



**Notice of meeting of
Highways PFI Ad Hoc Scrutiny Committee**

To: Councillors D'Agorne, Hall, Livesley, Merrett, Moore
(Chair), Simpson-Laing and Vassie

Date: Monday, 26 February 2007

Time: 6.00 pm

Venue: The Guildhall

AGENDA

1. Declarations of Interest

At this point Members are asked to declare any personal or prejudicial interests they may have in the business on this agenda.

2. Minutes (Pages 1 -
2)

To approve and sign the minutes of the meeting held on 3 January 2007.

3. Public Participation

At this point in the meeting members of the public who have registered their wish to speak regarding an item on the agenda or an issue within the Panel's remit can do so. Anyone who wishes to register or requires further information is requested to contact the Democracy Officer on the contact details listed at the foot of this agenda. The deadline for registering is Friday 23 February at 5pm.

4. Highways Maintenance Procurement Process (Pages 3 -
& PFI – Final Draft Report 18)

This report details the recommendations proposed as a result of the above scrutiny review.

5. Any other business which the Chair considers urgent under the Local Government Act 1972

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For more information about any of the following please contact the Democracy Officer responsible for servicing this meeting Tracy Wallis

- Registering to speak
- Business of the meeting
- Any special arrangements
- Copies of reports

City of York Council

Committee Minutes

MEETING	HIGHWAYS PFI AD HOC SCRUTINY COMMITTEE
DATE	3 JANUARY 2007
PRESENT	COUNCILLORS D'AGORNE, HALL, LIVESLEY, MERRETT, MOORE (CHAIR) AND VASSIE
APOLOGIES	COUNCILLORS SIMPSON-LAING

1. **DECLARATIONS OF INTEREST**

Members were invited to declare any personal or prejudicial interests which they might have in any of the business on the agenda. No interests were declared.

2. **PUBLIC PARTICIPATION**

It was reported that there had been no registrations to speak at the meeting under the Council's Public Participation Scheme.

3. **SCOPING REPORT: HIGHWAYS PRIVATE FINANCE INITIATIVE (PFI)**

Members received a report which provided them with the opportunity to discuss and review the remit for the Highways Private Finance Initiative (PFI) scrutiny review. It was noted that the topic originally registered by Cllr Simpson-Laing had subsequently been amended and the remit split into two parts:

- A. To address the urgency of the PFI issue
- B. To ensure thorough investigation of the bidding process

The discussion centred around the objectives of Part A of the review as agreed by SMC at a meeting on 20 November 2006. Members recognised that the timescale for completing Part A was very tight and therefore they agreed to meet informally on 17th and 22nd of January to consider the first three objectives as follows:

- i. To examine the potential efficiencies from a PFI arrangement
- ii. To make recommendations with regard to available alternative options in the event that a PFI outcome was unsuccessful
- iii. To look at the cost effectiveness of those options, including improved ways of working

It was agreed that an interim report detailing findings on the first three objectives and requesting further time for the review, could be presented to SMC on 29 January 2007. Further informal meetings would then need to be arranged for February to consider the remaining two objectives:

- iv. To profile expenditure over the lifespan of the PFI and any associated secondary costs

- v. To understand the cost implications associated with the PFI and its outcome, if successful

Copies of the confidential PFI Expression of Interest submitted by the Council in September 2006 were circulated to Members only at the meeting. It was recognised that it could potentially provide information in regard to the first objective so Members agreed to study the document prior to the meeting on 17th January.

It was recognised that one of the key issues for the Council was how the PFI would be financed. In regard to the final two objectives listed above, some Members expressed concern that about the fullness of financial information made available to Members at the time of agreeing the decision to proceed with the PFI. To help assess that information and consider whether had been properly considered, Members requested that copies of the following papers be made available for the meeting on 17th January:

- Summary of the Best Value Review from June 2001
- Report on 'Highway Services – PFI Option' presented to Urgency Committee on 5 September 2006

Members were informed that other strategies were in place for procuring services upto 2010 after which the PFI would come into play should the bid be successful. The outcome from the submission of the council's Expression of Interest was expected by the end of January 2007 and at that stage the Council would need to decide if the wished to go ahead with submitting an Outcome Business Case (OBC). It was noted that no further costs would be incurred by the Council until work commenced on the OBC.

Members also requested that a expert witness be called upon to give an unbiased view on the PFI process and the Council's decision to proceed. It was agreed they should attend the meeting on 17 January 2007 if possible.

- RESOLVED:
- (i) That informal meetings be held on 17th and 22nd January to progress the review
 - (ii) An expert witness attend the meeting on 17th January, if available
 - (iii) An interim report on the progress with the first three objectives be presented to SMC on 29th January together with a request for more time to consider the remaining objectives
 - (iv) That a final draft report on Part A of the review be presented to SMC on 26th February.

Cllr RICHARD MOORE (Chair)

Meeting started at 4:30pm and finished at 6:10pm



Highways PFI Ad-Hoc Scrutiny Committee

26 February 2007

Highways Maintenance Procurement Process & PFI - Final Draft Report

Background

1. In September 2006, Scrutiny Management Committee (SMC) agreed to proceed with a review of topic No.135, into Highways Maintenance Procurement and the Private Finance Initiative (PFI) bid. SMC were informed that the Expression of Interest (EoI) associated with the PFI bid had already been submitted to the Department for Transport (DfT). They therefore requested that the original topic registration, registered in April 2006 by Cllr Tracey Simpson-Laing, be revised to take this development into account.
2. In November 2006 SMC considered the revised registration together with a draft remit which proposed the issues raised be dealt with in 2 parts. SMC agreed that part A of the review should centre entirely on how scrutiny could help prepare for the procurement of highways maintenance when the outcome of the PFI is known and consequently, how it could contribute to maximizing the Council's efficiencies and improving its procedures. It was felt that this would contribute proactively to the ongoing development work in anticipation of the outcome of the PFI bid in January 2007.

Corporate Priorities

3. It was recognised that this review could contribute to improving 'the actual and perceived condition and appearance of the city's streets and open spaces' by helping to improve the Council's procurement arrangements for highways maintenance. In rationalising our procurement arrangements, it could also help to improve our organisational effectiveness.

Options

4. Members can support all, some or none of the recommendations proposed as a result of this review, for submission to Scrutiny Management Committee and then to Executive.

Remit

5. In coming to a decision to review this topic, the Scrutiny Management Team recognised certain key objectives and the following remit was agreed:

Aims

To contribute to the development and establishment of a strategic and effective highways maintenance procurement strategy in York

To understand the cost implications associated with the PFI bid and its outcome if successful.

Objectives

- a) examining the potential efficiencies from a PFI arrangement;
- b) making recommendations with regard to available alternative options in the event that a PFI outcome is unsuccessful;
- c) looking at the cost effectiveness of those options, including improved ways of working;
- d) profiling expenditure over the lifespan of the PFI and any associated secondary costs.
- e) To understand the cost implications associated with the PFI bid and its outcome if successful.

Examining the potential efficiencies from a PFI arrangement

Consultation

6. Prior to the commencement of this scrutiny review, the Council had already submitted an Expression of Interest in relation to the Highways PFI. As part of that process officers had fully examined the potential efficiencies which could be gained from a PFI arrangement.

Information Gathered

7. The identified efficiencies to be gained from a PFI arrangement include:
 - a) Clearing the backlog of repairs
 - b) Improving maintenance services to allow the right maintenance at the right time
 - c) Lower future maintenance requirements
 - d) Effective and efficient network management resulting in improved traffic flows, accessibility and reliability
 - e) Improvements in congestion, air quality and ecological footprint¹
 - f) A safer and secure environment
 - g) The provision of sufficient investment to provide a springboard for the development of broader Council objectives

Issues

8. Members of the Committee studied the EoI previously submitted. This highlighted the problem facing City of York Council as it identified a

¹ York is the only city in the country with a working Eco Footprint model and a target of 70% reduction on carbon emissions over the next 50 years.

substantial backlog of maintenance works on the highway network valued at an estimated £127.5m. It recognised the Council's inability to fund whole life cycle asset management principles through intervention maintenance, resulting in an accelerated decline in asset value and network conditions. To be able to rehabilitate the asset and meet the central Government target of eliminating highways backlog by 2014/15, it is estimated that an additional £155m of capital life cycle replacement would be required to maintain the rehabilitated asset over the next 20 year period.

Members considered the options available to the Council listed in the Expression of Interest and were confident that full consideration had been given to the possible efficiencies to be gained from a PFI arrangement, and that no further work was necessary in relation to this objective.

9. It was recognised that in order to decide whether to proceed to the next stage of the PFI process, the Council would need to weigh up the recognised efficiencies against the annual commitment in terms of budget which would be required over the 25-year term of the PFI (irrespective of any future budget constraints).

Members acknowledged that PFI was the only scheme which could deliver an holistic approach across the entire unitary authority area.

Recommendation

10. That the efficiencies gained through the PFI approach as highlighted within the Expression of Interest be considered when deciding whether or not to proceed with the PFI process.

Reason: To ensure the most effective and financially viable outcome for highway repairs and maintenance, is achieved

Implications

11. There are no known Financial, HR, Equalities, Legal or other implications associated with the above recommendation.

Available alternative options in the event that a PFI outcome is unsuccessful

Consultation

12. The Assistant Director (City Development & Transport) provided the Committee with information on two simplistic alternative options to PFI – see Annex A.

Information Gathered

13. In considering these two alternatives, it was recognised that:
 - a) both had merits and drawbacks

- b) both were direct opposites in approach but there were potentially many possibilities for combining elements of each.
- c) careful consideration would need to be given to achieve the optimum solution for each particular aspect of work to be undertaken

Issues

14. The Committee were drawn towards the partnership approach but recognised the complexity of calculating the optimum solution for procuring service delivery. The Committee agreed that, given the timescale, it would be better to look at the key principles which should be taken into account at the time of selecting an alternative approach, rather than attempting to determine which approach should be used.. It also recognised that the work undertaken to produce the EOI would assist any other work required if the PFI outcome was unsuccessful. Members identified the following key principles which they felt would need to be considered when deciding how to proceed:

(a) Affordability

The level of funding available will influence which work method is adopted. Any work programme should be accurately costed as far as possible at the outset to avoid any overspends.

(b) Value for Money

Historically, some local authorities engaged in partnerships for efficiency savings which did not ultimately materialise. Any contract should ensure that perceived efficiencies are realistic.

(c) Sustainability

The Transport Asset Management Plan (TAMP) should be reviewed on a regular basis to ensure that the most sustainable working practices and materials are used.

(d) Risk Management

Members were particularly concerned regarding this issue. It was acknowledged that the balance and transfer of risk is central to any procurement consideration. If a partnership route is adopted, it should be ensured that the appropriate level of risk is borne by each party.

(e) Control

Regardless of the approach undertaken, the Council should ensure that control of any project is suitable to the selected approach. Where work is held in house, it was acknowledged that there were restrictive practices. These would not be applicable in a partnership approach.

(f) Innovation

Any contractor should embrace new innovative approaches in working practices, machinery and materials to ensure that any construction is undertaken to the optimum benefit of the Council, contractor and residents.

(g) Residents Priorities

Priorities of residents should be considered in the planning and construction of any development. Issues raised should be catered for as much as possible bearing in the mind contractual restraints and provided neither the quality nor the efficiency of work are detrimentally affected.

(h) Long Term Liabilities

Members recognised these would exist in any partnership approach and would not necessarily be apparent at the outset of any contractual arrangement. They appreciated, however, that selecting the 'right' partner in any contractual arrangement could help minimise liabilities.

Recommendation

15. That in the event that the PFI outcome is unsuccessful, the key issues identified should be taken into consideration when deciding upon an alternative approach.

Reason: To ensure the best alternative option for procuring service delivery.

Implications

There are no known Financial, HR, Equalities, Legal or other implications associated with the above recommendation.

The cost effectiveness of alternative options to PFI, including improved ways of working

Consultation

16. Officers from the Council's Resources Directorate provided information on various sources of alternative funding. It was recognised that some of the different sources would only be applicable to certain approaches. Some were unlikely to fund maintenance works and others would not provide funding on the large scale required.

Information Gathered

17. The alternative sources of funding identified were:

(a) Venture Capital

This would only be available for partnership working. It was understood that funds could be drawn down from the Council's Venture Fund (part of the Council's Reserves) with the Fund expecting return of profit.

(b) Prudential Borrowing

This would provide funds with which to undertake a works programme, but it would be necessary to identify where savings could be made in future years to repay the loan.

(c) Yorkshire Forward

It was considered that there would need to be an identifiable improvement to the economic wellbeing of the city in order to access funding from this source. It was also considered that there would probably have to be a benefit to the region.

(d) National Lottery

It was considered that the amounts of funding would be relatively small and that it would be a support but not a major source. Funding from the Lottery would be for very specific purposes, e.g. heritage, arts, sports, Conservation Areas, etc., and would not be available for maintenance programmes.

(e) European funding sources

It was considered that any EU funding would need to be linked with partnership working, possibly even between countries. Access to funding from this source would not necessarily depend solely upon the scheme but also how it would be implemented and what new innovation was involved.

Issues

18. The Committee acknowledged that on the basis of the information received, the Council could not expect to receive sufficient alternative funding on the scale of PFI to finance all of the identified remedial works required to the highways infrastructure. This in turn would result in its further decline.
19. In order to complete all of the remedial works required and sustain a full maintenance programme, the Council would have to make a much larger annual commitment in terms of budget than that which would be required over the 25-year term of the PFI. This again would have far reaching financial implications.

Recommendation

20. That in the event that the Council's Expression of Interest is successful, the decision to proceed to the next stage of the PFI process, i.e. submitting an Outline Business Case, be weighed against the resulting greater annual budget commitment required from the Council if the Highways repair and maintenance works are to be carried out.

Reason: To ensure the most cost effective method for funding the required works.

Implications

21. There are no known Financial, HR, Equalities, Legal or other implications associated with the above recommendation.

Profile of expenditure over the lifespan of the PFI and any associated secondary costs

Consultation

22. The Assistant Director (City Development & Transport) provided information on some of the factors which will affect the overall cost of a PFI arrangement to the Council. One of the main factors would be managing the risks involved. As part of the process of drawing up a PFI contract between a potential partner and the Council, an appropriate level of risk should be considered and agreed by each party.
23. Contract costs would be influenced by the level and amount of risk accepted by the partner. Therefore, the Council will need to take account of this within the negotiations.

Information Gathered

24. Three main risks were identified, as follows :

(a) Project Risk

Substantially, this means not achieving a signed contract at the end of the PFI bidding process. This is a pathfinder project and it is anticipated the DfT will want to identify a best practice approach for future use. As a result, it is recognised that the whole process could take longer to complete which would result in higher costs. It is expected that the DfT will be likely to provide advice, resources and possibly financial support to assist the process.

(b) Latent Defects

As part of the bidding process the Council would need to carry out investigative works on the major highway assets e.g. bridges, to be able to best describe their condition and to identify any defects. Although this work would add to the project costs it is recognised that it would assist in the process of drawing up a contract and transferring risk to the partner. As a result this could save the Council money in the long term, as any partner would be likely to balance the contract costs with the amount of relevant accurate information supplied about the assets. The investigative works are likely to have significant cost which would be beneficial for a PFI contract though, if unsuccessful, the benefits from the information gained would not necessarily outweigh the costs incurred.

(c) Contract Risk

There are several areas within the contract where the amount of risk to be transferred would need to be carefully considered:

(i) Legislation

No contractor would accept risk related to changes in legislation. This is a non-transferable risk and the effects are unforeseeable.

(ii) Inflation

Any contract will allow for a certain level of inflation but over such a long term project it is impossible to completely cater for extreme variances.

(iii) Vandalism

It is impossible to foresee what effect this may have on any contract and any partner would be reluctant to accept this risk without some form of indemnity from Council.

(iv) Liquidation

This risk, although catered for through financing arrangements of the partner would prove problematical should a new partner need to be sourced.

(v) Affordability

The long term nature of this type of contract raises questions regarding the level of funding which the Council could and would commit with the internal and external funding pressures it faces.

Issues

25. It is clear that it is impossible to identify all possible risks involved with such a long term contract but failure to maintain and repair the highways infrastructure carries its own risks. For example, the Council presently self insures against claims and has an extremely successful repudiation rate, but it is considered that the number of claims would be likely to increase as the infrastructure continued to deteriorate. Also, as central Government has set a target of eliminating highways backlog by 2014/15, the Council may incur costs if this work is not completed on time.

Recommendation

26. That it be noted that as there are too many unknown quantities at this stage in the process, the total expenditure over the lifespan of the PFI cannot be properly identified.

Implications

27. There are no known Financial, HR, Equalities, Legal or other implications associated with the above recommendation.

The cost implications associated with the PFI bid and its outcome if successful

Consultation

28. The Assistant Director (City Development & Transport) presented information on the timetable for the remaining stages of the PFI process. This included information on the associated cost implications for each stage and the points at which a decision would need to be taken on whether or not to proceed – see Annex B.

Information Gathered

29. The Director of Resources presented a summary of the budget for 2007/08 which highlighted expected pressures. It was recognised that a decision to

proceed with the next stage of the PFI bid, i.e. submitting an Outline Business Case would have an effect on the 2007/08 budget. The summary also recognised that the largest proportion of cost would be likely to be incurred in 2010/11, as the majority of cost occurs in the last few months.

Issues

30. Although there are recognised cost implications associated with a PFI bid, these costs would be reimbursed when the PFI scheme commenced. It is clear that the overall cost of the PFI approach to the Council would be less than completing the same amount of work of the same quality and standard via alternative methods. The Council could only finance the same amount of remedial and maintenance works as done through a successful PFI, by putting severe constraints on other budget commitments over the 25-year period. The drawback of the PFI route would be that the Council cannot predict what else may occur during the next twenty-five years that may result in further budget pressures and once a PFI contract is signed, the Council could not reduce its financial commitment to the repairs and maintenance works to allow the budget to be reassigned. The Council would have little room to manoeuvre with regard to its financial commitments.

Recommendation

31. That in the event that the EoI is successful, careful consideration should be given when deciding whether to proceed to each of the following stages of the process, thereby ensuring a full understanding of the cost implications.

Implications

32. There are no known Financial, HR, Equalities, Legal or other implications associated with the above recommendation.

Acknowledgements

The Committee would like to record its thanks to the various officers who have supported its work. The assistance and advice received has been appreciated, and without this support it is unlikely that the scrutiny could have been completed in the timescale. In particular thanks go to:

Damon Copperthwaite, Assistant Director (City Development & Transport)
Paul Thackray, Head of Highway Infrastructure, City Strategy
Simon Wiles, Director of Resources
Patrick Looker, Resource & Business Manager, City Strategy
Melanie Carr, Scrutiny Officer
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Cllr Richard S. Moore
Chair
Highways
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Scrutiny Ad-Hoc
Sub-Committee

**Final Draft Report
Approved**

Date 22 February 2007

Wards Affected: *List wards or tick box to indicate all*

All

For further information please contact the author of the report

Background Papers:

Local Government Private Finance Initiative (PFI): CYC Expression of Interest

Annexes

Annex A - Alternative Procurement Options
Annex B – Timetable for the Remaining Stages of the PFI Process

Basic Service Delivery & Procurement Options

Approach	Traditional	Partnership
Scope	Broken into components i.e. Surfaces Street Lighting Routine / Reactive Technical i.e. traffic signals, CCTV	All inclusive with one partner
Client	Large	Small

Contract Arrangements

Specification	Input - where an exact job specification is agreed with the contractor prior to work commencing.	Output - Having agreed the outcome, the partner decides how to achieve this and then carries out the work. For this to be successful the partnership would need to be based on trust, openness and honesty. To achieve this level of compatibility, the two partners have to be confident that they both have the same work ethos and standards, therefore much time will be spent at the contract stage to ensure both parties fully understand the requirements of the other. They are equal partners and must both deliver on their side of the bargain
Risk to Council	Retained - risk remains with CYC	Transferred - a majority of the risk is transferred to the partner. The partner will not accept unknown risk i.e. inflation, insurance, changes to legislation.
Cost	Medium, there could be some increase due to variations	High - Initial high cost because partner takes on majority of risk including the biggest risk of all - construction risk. Partner has limited ability to come back for extra money
Term	Medium (5-7 yrs)	Long (7-10yrs) - Partner covers his costs over a longer term.
Incentive	No - The contractor has agreed a price before the work commences therefore there is no incentive to be more efficient	Yes - With a longer term there is more incentive/benefits to be more efficient

Procurement Arrangements

Evaluation	80% price / 20% "quality" - Tenders received are considered mainly on the cost as the specification set by CYC would have been written in terms of the required levels of quality	40% price / 60% "quality" - As the partner will be wholly responsible for the standard of work carried out it is important to consider the "quality" of the partner (e.g. whether the work ethos is compatible) when agreeing a contract. This becomes a much more important factor and outweighs the issue of cost.
Method	EU restricted standard tender	EU restricted or competitive dialogue (if the rules for competitive dialogue are met)

Cost	Medium - specifications are drawn up for each aspect of work	High - More time and resources are spent at the procurement stage to ensure the partnership is solid and will achieve the required outcomes.
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City of York CouncilPrivate Finance Initiative : Highway Maintenance Pathfinder ProjectDraft Timetable and Decision Making Points

Expression of Interest : Annex 10

<u>Activity</u>	<u>Timescales</u>	<u>Decision</u>	<u>Time</u>
<u>Preliminary Phase</u>			
Development of Eol	June 06 – Sept 06		
		Urgency Committee: To approve submission of Eol	5 Sept 06
Submission of Eol to DfT	10 Sept 06		
		Approval of Eol by DfT Project Review Group	April 07
		Executive Report: Implications of the project including risk, submission of OBC, funding of the project	July 07
Appointment of a project team	June 07		
Preparation of Outline Business Case	June 07 – April 08		
		Executive Report: To approve submission of OBC and agreement to procurement process	April 08
Submission of OBC to DfT	April 08		

Approval of OBC
by DfT Project
Review Group Aug
08

Procurement

Advisors Develop advisor contracts April 08

Issue OJEU Notice May 08

Issue PQQ June 08

Appoint short list,
seek proposals July 08

Advisor interviews Aug 08

Executive Report: Aug 08
To approve
appointment of
advisors

Appointment of
advisors Sept 08

Service
Providers Development of
Contract Details June 07 – May 09

Issue OJEU Notice Oct 08

Issue PQQ and
seek Expressions
of Interest Nov 08

PQQ Evaluation
and Short Listing Dec 08

Executive Report: Jan 09
To approve stage
1 short list of
service providers

Invite Submission
of Outline Solutions Jan 09

Submission of
Outline Solutions Mar 09

Evaluation and April 09

dialogue of Outline
Solutions

Executive Report: May 09
To approve Stage
2 short list of
service providers

Invite Submission May 09
of Detailed
Solutions

Submission of June 09
Detailed Solutions

Evaluation and June 09 – Jan 10
dialogue of Detailed
Solutions

Close dialogue Feb 10

Invite Final Tenders Feb 10

Evaluation of Final May 10
Tenders

Clarification of Final May 10 – Aug 10
Tenders

Executive Report: Sept
To approve 10
selection of
preferred Service
Provider

Final clarification, Sept 10 – Nov 10
due diligence.

Preparation of Final Sept 10 – Nov 10
Business case to
DfT

Executive Report: Dec 10
To approve the
Final Business
Case for
submission to DfT

Submit FBC to DfT Dec 10
PRG

Approval of FBC
by DfT Project
Review Group Feb 11

Financial Close and Award of contract Feb 11

Mobilisation and start of Contract Feb 11 – July 11

Damon Copperthwaite
19 February 2007