Submission of Information	~~[Address]~~Director of Property & Architectural Services, Highland Council, Glenurquhart Road, Inverness, IV3 5NX Fax No: ~~[●]~~ 01463 702222	Authority's Representative for submission of information	Acceptable	
83.2	Contractor's Obligations	Subject to Clause 83.3A, 83.9 and 83.10 the Contractor shall, at its own cost (but subject to an obligation to mitigate the costs of such	Correction of cross-reference	Acceptable	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		repair and/or replacement works to the extent reasonably practicable, in accordance with the Operational Services Specification (and also having regard to its obligations under Clause ~~83 .7~~83.7)):			
83.3A.1	Maximum Annual Liability	…in accordance with the provisions of the ~~Service~~Operational Services Specification and all such costs and deductions relating thereto shall be borne by the Contractor.	Change to conform Payment Mechanism and rectification provisions	Acceptable	
83.9.1&2	Rectification Period	83.9.1 Where Clause 83.3A (*Maximum Annual ~~Liabiltiy~~Liability*) applies, the provisions of this Clause 83.9 shall apply accordingly. 83.9.2 ~~Where malicious damage occurs, the requirements of the Operational Services Specification to achieve temporary rectification shall apply.~~ Save to the extent provided in terms of Clause 83.10	Change to conform Payment Mechanism and rectification provisions	Council to confirm that the arrangements in respect of Malicious Damage / risk sharing represent VfM	
83.9.2.2	Rectification Period	If either party believes that the Malicious Damage Rectification Programme proposed is not reasonable, or that the cost is excessive, the matter shall be referred to the Dispute Resolution Procedure. ~~Subject to Clause 83.10, the agreed or determined period for permanent repair and/or replacement contained within the Malicious Damage Rectification Programme, shall then be the Rectification Period for the purpose of Schedule Part 7 (*Payment Mechanism*) and the Operational Services Specification.~~	Change to conform Payment Mechanism and rectification provisions	As above	
83.9.4	Rectification Period	Where, during the Rectification Period referred to in Clause ~~83.9.2,~~83.10.2, the Contractor identifies (which it shall do as soon as reasonably practicable)	Change to correct cross reference	Acceptable	
83.9.5	Rectification Period	~~83.9.5 Save where Clause 83.3A (*Maximum Annual Liability*) applies, in the~~	Change to conform Payment Mechanism and rectification	As above	

Clause	Clause Heading/ Description	Amendments to PB9	Comment	FPU response 15-02-06	
		~~event that the malicious damage is not rectified by the expiry of the Rectification Period (as amended as the case may be) referred to in Clause 83.9.2 then, for the purpose of Schedule Part 7, the Logged Failure Time shall be deemed to be 9a.m on the Business Day immediately following the day on which the proposal is first agreed or determined under the Dispute Resolution Procedure.~~	provisions		
83.10.1	Authority to instruct	Where Clause 83.3A (*Maximum Annual Liability*) applies, the Authority may, within ~~[5]~~10 Business Days following agreement or determination of the Malicious Damage Rectification Programme or any amended Malicious Damage Rectification Programme instruct the Contractor in writing (copied to the FM Contractor at such address as may be notified to the Authority from time to time) to carry out the necessary repair, replacement or cleaning and following receipt of such written instruction the Contractor shall proceed to do so in accordance with the Malicious Damage Rectification Programme.	Change to reflect agreed timescales and arrangements for repairs and rectification	Acceptable	

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Grant Thornton

ALPHA SCHOOLS CONSORTIUM

HIGHLAND COUNCIL EDUCATION, CULTURE AND SPORTS SERVICES PPP2 PROJECT

FUNDING COMPETITION REPORT

JUNE 2004

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CONTENTS

Appendices

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1 INTRODUCTION

1.1 This document sets out the process undertaken in respect of the funding competition carried out by The Alpha Schools Consortium and its financial advisers, Grant Thornton, for the Highland Council Education, Culture and Sports Services PPP2 Project.

1.2 The document has been prepared by Grant Thornton for The Alpha Schools Consortium for the purpose of informing The Highland Council and ultimately The Scottish Executive PFU of the funding competition process which has been undertaken and should not be used for any other purpose.

1.3 Grant Thornton makes no representations or warranty as to the information contained herein and accepts no liability to The Scottish Executive, The Highland Council or any other party in respect of this.

1.4 The information contained within this document is private and confidential and should not be disclosed to any other party, other than those listed above, except with the prior written consent of Grant Thornton.

2 BACKGROUND

2.1 As required by the Highland Council's ITN, the Alpha Schools Consortium ('Alpha') undertook a funding competition to determine the best available funding terms for its bid. This process involved the consideration of senior debt and bond finance, subordinated debt and equity terms for the project.

A list of potential funders was developed by Alpha and Grant Thornton based on existing relationships and known willing funders.

2.2 Initial informal contact was made by telephone with the potential funders in the second week of April, stating estimates of the finance requirements and the potential different sources of funding being considered. After expressions of interest in providing senior debt, bond finance and/or equity were made verbally, copies of the Information Memorandum for Funders, the draft Project Agreement and the draft Risk Matrix were issued between 8 and 16 April 2004. Copies of the issued documentation have been attached as Appendices (Appendix I - IM for Funders.doc, Appendix II - HS PA Draft 1 v13.doc, - Risk Matrix as per Council ITN.doc).

2.3 Terms were sought for both standard and mandatory variant bids.

2.4 The funders approached were chosen for their perceived ability to provide finance in education projects of this size in the timescale required. The number approached exceeded those outlined in the original funding strategy document because the initial verbal comments from funders indicated there was an appetite to become involved in the project, and it was felt that better value could be obtained by widening the competition. The intention was to undertake an initial review of the funding terms and instruments offered by each to reduce the number of bidders, with the remaining funders terms being modelled to indicate which was preferable.

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2.5 The funders mentioned in the funding strategy document were merely indicative (hence why Quayle Munro and HSBC were not involved).

2.6 The following funders received Information Memoranda for the provision of funding terms

	Type of Instrument Offered	**Terms Received**	**Senior Debt Terms Considered Further**	**Bond/ Monoline Terms**
Royal Bank of Scotland	Senior Debt/ Equity	✔	✔	
Dexia	Senior Debt/ Equity	✔	✔	
HboS	Senior Debt/ Equity	✔	✔	
Lloyds	Senior Debt	✘ missed deadline	✘	
Barclays	Senior Debt/ Bond/ Equity	✔	✔	✔
DEPFA	Senior Debt	✔	✘	
Royal Bank of Canada	Senior Debt/ Bond	✔	✘	✔
AMBAC	Monoline	✔		✔
FSA	Monoline	✔		✔

3 RESPONSES TO INFORMATION MEMORANDUM FOR FUNDERS

3.1 Funding terms were received from all of the funders approached by 19 April 2004 with one exception. Lloyds terms were received late (26 April) and since the terms offered demonstrated no greater value for money than the others, Lloyds were excluded from the competition.

3.2 A summary of the original term sheets has been attached to this document as Appendix IV.

3.3 An initial review of the terms received concluded that within each of the funding instruments there was no one clear preferred funder in terms of value for money. Each bid offered benefits and drawbacks in terms of different requirements.

3.4 All of the funders approached made comments on the Council's Project Agreement. specific comments can be seen within each of the individual terms sheets received. These tended to be on funder specific issues which are the subject of ongoing discussions with the Scottish

Executive. Details of the issues raised were submitted as part of the legal commentary included within the ITN.

3.5 In order to limit the number of parties involved in funding the project, and therefore mitigate potential delays, it was concluded that it was best to take equity from the fewest number of equity providers possible. Initially, Alpha Schools believed that there may have been a lack of capacity within Noble and AWG to fund 100% of the equity requirement. However during the bid phase, both companies obtained approval from their Boards to provide 50% of the equity each. Therefore the requirement for a third equity provider was not required.

Senior Debt

3.6 The initial terms received collated and were compared by Grant Thornton and the Consortium based on experience and concentrating on those terms which would have the most significant effect on value for money. On the basis of this evaluation of the indicative terms supplied in the term sheets, the long list of potential senior debt/ equity funders was reduced to Royal Bank of Scotland, Dexia, HBoS and Barclays. Whilst the initial terms offered were competitive, there was very little to differentiate between these four offers.

3.7 Each of the remaining Senior Debt funders identified in 2.6 above was then contacted and asked to reconsider the parts of their terms that were considered to be off-market.

Bond Underwriting

3.8 Bond underwriting terms were sought from two sources, Barclay's and Royal Bank of Canada. Barclay's offered equity, but no bond as part of an EIB solution. Royal Bank of Canada did not offer equity, but did offer a bond as part of an EIB solution. For the bond solution, HBoS indicated that they would be interested in discussing bond finance if it was pursued, but offered no terms.

3.9 The terms offered by both Barclays and Royal Bank of Canada were competitive based on both Grant Thornton and the Consortium's experience of the current PFI market, and there was very little to differentiate them on economic grounds.

3.10 At the time of evaluating the bond solution, it had been agreed that AWG and Noble could between them provide 100% of the equity. Also it was felt that the involvement of EIB would be economically advantageous to the project. On the basis of this and the experience demonstrated by Royal Bank of Canada in providing bond underwriting within the Scottish PFI sector, it was therefore decided that if a bond solution was to be followed, the preferred provider would be Royal Bank of Canada.

Monoline

3.11 For the monoline, FSA and Ambac were asked to submit terms. Based on the current PFI market experience of the Consortium and Grant Thornton, the terms submitted were considered to be competitive. The preferred supplier was chosen as Ambac at this stage without re-consideration of terms. The two providers offered similar terms, with Ambac showing slightly more willingness to be flexible on cover ratios and reserve accounts. The Consortium had prior experience of working with Ambac, and was impressed by their flexibility and willingness to progress projects.

4 EVALUATION OF REVISED SENIOR DEBT TERMS

4.1 Revised terms were received from Royal Bank of Scotland (26 April) HBoS (23 April), Dexia (27 and 29 April) and Barclays (27 April) and are detailed in Appendix V.

4.2 The revised terms received from the short-listed senior debt funders were modelled assuming EIB involvement in funding, 50% of the senior debt requirement. Indicative terms had been received from the EIB prior to commencement of the funding exercise, and updated on 30 April 2004. At this stage of the process, only indicative project costs were available, and matters such as the length of construction period were still uncertain. As a result, the model used differed from the final models, but the same model was used to evaluate all funding terms.

4.3 A summary of the results of the modelling exercise is attached to this document as Appendix VI, along with the updated summary of all terms received, Appendix V. There remained very little difference between funding terms, but the terms offered by Dexia were marginally more beneficial in terms of the Unitary Charge than those of the other three shortlisted.

4.4 A number of evaluation criteria had been identified as part of the funding strategy. The evaluation considered which terms were most economically advantageous, deliverable, and flexible after financial close. Comments were also sought as to the involvement of the EIB, and any potential comments each funder may have on the Scottish Standard Schools Contract ("SSSC").

4.5 From the responses received, it was apparent that all funders approached were open to EIB involvement, although some terms offered did vary depending on whether the EIB were to be involved. Comments on the SSSC were also similar, and as noted above, centred on the general funding issues which have been the subject of discussions between the banking community and the Scottish Executive.

4.6 In terms of flexibility after financial close, the relationship with each potential senior debt provider was considered. Ultimately, however, each funder demonstrated a willingness to assist the project and this was not a distinguishing factor in the decision to appoint a preferred senior debt provider. Therefore, the decision was largely driven by the financial appraisal of terms offered and their deliverability, with Dexia providing the best value by a small margin.

4.7 Dexia was selected as preferred senior debt funder on 3 May 2004, with the other potential funding parties being informed of the decision over the following days.

4.8 The sole underwriting of the senior debt requirement was not a specific requirement of the funding IM, although representations on possible treatment were requested (Funding IM at 4.6). However, Dexia did offer the possibility of the sole underwriting as opposed to syndication and this was viewed as being preferential in the eyes of the Consortium. It was felt that this would remove any potential divergence of terms and funder management issues which can arise from the involvement of more than one underwriter.

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5 EIB INVOLVEMENT

5.1 The EIB has been involved in the project from an early stage. Initial terms were provided to the Consortium by the EIB in October 2003. These terms were purely indicative and were based only on a senior debt solution. However, subsequent meetings with the Consortium outlined general principles of EIB involvement (such as that they would not be seeking a third party guarantee, and would rank *pari passu* with other lenders).

5.2 The EIB also met with the Consortium on a number of occasions and were kept updated of the progression of the project. They indicated that they would have similar queries on the project agreement as the other potential funding parties, namely those being discussed with the Scottish Executive.

5.3 Revised terms were provided by the EIB on 30 April 2004. These included EIB terms for a bond finance solution.

5.4 The indicative terms provided by the EIB are not as detailed as those received from the other funding sources which were approached. The EIB is unable to provide any further detail until the appointment of Preferred Bidder.

6 CONCLUSIONS

6.1 The funder competition has been conducted in a rigorous manner with a clear audit trail. The funders approached were all recognised, experienced funders of PPP projects with the capability to deliver the deal.

6.2 All funders were given the same information to price their bids, underlined by the very close similarity of the terms received.

6.3 Certain funders, regarded as those offering the most attractive terms, were asked to clarify and resubmit their terms and these were then tested through the same financial model to determine which offered the optimal solution to The Alpha Schools Consortium and The Highland Council. The reconsidered terms submitted were more competitive and thus offered improved Value for Money to the Highland Council through a reduce Unitary Charge. It was on this basis that a senior debt solution funded by Dexia in the case of the standard bid submission and Dexia and EIB in the case of the mandatory variant bid submission was chosen.