



LOCAL GOVERNMENT PFI PROJECT SUPPORT GUIDE (2008-09)

The Private Finance Initiative (PFI) enables local authorities to enter into a contract with the private sector for the provision of services involving new or improved capital assets. Support can be allocated by central Government departments towards the cost of the capital element of PFI projects. Local authorities taking out leaseplus agreements with LIFT companies may also be eligible for such support. Notification that grant will be paid, the conditions and the level of capital investment which will be supported are set out by issuing a "PFI credit" in the form of a letter from the sponsoring department.

This guide provides advice to those local authorities seeking central government support for PFI or LIFT projects. Those authorities who wish to formally submit a grant claim should consult the *Local Authority PFI Annuity Grant Determination (No 1) 2008 [No 31/1047]* or - if claiming grant on a declining balance basis - the *Local Authority PFI Declining Balance Grant Determination (No 1) 2008 [No 31/1048]*.

The guide is arranged as follows:

- Section A: Administrative arrangements for PFI credits
- Section B1: Endorsement letter
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- Section C: Qualifying criteria
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The method of calculating PFI grant is unchanged in 2008-09. The interest rate used in the calculation of grant, and the discount rate used in the calculation of PFI credits, is determined to be 5.5% for all projects endorsed in 2008-09, and 5.4% for all projects endorsed in 2009-10 and 2010-11. The scaling factor, which is used for all projects other than HRA projects, is determined to be 1.0 for all projects endorsed from 2008-09 to 2010-11.

SECTION A

ADMINISTRATIVE ARRANGEMENTS FOR CENTRAL GOVERNMENT SUPPORT

The following outline of arrangements applies to most PFI projects, but see Section A(5) below for differences in approach for Building Schools for the Future (BSF) and LIFT projects.

(1) First Approach

(1.1) Invitation to produce an OBC. The procedures for applying for central government support vary between departments. Some hold annual bidding rounds inviting Expressions of Interest / Strategic Outline Cases, whilst others will assess proposals submitted at any time. To reduce the risk of abortive work, authorities are recommended to check on the procedures and to discuss their proposals with the 4ps and the department concerned at an early stage. However proposals are received, departments will select those they wish to see proceed further. Authorities will be invited to produce an Outline Business Case (OBC) for those projects selected. Authorities should appreciate that a firm commitment on revenue support towards the costs of the PFI scheme cannot be given at this stage.

(2) Project Endorsement

(2.1) Outline Business Case. As well as any policy criteria, the OBC must cover all the criteria set out in Section C of this document. The OBC should always include as an Appendix a checklist indicating the paragraph numbers in the main documentation where information on each of the criteria is to be found. In drafting an OBC, authorities are advised to take account of the advice in the 4ps publication *The Outline Business Case*, the guidance in 4ps procurement packs, and departmental guidance.

(2.2) Assessment of the OBC. A first assessment will be undertaken by the sponsoring department – in some cases in conjunction with its relevant NDPB. If all criteria are met satisfactorily, and if the project is approved by Ministers (such approval may have already been given at an earlier stage), the OBC will be submitted to the PFI Project Review Group (PRG), seeking its endorsement. The formal PRG procedure takes a period of 5 weeks, following any departmental assessment. Endorsement of a project indicates that PRG considers that it (i) is sufficiently developed to be commercially viable / bankable; (ii) has demonstrated that PFI is the best value for money procurement route; (iii) is affordable, taking account of the agreed level of PFI credits; and that the authority (iv) is committed to the use of standard contract conditions and to good quality design; and (v) has the strategy and capacity to undertake the procurement. A project that is not endorsed at a meeting may be invited to do more work in particular areas and return for re-consideration.

Further guidance on PRG procedures can be found in the PRG Code of Practice, available on the Treasury website¹.

(2.3) Endorsement letter. If a project is endorsed by PRG, the sponsoring department (or major department in the case of a jointly sponsored project) will send a formal endorsement letter (the template at Section B1 provides a framework, and in some circumstances options, although each letter will be tailored to meet the specific needs of each sector and project – this will be especially so for BSF or LIFT projects). This letter will include standard and specific conditions, and set the endorsement date which is used to determine a number of rates used in grant and PFI credit calculations. Some conditions may need to be met before the project is taken to the market. A project with such conditions is nonetheless considered endorsed at the date of the relevant PRG meeting.

(2.4) Publication of the OBC. Authorities are urged to publish their OBC (bar commercially confidential information) on their website as soon as possible after endorsement. Some sponsoring departments will require the publication of the OBC as part of their funding commitment.

(3) Procurement to Preferred Bidder

(3.1) Value for Money. Throughout procurement local authorities are expected to undertake Stage 3 of the Treasury standardised Value for Money (VfM) assessment procedure², and report any problems to the relevant sponsoring department.

(3.2) Additional Support or Reduced Outputs. Although the aim is to avoid such a situation, in some cases a project may prove to be unaffordable as set out in the OBC. In such cases a request for additional support and/or a reduction in outputs/ benefits (“de-scoping”) may be proposed (note: de-scoping should not be confused with innovation where the outputs/benefits are achieved in a more efficient way). In general both approaches are bad practice - the project will generally have been prioritised because it delivered a certain set of benefits for a certain cost, i.e. it was better VfM (in its broad sense) than other projects. A change in the VfM could bring into question the original decision. However, in some cases a department may conclude that the revised project remains VfM and a decision on the balance of additional support or reduced outputs needs to be made by the sponsoring department, in the context of both the project and the overall programme.

If the increase in PFI credits is over £10 million or 20%, whichever is the lower, that project will also need to be re-submitted to PRG for further approval. If the increase is below that level, but there is any indication that the request has been deliberately engineered to avoid the limit, then the sponsoring department is advised to consider whether it should nonetheless still approach PRG for advice. Where reduced outputs are concerned, it is likely that quantification will be more difficult, but to the extent possible a reduction of more than 20% should

¹ www.hm-treasury.gov.uk/media/EED/C7/PRG_Code_of_Practice_v2.0.pdf

² www.hm-treasury.gov.uk/documents/public_private_partnerships/additional_guidance/ppp_vfm_index.cfm

be treated in the same way as a similarly sized increase and the scheme referred to PRG for advice.

(3.3) Final Business Case. Where a project is being procured using the competitive dialogue procedures, the authority should submit a Final Business Case (FBC) for agreement by the sponsoring department, prior to selecting a preferred bidder. The FBC should provide re-assurance that the project continues to support the aims and outputs approved at OBC, and that the procurement process has been such as to ensure VfM. The FBC should set out any proposed derogations to the standard contract conditions for each 'final tender' being assessed by the authority and these need to be agreed with the sponsoring department. Any post-preferred bidder risks should be highlighted.

Older projects which are not using the competitive dialogue procedures should submit their FBC, which should cover the same issues, before financial close but when confident that there will not be further significant changes to the project. In such cases, the authority should also ensure that any derogations to the standard contract conditions have been agreed with central government before it appoints the preferred bidder.

(3.4) Second stage reviews. Selected projects (whether using the competitive dialogue procedures or not) will be required to undertake a Second Stage PRG review prior to selection of the preferred bidder. This will examine proposed derogations from standard contract terms for each 'final tender' being assessed by the authority as well as the continuing VfM and affordability of the project.

(3.5) Promissory note. A promissory note (template at Section B2 – note that the comments about the endorsement template at para. 2.3 above also apply to this letter) does not need to be sent at any particular stage if the authority does not require it, but may be requested to provide assurances about the continued support in principle of the department if that is needed.

(4) Contract signature

(4.1) Contract signature target date. A target date for the project to reach financial close will have been agreed between the local authority and department and recorded in the endorsement letter. Should that target date be missed, any possible action will be a matter for the sponsoring department. Authorities are urged to alert departments as early as possible if that seems likely to happen.

(4.2) Confirmation of Financial Close. The authority should send written notification of the date financial close is reached, together with a short record of any changes to the case as set out in the FBC. In considering the latter, departments will bear in mind the requirements of competitive dialogue.

(4.3) PFI credit letter. A PFI credit letter (template at Section B3 – note that the comments about the endorsement template at para. 2.3 above also apply to this letter) will always be sent by the sponsoring department when the project

reaches financial close. This letter is the formal date at which a PFI credit is issued, and is the record of all factors used in calculating PFI grant.

(4.4) Publication of the FBC. Authorities are urged to publish their FBC (bar commercially confidential information) on their website as soon as possible after financial close. Some departments require publication of the FBC as a condition of PFI funding support.

(5) Building Schools for the Future (BSF) and Local Improvement Finance Trust (LIFT) projects.

(5.1) BSF. BSF projects receive endorsement from a separate panel, rather than PRG, but the purpose is essentially the same. This panel - the Main Review Meeting (MRM) – is chaired by Partnerships for Schools (PfS) with attendees from the Department for Children, Schools and Families (DCSF), Partnerships UK (PUK) and HM Treasury. Standard letters are significantly different, particularly as approval is for more than PFI, also covering Design & Build and ICT. As PRG is not involved in endorsement there are no second stage reviews, but PfS provide constant monitoring and liaise as necessary with PUK and HM Treasury.

(5.2) LIFT. Unless advised otherwise by the sponsoring department, the above procedures apply to LIFT projects, both during initial procurement and later phases / tranches of work. Some variations for projects involving a leaseplus agreement with a LIFT Company are set out in Section I of this Guide.

SECTION B1

ENDORSEMENT LETTER

I am writing to inform you that consideration of the outline business case (OBC) you submitted on *[date]* for the *[name of project]* PFI project has been completed. I am pleased to be able to tell you that your project was endorsed by the Project Review Group (PRG) on *[date]* as ready to enter into procurement *[subject to the conditions set out below]*. We expect that central Government revenue support will be given based on PFI credits of *[£... million]*. *[For jointly sponsored projects: This comprises £... million from ... and £... million from ... This department will be the lead sponsor for your project.]* Your scheme should be developed so that it is affordable within this offer.

Conditions

Support for this project depends on the project continuing to meet all the published criteria in the Department for Communities and Local Government *Local Government PFI Project Support Guide*, available at www.local.communities.gov.uk/pfi/pfigrant.htm. In particular, you are reminded of the requirements on the use of standardised contract documentation; and on sharing documentation, including publication of your OBC (barring any sensitive information) on your website as soon as possible.

[Departments should set out any conditions imposed by PRG and any that they may wish to add].

This letter is without prejudice to any other consent that may be required, for example, in connection with planning legislation.

Procedures

Please keep in touch with us about the progress of your project during procurement.

In particular, you must inform us immediately if you wish to change aspects of the project in any material way from the case agreed. That particularly includes changes to the outputs, need for PFI credits, or the timetable, where we have agreed that you are aiming to reach financial close by *[date]*. If changes are required to any of these aspects of the project you will need to obtain the Department's written agreement in good time before the contract is signed. Failure to obtain any of these could potentially mean withdrawal of support for the project, and would invalidate any undertaking by the Department or PRG to support your scheme.

You should send a Final Business Case (FBC) to this Department before you select a preferred bidder. The FBC should provide re-assurance that the project continues to support the aims and outputs approved at OBC, and that the procurement process has been such as to ensure VfM. It should set out any proposed derogations to the standard contract conditions for each 'final tender'

being assessed by the authority and these need to be agreed with the sponsoring department. Any post-preferred bidder risks should be highlighted. A number of projects will also be selected for a second stage review by PRG and you will be notified in due course if your project is selected.

We will formally issue PFI credits on the basis of a letter confirming the date financial close was reached and reporting any post-FBC changes. In doing so we will provide you with details of how and when revenue support can be claimed *[as set out in the Local Government PFI Annuity Grant Determination for the financial year in which grant is first claimed.] [as HRA Subsidy.]* The interest rate which will be applied in calculating grant for your project will be ..%, and the scaling factor ... Your authority will need to ensure that funds are available to cover that part of the payments to the contractor which will not be met by central Government.

You will be eligible for grant when *[the [first] permanent asset is completed, which should be taken to mean ...][responsibility for the maintenance of assets is transferred]. [If PFI credits are to be phased this must be set out, citing the level of PFI credit for each phase and when support for each will start].*

Revenue support is not intended to match or correlate directly to the payments that arise under a PFI contract. However, the Government is committed to supporting good PFI projects and to assisting the development of PFI in the local authority sector. Its policy is therefore to maintain revenue for PFI projects in the long term, consistent with the long-term nature of PFI contracts, even though formally such support cannot be guaranteed.

SECTION B2

PROMISSORY NOTE

I refer to our earlier correspondence letting you know that the Project Review Group had endorsed this project. I note from your letter of *[date]* that your project continues to meet the relevant published criteria and the conditions set out in the endorsement letter of *[date]*. I confirm that if the transaction were entered into on these terms, this Department would issue your authority with a PFI credit letter for an amount of *[£... million]*. *[This includes £... million provided by [other department].]*

All terms, and eligibility for grant, are as set out in the endorsement letter *[and subsequent letter(s) of [date(s)]]*. *[If there have been any changes agreed to the scope or PFI credits, these should be referred to.]*

You should continue to seek prior approval if, between now and contract signature, different terms are negotiated which affect either the nature of the scheme or the potential amount of the PFI credit, or if those terms differ from those in the relevant PFI standardisation documents. Any departure from these terms could affect your authority's entitlement to PFI credits, and will in any case risk delay to the project if PRG decides to have the proposed departures reviewed. Should we wish to support the revised project we would issue a further letter.

SECTION B3

PFI CREDIT LETTER

Thank you for confirming that financial close was reached on the above transaction on *[date]* and that the contract was agreed on the terms set out our letter(s) of *[date(s)]*. This completes the documentation needed by this Department to formally issue PFI credits for this project for an amount of *[£... million]*. *[This includes £... million provided by [other department].]*

You are required to send a copy of the signed project agreements in electronic form to: PFIcontracts@hm-treasury.gsi.gov.uk. This will be used for compliance monitoring purposes. You should also publish your FBC (barring any sensitive information) on your website as soon as possible.

You will be eligible for grant when *[the [first] permanent asset is completed, which should be taken to mean ...][responsibility for the maintenance of assets is transferred]*. *[If PFI credits are to be phased this must be set out, citing the level of PFI credit for each phase and when support for each will start]*.

Revenue support will be paid once a valid claim form has been received, *[as set out in the Local Government PFI Annuity Grant Determination for the financial year in which grant is first claimed.] [as HRA Subsidy.]* The interest rate which will be applied in calculating grant for your project will be ..%, and the scaling factor ... Your authority will need to ensure that funds are available to cover that part of the payments to the contractor which will not be met by central Government. More information on PFI grant, is available in the Department for Communities and Local Government *Local Government PFI Project Support Guide*, available at www.local.communities.gov.uk/pfi/pfigrant.htm

Revenue support is not intended to match or correlate directly to the payments that arise under a PFI contract. However, the Government is committed to supporting good PFI projects and to assisting the development of PFI in the local authority sector. Its policy is therefore to maintain revenue for PFI projects in the long term, consistent with the long-term nature of PFI contracts, even though formally such support cannot be guaranteed. Termination or variation of a PFI contract would not in itself lead the Government to reassess the level of revenue support, although that would depend on the extent to which the anticipated capital investment had occurred.

SECTION C

QUALIFYING CRITERIA

To qualify for support a project must demonstrate in its OBC that it meets the following qualifying PFI criteria. An OBC will also wish to demonstrate how the project contributes to general government objectives such as diversity, cohesion and empowerment.

(1) Outputs

(1.1) Output specification. The OBC should include a first draft of an Output Specification which should be set out as a clear definition of the objectives and outputs needed, with the standards required (rather than particular assets or solutions). This is a key characteristic of PFI contracts and allows for innovation and efficiency on the part of the private sector. The specification should be based on best practice and precedent from similar projects, and be consistent with affordability assumptions. An illustrative solution will generally be needed in order to undertake the necessary financial analysis, but it should be clear that this does not constrain the final solution.

(1.2) Planning and performance framework. Projects must be consistent with and flow from the authority's plans and priorities, including Best Value Performance Plan and Community Strategy, the Capital Strategy and Asset Management Plan and/or the relevant strategic service plan.

(1.3) Sustainable development. Projects must demonstrate an integrated approach to the social, environmental and economic well-being of the area, now and for future generations, in line with the OGC guidance note *Green Public Private Partnerships*. This covers the promotion of sustainable development in location, design, construction, operation and maintenance.

(1.4) Design quality. Where relevant, projects must show that they contribute to the Government's commitment to achieving "Better Public Buildings". Evidence could include the possible appointment of a 'design champion'; involvement of stakeholders; use of Design Quality Indicators (available from Construction Industry Council); use of expert advice on design (including any involvement with CABE); and the extent to which design quality will be a key evaluation criteria for bidders. If the project involves construction work and life-cycle maintenance of buildings authorities should demonstrate how they intend to meet, as appropriate, the key objectives of the Egan Report. Authorities are expected to take account of the latest guidance on design quality in PFI projects available from OGC, CABE and 4ps. In some areas there may also be sector specific guidance.

(2) Options Appraisal

(2.1) Project options. Projects must show that they are value for money, firstly in terms of a project scoped to best meet the needs and outputs identified. An OBC will therefore often include a cost/benefit analysis of the various options to

demonstrate why the approach proposed was chosen. The methodology used should be in line with the Treasury guidance *Appraisal and Evaluation in Central Government* (the 'Green Book').

(2.2) Procurement options. Value for money must also be shown in relation to the best procurement option. This should be done using the Treasury standardised VfM assessment procedure³. This includes both qualitative and quantitative elements, which should both contribute to informing a wider judgement. Local authorities need to include a Stage 2 project assessment in the OBC, which will build on the Stage 1 programme assessment produced by the relevant sponsoring department. They should comment on any areas where their assessment differs from the general programme assumptions. Authorities should detail the sources of their information, and provide supporting material such as benchmarking against similar projects. The data used should be consistent with that used in other financial models.

(3) Affordability

(3.1) PFI payments. The authority should submit financial models which set out the projected PFI service payments (the “unitary charge”) for the reference project. These should show basic capital and revenue inputs, funding and timing assumptions. All financial models included in an OBC should be signed off by advisors.

(3.2) Sources of funding. The models should use the projected costs to derive the PFI credit amount requested as detailed in Section D of this Guide. Again, all inputs, assumptions and calculation methods used should be set out. Other sources of funding must also be detailed. That includes assumptions on third party income and funding by partners (see also para 6.1). Any capital contributions planned should be exceptional, and an explanation of why they are necessary and how the risks involved would be mitigated must be provided.

(3.3) Affordability. Payments should be shown alongside funding sources over the whole life of the contract (including also any interest earned on grant received in excess of that year’s payments). The level of payments which the authority will have to meet itself (sometimes referred to as the “affordability gap”) which this reveals must be accepted by members, senior management and budget holders. This should be done by reference to formal minutes. That commitment must take account of sensitivity analysis on factors likely to change.

(4) Contract

(4.1) PFI contract. A project contract must be based on accepted standardised contract documentation. With the exception only of LIFT projects, this will be *Standardisation of PFI Contracts* (SoPC), as well as recognised sector specific guidance, including Building Schools for the Future contracts and 4ps procurement packs. The version used, any addenda, and possible agreement

³ www.hm-treasury.gov.uk/documents/public_private_partnerships/additional_guidance/ppp_vfm_index.cfm

to any derogations, should comply with the most recent instructions issued by HM Treasury.⁴

(4.2) Payment mechanism. As a result of following the standard contracts noted above, eligible projects will be structured so that the transaction includes payment of fees at annual or more frequent intervals. In most cases payments should not be made until works have been completed and accepted, and the level of payment will at least partly be determined by performance standards or usage. Although up-front capital payments may in some exceptional cases be value for money, these must be agreed with HM Treasury at an early stage.

(4.3) Risk register. Projects must supply an acceptable risk register (risk allocation) making a preliminary allocation of all the foreseeable risks associated with the scheme between the parties. This should follow standard form guidance including sector specific guidance where relevant such as 4ps procurement packs.

(4.4) Indemnity or guarantees. No indemnity or guarantees must be given by the authority to any person in respect of any liabilities of the contractor with whom they enter into the contract (whether those liabilities were incurred in respect of the contract or otherwise).

(5) Accounting Treatment

(5.1) Use of Financial Reporting Standard (FRS) 5. A project must be considered a PFI contract under standard accounting requirements. FRS5 provides the basis for determining whether projects should be accounted for as a PFI contract or as akin to a lease - when Statement of Standard Accounting Practice (SSAP) 21 should be applied. The determination is based on whether or not there is an associated service element which is not independent of payments for the property.

(5.2) Balance sheet treatment. Central Government has announced that it will be moving to International Financial Reporting Standards (IFRS), which will affect the way in which PFI assets are accounted for on the balance sheet. However, these new arrangements are not yet in place, and until a further announcement is made, authorities will need to provide an "initial view" of the accounting treatment as set out in Section 2 of *Technical Note No. 1 (Revised) How to Account for PFI Transactions (June 1999)* available from the Treasury web site. The initial view must be supported by comments from the authority's external auditor as to whether it is reasonable. Should it appear likely during or after procurement that the initial view is likely to change, the sponsoring department should be notified immediately.

(6) Deliverability

(6.1) Project Director. The Project Director plays a key role in delivering the PFI/PPP project, and is therefore considered the most critical appointment to

⁴ www.hm-treasury.gov.uk/documents/public_private_partnerships/ppp_standardised_contracts.cfm

the project. The Project Director should be 'empowered' to do the deal, and the seniority of the person appointed will need to reflect the complexity of the project and the local authority's decision making structure. For most PFI projects, the Project Director will be supported by a Project Manager and a multi-disciplinary project team. Depending on the project and team, either the Project Director or Manager plans and allocates responsibilities for the project's tasks and development as part of the project methodology and takes day-to-day responsibility for leading and managing the development, procurement, execution and delivery of the project. They will be responsible for leading the discussions and 'competitive dialogue' with bidding consortia.

(6.2) Project team. The project director should be supported by a properly resourced project team with project management experience and the necessary range of skills and experience relevant to the project. This experience needs to be demonstrated in the OBC. The team need to be working within a suitable project management structure, which should be outlined with specific reference both to reporting lines to the project board and members; and to the delegation of suitable powers to allow effective management of the project. The project will be expected to be accessible to the involvement of the 4ps and departments.

(6.3) Sponsorship and support. Projects must have support from all key sponsors (such as Councillors and Senior Officers) and other stakeholders such as School Governors. A project owner or 'local champion' who will be sufficiently well placed to promote and pilot the project and drive it to successful implementation should be identified. Typically this would be the Director for the relevant service area, the chief executive, or the executive member who has the authority to negotiate and ensure that the project is completed. There must be an effective communications strategy to liaise with all interested groups and keep them informed of progress / key decisions. Where affordability depends on funding from other parties, commitment by those bodies to the levels set out in the affordability assumptions must be demonstrated.

(6.4) Commercial interest. A project must be able to show evidence of commercial interest. The authority should set out its approach to market sounding exercises, and provide evidence of the number of organisations contacted and their response. If there are likely to be factors which might hinder a good competition (e.g. geographic or sector related) these should be addressed.

(6.5) Internal Risk Register. A register should be included identifying all the risks to be managed by the public sector during procurement, ranking them in order of importance, and assigning risk owners and mitigation strategies. There should be regular reporting of risk management to the project board and a process to regularly update the risk register. If there have been any recent gateway reviews to inform the register, information on this should be included.

(6.6) Advisors. A project will need to demonstrate that suitable advisers are in place (or, if not, when they will be), with the necessary funding. These are likely to need to cover technical, financial, legal, and insurance. If the authority is using in-house resources they should demonstrate that they are suitably skilled and experienced. For external advisors, the terms of appointment should be

detailed (including requirements to share information, and arrangements for periodic review), and - if already appointed - their relevant sector specific experience.

(6.7) Timetable. A timetable should be prepared covering all stages from submission of the initial proposal to start of service provision, bearing in mind that the process has changed recently under the competitive dialogue procedure. In particular a realistic deadline should be proposed to reach contract financial close, with stages of the procurement process kept to a minimum consistent with achieving value for money. This should be consistent with the model procurement timetables in 4ps procurement packs. Authorities are advised to ensure that the timetable and affordability assumptions are consistent.

(6.8) Statutory processes. The impact of statutory processes such as planning permission, public enquiry etc. on the project must have been considered. Processes should either be complete or an authority will need to indicate how any potential problems will be resolved in the procurement process. That should include any risk mitigation strategy, a consideration of the potential impact on the timetable, and a description of consultations possible at the stage reached. An authority should consult with the relevant sponsoring department and follow any additional guidance which may be available on what is expected on planning and site issues before a project goes to the market.

(6.9) Sharing of Information. The local authority must confirm that they will be ready to share experience and contract documentation throughout and at the end of procurement, at no cost, with other local authorities procuring similar projects, with Government departments, their agents and with the 4ps. This information will be held as confidential, but any information of genuine commercial sensitivity (which is expected to be minimal) may be withheld. Authorities should make clear to potential contractors that this information-sharing requirement is a formal condition imposed by the Government as a condition of support.

(6.10) Operational phase. The authority should show that it has a strategy to ensure a smooth transition from procurement to the operational phase of the project; and that sufficient resources will be available to allow for adequate monitoring of the operational contract. Authorities are advised to refer to the Operational Taskforce Note *Project Transitional Guidance*⁵.

⁵ www.hm-treasury.gov.uk/media/2/3/pfi_projecttransition_210307.pdf

SECTION D

CALCULATION OF PFI SUPPORT

PFI support is intended to be a contribution towards that portion of contract payments which could theoretically be attributed to the capital investment being undertaken - that is, the portion which would be classified as capital expenditure under Section 16 of the Local Government Act 2003 if the asset had been procured traditionally, rather than by PFI.

(1) Scope of Project

(1.1) Reference Project. The PFI credit amount is generally agreed at OBC stage. In some cases a sponsoring department may revisit the calculation later in the procurement process, but that is not a general requirement. The final design will not be available at OBC stage, and authorities will generally develop a reference project on which to base costs, although in some sectors that will be done by using a funding model or toolkit. All parties wish to see limited increases in costs, including in the level of PFI credit after the OBC is endorsed, which means that it is important for the reference project to be as close to the final one as possible (without limiting the scope to innovate to reduce costs). See also Section A(3.2) on making changes in order to make a project affordable.

(1.2) Shared accommodation. In some accommodation projects, the local authority may share a building with another body. In such cases, the full costs should be split between the occupiers according to the relative proportion of usable space - the PFI credits may therefore cover a proportion of shared space, circulation, plant, etc.

(1.3) Associated work or receipts. It should be noted that the PFI credit can only support the capital value of the PFI contract itself. It cannot cover associated works under other contracts, even if these are linked as part of a broader project (for example, purchase of land by the local authority for subsequent transfer or sale to the PFI contractor). There may also be associated receipts as a result of the sale of assets released by the project. Authorities are required to notify the sponsoring department at an early stage about these and agree how they should be used. Under BSF this is covered by a sharing mechanism.

(2) Standard Approaches to PFI Credit Calculation

(2.1) Toolkits. In a number of sectors, including schools and housing, the sponsoring department has a standard approach to calculating the level of capital investment which will be supported and provides a toolkit for completion (in the case of BSF the Funding Allocation Model (FAM) covers more than just PFI). In most cases they follow the same general principles as discussed below, although street lighting projects are based on the difference between the capital costs of the PFI option and the 'do minimum' option over

the first 5 years - more detail is available in the 4ps street lighting procurement pack.

(3) Non-standard PFI credit calculation

The steps necessary to calculate the maximum PFI Credit permissible are as follows:

(3.1) NPV of unitary charge. The starting point for a sponsoring department in deciding on the level of support to offer is to calculate the NPV of the annual unitary charge over the anticipated life of the contract. To determine the NPV, the annual nominal (cash) costs should be discounted by the prescribed PFI discount rate for the financial year in which the OBC is expected to be endorsed by PRG (NOT at 3.5% + RPI). The prescribed discount rates for 2008-09 to 2010-11 are set out on page 1 of this document. The discounting should use the anticipated start date (see below) as the base date. The first 12 months of payments should therefore be Year 1, rather than actual or financial years.

(3.2) Revenue abatement. As noted above, PFI support is only for the capital element. There needs therefore to be a means of determining what proportion of the total NPV can be classified as capital, and what proportion revenue. This is referred to as the 'revenue abatement' figure. In some sectors, sponsoring departments may have agreed standard prescribed figures for this. For example, some accommodation projects (but not all) have used a revenue abatement figure of 30%, i.e. 70% of the total NPV is assumed to be capital and 30% revenue. Separate figures exist for some types of transport project, and authorities should consult departments for guidance on these standard revenue abatement figures.

However, in some cases the prescribed 'abatement' figure may not be appropriate, or there may not be one for the particular type of project (possibly because projects are one-off in nature). In these cases, a project specific revenue abatement figure needs to be calculated. To do this, the local authority needs to estimate how much of the regular unitary charge payments will be used to finance the various components of the project. Note that this means that it is the funding costs of the initial capex (interest and repayment of principle of the initial loans) which are being estimated, rather than the initial capex itself.

Each component of the unitary charge can then be identified as either capital or revenue. Classification will be determined by general accounting practice, but the following gives a broad indication of the likely results. Some of the costs are entirely capital and others revenue (although judgements between lifecycle (capital) and hard FM (revenue) will be less clear cut). Other costs are more generalised and relate to the project as a whole. The following gives a broad division, and any doubts should be resolved with the sponsoring department:

Capital:

Funding costs (i.e. principal and interest of senior and subordinated debt that has been used to fund initial capex (inc. prelims, fees, design, construction insurance, asset purchase, etc))

Lifecycle costs and any other capital costs not funded from debt, inc. that funded by equity

Revenue:

Soft FM (cleaning, security, etc)

Hard FM (buildings and grounds maintenance)

Utilities (if in the unitary charge, not a pass-through cost)

Buildings insurance (if in the unitary charge, not a pass-through cost)

General:

SPV set-up, overheads and running costs

Tax

Note that if utilities costs and/or building insurance are treated as a pass through cost, they will be excluded from the initial calculation above of the NPV of the unitary charge.

Since the general costs are incurred in respect of the entirety of the services and the project, it is difficult to say that they are all definitely “capital” or “revenue”. Consequently they can be disregarded when calculating the 'revenue abatement' figure, which is instead the proportion of definitely capital items compared to definitely revenue.

| | | |
|----------|--------------------------|-------------------|
| Example: | NPV of unitary charge = | £60m |
| | NPV of Capital element = | £30m |
| | NPV of Revenue element = | £10m |
| | NPV of General element = | £20m |
| | Revenue abatement = | 25% (£10m / £40m) |
| | PFI credit amount = | £45m (£60m - 25%) |

In some cases, the total project costs may be partly funded from capital contributions. If that is the case, these contributions must be considered to fund the capital element only. As a consequence the balance of capital to revenue funded via the unitary charge will be somewhat different to the balance for the project as a whole, and this should be borne in mind when calculating the revenue abatement figure.

(3.3) Project receipts. If local authority assets are transferred as part of the project, this would normally be expected to be done in exchange for a reduced unitary charge. If that is the case, notional receipts do not need to be included in the PFI credit calculation. However, if the authority receives an actual payment for such assets, the amount should be deducted from the PFI credit amount to reflect its use in reducing the costs of the project rather than being used elsewhere in the authority. This removes any perverse incentive to

pursue such a route unless it should be better VfM. Note that this is different to receipts from related assets (see 1.3 above).

(3.4) Residual value. In a few cases, most specifically non-HRA housing and LIFT projects, the asset becomes the property of the private sector contractor at the end of the contract period. In such cases, the unitary charge is less than it would otherwise be as there is a presumed residual value with the Contractor that will help meet part of the costs of the project. Under LIFT there may be an arrangement for the local authority to purchase the asset at the end of the contract, and in these cases, PFI credits can be issued to cover these costs.

(4) Final PFI credit award

(4.1) Offering less than the maximum. It is for the sponsoring department to conclude, based on the details of the project and the needs of its whole programme, whether to offer the maximum total capital value - calculated as set out above - or a lesser amount. If a lesser amount is offered consideration needs to be given to affordability, i.e. how the local authority might fund the balance.

(5) Increases in PFI credits

(5.1) Discount rate. Projects seeking an increase in PFI credits should recalculate the PFI credit amount by discounting at the rate in force when they that project was originally endorsed or, for those endorsed prior to 2005-06, a rate of 6.3% (see Section E (4) for the matching treatment of the interest rate used).

SECTION E

CALCULATION OF PFI GRANT

(1) Annuity PFI grant. Most PFI projects now receive grant calculated on an annuity basis. The following description of the way in which that will be calculated is intended to supplement and interpret, but in no way to override the express terms of the formal 2008 determination - the *Local Government PFI Annuity Grant Determination (No 1) 2008 [No 31/1047]* - available at www.local.communities/pfi/index.htm.

(2) Annuity calculation. A formula is provided in the determination as the means of calculating the annual annuity grant payments. However, in practice this can be done by using the Excel PMT spreadsheet function. The annuity calculation includes some simplifying assumptions:

(2.1) the interest in the annuity is calculated annually, using the opening balance to calculate interest for the whole year, even though payments are quarterly.

(2.2) the length of the annuity is based on the mid-month points for the start and end dates rather than being accurate to the day. This is consistent with the way in which the level of grant is calculated in the first and last years.

The latter point does mean that the period assumed in the calculation will not always exactly match the contract length. However, that is more than outweighed by the assumption at 2.1 above.

(3) PFI credit 'uplift'. The opening balance will normally be the PFI credit figure agreed between the sponsoring department and the authority. It should be noted that this will be the exact figure quoted in the PFI credit letter.

However, in some older cases "uplift" is applied as described in the determination. This was intended to compensate for discounting applied to years between contract signature and service commencement, since contract signature was originally used as the base date for discounting. After 1 April 2002 the discounting methodology changed so that service commencement was used as the base date. "Uplift" is now only applied to those projects where the original contract signature base date was used. That will be those projects endorsed by the PRG before 1 April 2002; but also some schools projects endorsed later. In the latter cases confirmation will be sought from the sponsoring department that the final PFI credit figure (whether determined in the OBC or at a later agreement to an increase) was calculated using a contract signature base discounting date.

(4) Interest rate and scaling factor. The interest rate and scaling factor for new projects will be set as that in force when the project was endorsed, as recorded in the endorsement letter sent by the sponsoring department. For all projects endorsed prior to 2005-06 an interest rate of 6.3% will be used. The

rate will not change if there is a subsequent increase in PFI credits agreed, (see Section D (1.3) for the matching treatment of the discount rate used).

The interest rate matches the interest rate for the debt charges element of RNF in the financial year in which the project is endorsed, the main difference being that the rate does not vary for any particular project during the period it is paid grant. A scaling factor was introduced for PFI annuity grant in 2005/06, with a maximum rate of 1.0.

(5) Disputes. Any disagreements over any relevant factors, inc. most commonly contract signature dates, must be resolved between the authority and the sponsoring department.

(6) Variations. If a post-contract signature variation is agreed and the sponsoring department agrees to support that variation, a separate PFI credit letter will be issued. There will be a separate calculation of PFI grant payment as if it were a new project. The discount and interest rates, and scaling factor used, will be those in force when the variation is agreed, not those used for the original project, and all support will be paid via annuity grant.

(7) Contract signature. In all cases contract signature is taken as that recognised in the PFI credit letter. For most projects now that is taken to mean financial close, and the concept of 'commercial close' is no longer used. This does not matter in terms of the interest rate. However, it is acknowledged that it will still have an impact on those older projects which may still be eligible for PFI credit uplift.

(8) First and last years. Grant is reduced in the first year so that a proportion of a complete financial year's grant is paid based on the month in which start date is reached. The calculation assumes a mid-month point so that a project starting in March will attract 1/24th grant (i.e. ½ month), one starting in February 3/24th grant (i.e. 1½ months), etc. Grant will also be reduced in the final year, using the same method.

(9) Phased projects. Where there is more than one phase of a project (see Section F(2)), each phase will be treated as if it were a separate project for the purposes of calculating grant.

(10) Declining balance grant. When PFI annuity grant was introduced in 1 April 2005, operational schemes and those which had reached ITN were given the option of continuing to receive grant under the previous declining balance grant regime. Projects which opted for declining balance at the time may still chose to switch to annuity grant at any time, but a switch in the opposite direction is not permitted. Payment of PFI declining balance grant will therefore be restricted to schemes in the local authorities listed in the *Local Authority PFI Declining Balance Grant Determination (No 1) 2008 [No 31/1048]*. The methodology for this grant has not changed since 2006-07.

(11) HRA grant. There is no determination specifically setting out the calculation of the grant for HRA PFI schemes. The basic methodology is,

however, the same as for PFI annuity grant with the exception that there is no scaling factor.

SECTION F

SUPPORT START DATES

(1) Start date

(1.1) New asset(s). When agreeing the value of the PFI credit sponsoring departments must, in addition to the value of the PFI credit being awarded, state how the "start date" will be recognised, i.e. when the authority will become eligible to claim PFI grant for that project. This should be when the asset becomes operational, defined as completion of acceptance testing or equivalent. For BSF projects it is referred to as the "services availability date". It should not be determined by payment to the contractor for interim services or temporary assets (e.g. site security or assets used for decanting purposes). If there are multiple assets, then the start date should be taken to be when the first one is operational, subject to a consideration of whether support should be phased – see below. In particular, care should be taken to ensure that a single asset is not completed artificially early purely to attract grant.

(1.2) Refurbishment. Where permanent assets are transferred and there is a distinct refurbishment period, these should be treated in the same way as new build and the start date will be when the asset returns to being operational. However, where a network of assets is transferred along with responsibility for maintaining them in an operational state, and a programme of investment (e.g. a street lighting or roads maintenance project), the start date will be when the assets are transferred.

(2) 'Phased' PFI projects

(2.1) Number of phases. The sponsoring department must determine whether there should be one "start date" for the whole project or whether it should be considered to consist of more than one "phase". In the latter case grant should start at different times for each of these phases. In taking such a decision the department should take account of the following general principles:

- Government Accounting requires that grant should not be paid in advance of need, which in the case of PFI project should be taken as the level of unitary charge being paid at any particular stage by the local authority in respect of the use of capital assets;
- As a consequence of the above, PFI credits should broadly follow the capital value added in the project; and
- The pattern of "phases" should be designed so that no significant clawback of PFI grant would be necessary should anticipated work be cancelled (see Section G below).

As projects become more complex with more assets being delivered (or phased delivery of one asset) the above guidelines need to be balanced with the need for the PFI grant regime to be manageable. Thus the sponsoring

department will need to consider whether a number of assets can be grouped together and considered as one "phase" for these purposes. The specifics of each project are likely to vary widely, but the following factors should be borne in mind:

- The number of "phases" should be limited and appropriate to the overall size of the project;
- The pattern of start dates should be considered to see whether there are distinct groupings in relation to the overall timescale.

As an example, assets which are the subject of different "waves" within BSF would be considered different phases. Projects consisting of a network of small assets (e.g. street lighting or similar) will not be considered to have distinct phases.

(2.2) Value of phases. If there are different phases, the PFI credits which apply to each phase must be stated in advance. It is for the sponsors to decide the level to be assigned to each phase. The capital value of each phase should be calculated separately as each will be a different base date for discounting. The interest rate (and discount rate) applied will be the same for all phases. However, the annuity length will be calculated separately for each phase.

SECTION G

POST CONTRACT SIGNATURE CHANGES

Changes may be made to the contract after it has reached financial close and the PFI credit has been issued.

(1) Increases. The most likely change will be one which will increase the capital value of the project. If a sponsoring department wishes to support such an increase it will be treated for grant purposes as if it were a separate contract. The discount rate in force at the time the increase is agreed should be used to calculate the level of the PFI credit. Grant will be paid separately in respect of the increase.

(2) Decreases. A variation may also be agreed which reduces the local authority's costs. This could be due to changes in the service element or financing costs. Neither of these would result in any reduction in support. It is established policy that in the case of refinancing the benefits will be shared on an equal basis between the contractor and the local authority, and not by central government.

However the variation could also involve reduced capital investment by the contractor, for example if it became clear that planning permission could not be obtained. This may lead to a reassessment of the PFI credit as set out in paragraph 4 below. It should be noted that there can be no reassessment once the assets are delivered and liabilities incurred by the local authority, even if those assets are subsequently destroyed or are no longer needed (unless there were exceptional circumstances as set out in paragraph 3.5 below). The effect of revising the PFI credit would depend on whether grant has started to be paid or not.

(3) Changes in the capital element. The overall level of expenditure under the contract may remain the same but there might be a shift from capital to revenue (for example, if a plan to achieve waste outputs by building a new asset was changed to transporting the waste to an existing facility). If that is the case then the sections above on reassessment still apply. It is recognised that this does impose considerations other than strict value for money on the freedom which the contractor has in responding to an output specification. Despite this it is felt important to maintain the principle that capital support should be for capital expenditure.

In other cases the nature of the assets may change, e.g. a change in the number or location, but the overall capital value remains about the same. In such circumstances an authority should notify the sponsoring department who will consider whether the alternative proposals are acceptable to them. If they are, support will continue without interruption.

(4) Reassessment. It is intended that reassessment should only be made where the nature of the assets has varied in a "significant" way. The initial

estimate of the capital element may be based on fairly broad assumptions and it would not be reasonable to try to make changes at the margins. This could also be seen as unduly restricting the contractor's freedom to innovate in meeting the outputs. Where a single building is involved, a reduction of more than 20% should be notified. A similar scale of reduction in other types of asset should be treated in the same way. Any reassessment of the level of support for any PFI project would be made by the sponsoring department, which should be the first point of contact. Reassessment will always be considered on a scheme-by-scheme basis after taking into account all the relevant circumstances.

(5) Exceptional circumstances. In exceptional circumstances, such as, for example, where continuation of support would unduly enrich or reward a deliberate abuse of the PFI contract, there could be a reassessment even if the capital assets had been delivered. In such a case, however, the Government would expect to take steps to ensure that the local authority was not thereby prevented from meeting in full the resulting liabilities to the PFI contractor and its funders for capital assets already delivered.

(6) Recovery. If the PFI credit figure is reassessed a calculation will be made to determine the amount of grant actually paid in excess of the amount which would have been paid based on the revised level of PFI credits. That will be recovered by deducting the amount from subsequent grant payments. Actual recovery of grant already paid would only be necessary where the excess was larger than could be recovered from future payments. Where an overpayment has been made the Secretary of State shall specify such an amount due to him by notice in writing before any recovery is made.

SECTION H

ADMINISTRATIVE ARRANGEMENTS FOR GRANT

(1) Legal basis of payments. Grant for all projects other than those which involve HRA housing will be paid under section 31 of the Local Government Act 2003 to receiving authorities listed in Local Government PFI Grant Determinations.

(2) Claim forms. The conditions for payment of grant are set out in Annex C of the relevant determination and include receipt of a valid claim. A valid claim is one which is made on the form PFIG1 or PFIG2, signed by the authority's Chief Finance Officer, copies of which can be printed from this department's website⁶.

The claim form should initially be sent to the sponsoring department. If a project is jointly funded one claim should be submitted to the lead department. The form should be accompanied by sufficient supporting documents to allow the form to be checked. This should include:

- a copy of the PFI credit letter to confirm the PFI credit amount (and the date of financial close where needed);
- a copy of the endorsement letter to confirm the date the project was endorsed;
- copies of the invoice and BACS remittance slips or receipt from contractor relating to the first payment; and
- relevant extracts from contract documentation as evidence of contract end dates.

Once a claim has been checked by the sponsoring department they will send it to this department, asking that grant be paid. The authority will receive notification of the amounts of grant and the dates on which each instalment will be paid.

A claim form only needs to be submitted when a project first claims grant. Subsequent years' grant will be based on that original claim form. The determinations set out how this will be done.

(3) Phased projects. Where there is more than one phase of a project (see Section D), each phase will be treated as if it were a separate project for the purposes of claiming grant. Therefore a new claim form needs to be sent for each phase, and each phase will generate separate payments of grant.

(4) Variations. If a post-contract signature variation is agreed and the sponsoring department has issued additional PFI credits a separate PFI grant claim form should be submitted.

⁶ www.local.communities.gov.uk/pfi/pfigrant.htm

(4) Audit requirements. There is no longer a requirement to send an audit form to the Department for Communities and Local Government. However, authorities are reminded of their continuing duty to ensure that accounting records are kept.

(5) HRA grant. Grant for HRA housing projects is paid as part of HRA subsidy rather than as a separate grant. There is no grant claim form, and payment is triggered by authorities sending a copy of the contract confirming the contract signature date to the Housing PFI team. The Communities & Local Government HRA team will then liaise directly with the authority to agree the Special Determination which will trigger the subsidy. Grant for the PFI scheme will then be paid as part of HRA subsidy until the end of the contract.

SECTION I

LIFT PROJECTS

This section sets out areas where LIFT projects differ from PFI. This replaces the separate note issued by ODPM in April 2005, which is now withdrawn.

In discussing LIFT and PFI some care needs to be taken with terminology, as terms do not have precisely the same meaning in the two contexts. In this Section:

- A *tranche* in LIFT consists of the collection of projects or schemes prioritised and funded by one Fund Co, which will be developed together so that the various approvals, inc. financial close, will be given for the whole tranche.
- A *project* or *scheme* in LIFT refers to an individual asset / building within a tranche.

In many ways, therefore, a LIFT tranche is most equivalent to a PFI project, which can often include several assets.

(1) Administrative arrangements for PFI credits

(1.1) First Approach. There is no separate allocation of PFI credits for local authority involvement in LIFT projects and any proposals must be assessed and prioritised against other competing possibilities. Proposals will be prioritised based on the quality of the scheme itself, rather than whether or not it is intended to use LIFT. A proposal may either be developed as the LIFT Co is being procured, or - more likely now - involve an existing LIFT Co.

A local authority may wish to include projects which they anticipate developing in different tranches in one proposal. In such cases, the sponsoring department may choose to endorse and thus provide a level of assurance of funding for the whole proposal. However, any such proposal should not be for tranches too far in future since that would tie up resources too far in advance of any prospect of the assets being delivered.

(1.2) Project endorsement. Whilst projects in more than one tranche may have been supported, the OBC should cover only those in the tranche being developed (though still set in the wider context of the whole proposal). A series of OBCs may therefore be necessary. It is, however, likely that the work involved in preparing later OBCs can be reduced by referring back to the first OBC unless different projects are very varied.

Working up the OBC parallels the development of a New Project Proposal under LIFT to Stage 1 approval. The areas which need to be covered in the OBC are broadly similar. The OBC should be submitted in sufficient time to be endorsed before LIFT Stage 1 approval, but not so far in advance that there might be changes between OBC endorsement and Stage 1 approval.

(1.3) Procurement. A FBC should be submitted shortly before Stage 2 approval. This should include a copy of the District Valuer (DV) review of the proposed rentals undertaken for LIFT Stage 2 approval. As with the OBC, there needs to be sufficient time for agreement before LIFT Stage 2 approval, but not so far in advance that there might be changes. It is expected that financial close would be reached shortly thereafter to avoid the danger that changes to the FBC may need to be agreed.

(2) Qualifying Criteria

(2.1) General. Most of the qualifying criteria set out in Section C apply equally to LIFT projects. Criteria which differ from PFI projects or which are of particular importance are discussed below.

(2.2) Commercial interest. Details of discussions and agreements with the LIFT Co should be included, including where the project has reached in terms of being included in the SSDP. A description of how the scheme(s) fit into the whole tranche of work should be provided together with the funding arrangements proposed for this. It is the tranche as a whole which needs to be bankable, and which is taken to the funding market with its own SPV (in this case a subsidiary of LIFT Co). Where it involves projects in the first tranche and the LIFT Co is being procured, a description of the procurement process also needs to be included.

(2.3) Accounting treatment. In order to be eligible for support projects must be considered a PFI contract under accounting standard FRS5. Therefore an early accounting opinion on this is needed, as well as the balance sheet treatment.

(2.4) Value for Money. Unlike PFI projects, individual LIFT projects may be VfM with a capital value of less than £20 million. In such cases the authority should show that the LIFT project is better VfM than conventional procurement but PFI need not be considered. Projects with a capital value of over £20 million should, however, be compared to both conventional procurement and PFI. As with all VfM assessments the overall conclusions will reflect both qualitative and quantitative considerations, backed up by evidence of assumptions and assertions used (eg if it is felt that LIFT can provide outputs more quickly than other means that should be demonstrated by reference to other projects), and will follow the Treasury guidance as described in Section C (2.2).

For projects over £20 million, the qualitative template should be modified so that there are 3 columns: LIFT, PFI and PSC. The qualitative assessment is likely to be extremely important in such cases as the models cannot be used to identify any quantitative differences between LIFT and PFI. The impact on options of any exclusivity deals signed under LIFT should be discussed here.

The government recognises that there are a number of areas where the Treasury quantitative model does not accurately reflect LIFT, but does not

believe that the differences are material, and so does not wish to see any alternative means of quantitative assessment. The authority should, nonetheless, comment on areas where the Treasury model does not take account of LIFT particulars. This will most obviously be in the following areas:

- Transaction/procurement costs. The model uses a minimum value of £750,000 for public sector costs and built-in assumptions about private sector costs. These are appropriate for PFI, but likely to be too high for LIFT projects. Authorities should in all cases provide separate estimates of public and private sector transaction costs. Public sector costs will reflect the complexity of the tranche and the opportunities to share costs across the public sector and will be broadly all incremental costs compared to not doing the procurement, inc. the wages of the internal project team and any external advisers; preparing business cases (inc affordability, VfM cases), drawing up participants' requirements, checking leaseplus agreement, and obtaining any necessary approvals. Private sector costs may include the costs of setting up any Fund Co, developing the project detail, inc. design, plans & drawings, producing the leaseplus agreement, obtaining planning approval, and producing the financial model and any other material needed by public sector.
- Residual value treatment. Unlike most PFI projects, some of the construction costs under LIFT will not be recovered via the annual charge, but via the residual value of the asset which the LIFT Co will own at the end of the contract. This means that the financing and profile of payments will be different to those the model assumes. It may be useful to provide estimates of the difference if possible. For a leaseplus agreement, the assumed reduction in the charge due to residual value and the proportion of debt covered by the residual value should be set out. (Note: any discussion must be clear about where the values being used are existing use and where alternative use).
- Unitary charge escalator. Under PFI an RPI escalator typically applies to only part of the unitary charge (not including the element relating to initial capex). However it applies to 100% of the LIFT leaseplus charge. The model will therefore not properly estimate the funding costs.

(2.5) Soft FM. A description of how 'soft FM' services (cleaning, security, etc) and the provision of fixed furniture and fittings and ICT will be handled must be included. Although this is generally true of PFI projects as well, it is especially relevant for LIFT projects as these items may not be part of the standard leaseplus agreement.

(3) Calculation of PFI credits and grant

There are no differences in the method of calculating PFI credits or grant compared to PFI. Sale of land to the LIFT Company and the use of residual value to cover a proportion of capital costs are issues of particular relevance to LIFT projects, but both are covered in Section D.