

ABERDEEN CITY COUNCIL

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COMMITTEE	Council
DATE	16 December 2015
INTERIM DIRECTOR	Richard Ellis
TITLE OF REPORT	Scottish Futures Trust Delivery Model (Hubco)
REPORT NUMBER	CG/15/151
CHECKLIST COMPLETED	Yes

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1. PURPOSE OF REPORT

This report outlines changes to the Scottish Futures Trust (SFT) Hub Design, Build, Finance and Maintain (DBFM) delivery model that are required to reinforce the classification of these projects as private sector under ESA 10 rules.

2. RECOMMENDATION(S)

It is recommended that the Council:

- i) note the changes being made to the Hub DBFM delivery model;
- ii) agree to the Hub Shareholders Agreement and the Territory Partnering Agreement being amended to accommodate these changes;
- iii) note that all participants within Hub North Scotland Ltd must agree to the amendment of these agreements before any projects in the area can proceed to financial close; and
- iv) agree to provide delegated authority to the Head of Finance and Head of Legal & Democratic Services to resolve any unforeseen issues that may arise during the implementation of these changes.

3. FINANCIAL IMPLICATIONS

There are no direct financial implications arising from this report.

#### 4. OTHER IMPLICATIONS

Amendment of the Shareholders Agreement and Territory Partnering Agreements will enable projects within the North Hub area including the South of the City School to proceed to financial close thereby minimising any further delays due to ESA 10 issues.

#### 5. BACKGROUND/MAIN ISSUES

##### 5.1 Background

5.1.1 Changes need to be made to the structure for delivering Hub Design, Build, Finance and Maintain (DBFM) projects in order to reinforce the classification of those projects to the private sector for national accounts purposes under European System of Accounts 2010 ('ESA 10') rules and the accompanying Manual of Government Deficit and Debt 2014 ('MGDD'). A new hub DBFM delivery structure has been approved by Scottish Ministers and must be applied to all DBFM projects signed since the introduction of ESA 10 on 1<sup>st</sup> September 2014.

5.1.2 This report outlines the 4 key changes proposed to be made to the hub delivery.

##### 5.2 Reasons for the Changes

5.2.1 Private classification of DBFM projects for national accounts purposes is required for Scottish Government to support projects from long term revenue budgets rather than capital budgets as they are constructed.

5.2.2 The rules under which the national accounts are compiled are set in Europe and under ESA 10, and supporting MGDD, changes have been made to the rules applicable to the classification of projects delivered under public private partnership structures such as hub DBFM.

5.2.3 In order to reinforce the required private classification under the revised rules, Scottish Futures Trust (SFT) has identified that:

i) Any perception of public sector control over the delivery company (the sub Hubco under the existing structure) must be avoided. This is achieved through the restructuring of that company as a stand-alone DBFM co.

ii) Public sector financing of projects whether through subordinated debt or through capital contributions to projects must be limited in order to maintain clarity of risk transfer to the private sector delivery partner.

### **5.3 Details of the Changes**

#### **5.3.1 Changes to the Sub Hubco Delivery Company**

- 5.3.1.1 The existing structure has the project delivery company as a fully owned subsidiary (a sub Hubco) of the Hubco. Under the revised structure the procuring participant for a DBFM project will contract with a company that sits outside of the Hubco corporate structure (a “DBFM Co”) rather than with a sub Hubco as at present.
- 5.3.1.2 The DBFM Co will be owned 60% by the private sector development partner, 20% by a newly formed private sector charity, 10% by SFT and 10% by the procuring participant. A majority of the DBFM Co directors will be appointed by the private sector developer partner and so the board of the DBFM Co will be under private sector control.
- 5.3.1.3 The shareholders in DBFM Co will have the right to invest subordinated debt in proportion to their shareholding.

#### **5.3.2 Changes to arrangements for investing Subordinated Debt in projects**

- 5.3.2.1 Under the existing arrangements Participants have the right to invest up to 30% subordinated debt in their own and in other participant’s projects. Under the new structure this right to invest is limited so that participants have the right to invest 10% of subordinated debt in the DBFM Co delivering their own project.

#### **5.3.3 Setting Up of a new Charity**

- 5.3.3.1 A charity will be formed (currently referred to as the Hub Community Foundation (“HCF”)) to assist and enhance the delivery of the wider community benefits that are connected with the activities of the hub programme.
- 5.3.3.2 HCF’s purposes will be the advancement of education, the advancement of health, the provision of recreational facilities and the relief of those in need. It will be for the HCF’s board of trustees to determine the causes that HCF will support and therefore the public benefit that HCF will deliver.

- 5.3.3.3 HCF will be established as a Scottish Charitable Incorporated Organisation and its Board of Trustees will comprise:
- a) 1 trustee appointed by SFT;
  - b) 1 trustee appointed by the 5 hub private sector development partners; and
  - c) A majority (3-5) of trustees who have an interest in the hub programme and its objectives but are independent of the public sector and the 5 private sector development partners.

5.3.3.4 HCF's members will be the SFT, the 5 private sector development partners and the independent trustees.

#### **5.3.4 Capital Contributions to DBFM projects**

5.3.4.1 Under the existing arrangements Participants can make a capital contribution towards the capital costs of the DBFM project. This would reduce the amount of the Annual Service Payment payable by the participant over the term of the DBFM contract.

5.3.4.2 Under the revised structure there will be no public sector capital contributions.

5.3.4.3 Local Authorities which had planned to make capital contributions to DBFM projects will not be able to do so and will have to make an increased contribution to Annual Service Payments in respect of the element of the capital cost it was intending to contribute. The "no better no worse" principle will apply and Local Authorities will not be expected to contribute additional financing costs above those they would have incurred had the capital contribution been supported by PWLB borrowing.

#### **5.4 Implications for Aberdeen City Council**

5.4.1 The implications for the Council are:

- i) The Council as a participant in Hub North Scotland Ltd needs to formally agree to these changes; and
- ii) As the participant commissioning the South of the City School, the Council needs to be aware that these changes will apply to this project and need to be made before it can reach financial close.

## **5.5 Implications as a Participant in Hub North Scotland Ltd**

- 5.5.1 The Council needs to formally agree to these changes and consent to the Hub Shareholding Agreement and Territory Partnering Agreement being amended to incorporate these changes.
- 5.5.2 SFT have commissioned Pinsent Masons to draw up the documentation for these changes in each Territory and this work has already been completed.
- 5.5.3 In terms of any challenge to these changes under Procurement Law, SFT commissioned Pinsent Masons to review this risk and Pinsent's conclusion is that:  
"We [Pinsent Masons] are of the view that there are strong arguments as to why the Variation should not be considered to constitute a material change and whilst there is a degree of risk associated with the Variation, in our view the likelihood of success of a challenge on grounds of material change is relatively low. Further such risk could be mitigated by publication of a Veat Notice (subject to section 2.6.4(d))." The Veat Notice has been sent to OJEU for publication.
- 5.5.4 Resolution of this ESA 10 issue has been a major issue and blockage for the Scottish Government, SFT and Hubco in closing projects and developing new ones. Closure of projects has been on hold pending resolution of this ESA 10 issue.
- 5.5.5 The Office of National Statistics (ONS) have recently advised that the proposed changes to the Hub DBFM model would support a private sector classification in line with EU guidance and in light of this the Scottish Government has announced that projects can proceed to financial close.
- 5.5.6 At the time of writing it is understood that all other Participants in Hub North Scotland Ltd have already agreed the changes required.

## **6. IMPACT**

### **Improving Customer Experience –**

No direct impact arising from this report.

### **Improving Staff Experience –**

No direct impact arising from this report.

### **Improving our use of Resources –**

By agreeing to the recommendations as detailed in this report, the Council, as a participant in Hub North Scotland Ltd will be confirming that the required changes can be made to the appropriate legal documentation. This in turn will allow projects, including the South of the City School, within the Hub North area to progress to financial close. This will minimise any further delays resulting from ESA 10 issues and reduce the risk of additional costs being incurred as a result of such delays.

### **Corporate -**

As a participant in Hub North Scotland Ltd, the Council has made a commitment to work with SFT in the development of projects to provide new facilities within the City, such as the South of the City School. Such projects link clearly to the visions and plans of the Council.

### **Public –**

This report demonstrates to the public the frameworks within which the Council works and provides assurance that action is being taken to continue to work within those frameworks.

## 7. MANAGEMENT OF RISK

Failure to agree to and implement the required changes to the aforementioned legal agreements would delay the progress of projects and could have a negative impact on the Council's relationship with SFT and the other participants of Hub North Scotland Ltd. There could also be detrimental financial consequences for the Council as a result of further delays. These risks will be mitigated by the approval of the recommendations in this report.

## 8. BACKGROUND PAPERS

SFT Revised Documentation and associated Pinsent Mason's Advice Note

## 9. REPORT AUTHOR DETAILS

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