NHS Greater Glasgow & Clyde

Gorbals Health and Care Centre

And

Woodside Health and Care Centre

Project Bundling Paper

December 2016

Contents

1 Proposed Investment

This paper is presented on behalf of NHS Greater Glasgow and Clyde (NHS GGC) to set out the financial efficiencies through bundling the projects to develop a new Gorbals Health and Care Centre and a new Woodside Health and Care Centre.

These projects are proposed to be bundled into one contract to be provided by hub West Scotland as part of Scottish Governments approach to the delivery of new community infrastructure.

"Gorbals Health and Care Centre"

NHS Greater Glasgow & Clyde presented an Initial Agreement document, '**Proposed Gorbals Health and Care Centre**', to the Scottish Government Capital Investment Group (CIG) on 18 July 2012. It received approval on the 9th November 2012. Subsequently the Outline Business Case (OBC) received approval on 24th April 2015. The Full Business case has now been prepared presented by CIG at their meeting on 10th January 2017.

"Modernisation and redesign of primary and community health services for Woodside"

NHS Greater Glasgow and Clyde presented an Initial Agreement document, 'Replacement Woodside Health and Care Centre', to the Scottish Government Capital Investment Group (CIG) in June 2012. It received approval on 9th November 2012. Subsequently the Outline Business Case (OBC) received approval on 24th April 2015. The Full Business case has now been prepared presented by CIG at their meeting in on 10th January 2017.

2 Financial Efficiencies through Bundling

The following financial efficiencies, in nominal terms, have been estimated through bundling the two projects. It is noted that there is added complexity of progressing two entirely independent construction sites under one project agreement.

Financial Efficiencies	2019/20	Project Lifetime
	£'000	**£'000**
Agency Fees	**25**	**265**
Due Diligence Costs	**32**	**32**
Financial Modelling	**30**	**30**
Sub hubco Management Fees	**56.8**	**1,420.8**
Input Costs	**tbc**	**tbc**
TOTAL SAVINGS	**166.8**	**1,770.8**

The savings are analysed in more detail below:

- Agency fees – savings of £10,000 per annum (£250,000 project lifetime) and £15,000 of fees saved during construction

- Due Diligence costs – Where appropriate fees with advisers have been established by hubco based on a bundled scheme. From discussions with hubco and based on the evidence provided, it is estimated that bundling the two schemes has resulted in savings in the region of £32,000 during development.

- Financial modelling – savings in operational model fees of £30,000 have been achieved as a result of the bundling of the two projects.

- sub hubco management fees – the bundling of project will lead to financial efficiencies as costs, especially labour costs, can be spread across the projects. The proforma management fee for each scheme was confirmed at £140,000 but at the New Project Request Stage, a management fee cap of £100,000 per scheme was agreed with sub hubco. As a result of bundling the two schemes, a combined fee of £143,168 was agreed. This equates to an annual saving in comparison to the NPR stage of £56,832 per annum or £1,420,800 over the project lifetime.

- Input Costs – awaiting info of net savings on construction costs as a result of bundling.

It should be noted that there is not anticipated to be any savings in the funding margins and fees for bundling the projects, due to the finance product that Aviva offers.

3 The Financial Case – Gorbals and Woodside

The following sections summarises the bundled financial case for Gorbals and Woodside Health and Care Centre projects. This sets out the following key features:

- Revenue Costs and associated funding
- Capital Costs and associated funding
- Statement on overall affordability
- Financing and subordinated debt
- The financial model
- Risks

3.1 Revenue Costs and Funding

3.1.1 Revenue Costs and Associated Funding for the Project.

The table below summarises the recurring revenue cost with regard to the Gorbals and Woodside Health and Care Centre Schemes.

In addition to the revenue funding required for the Gorbals & Woodside Health and Care Centre schemes, capital investment will also be required for land purchase (including site investigations £336.0k), equipment (£1,527.0k) and sub debt investment (£307.3k). Details of all the capital and revenue elements of the project together with sources of funding are noted below;

Recurring Revenue Costs Table

First full year of operation	**2019/20**
Recurring Costs	**£'000**
Unitary Charge	**2,880.7**
Depreciation on Equipment	**152.7**
IFRS – Depreciation	**1,258.6**
HL&P , Rates Domestics etc	**752.6**
Client FM Costs	**59.1**
Total Recurring costs for Project	**5,103.7**

3.1.2 Unitary Charge.

The Unitary Charge (UC) is derived from both the hub West Scotland Stage 2 submission and the Financial Model Gorbals Woodside v13 and represents the Predicted Maximum Unitary Charge of £2,880.7kpa, based on a price base of April 2013.

The UC will be subject to variation annually in line with the actual Retail Price Index (RPI) which is estimated at 2.5% pa in the financial model. The current financial model includes a level of partial indexation of 20% and this will be reviewed prior to financial close to ensure it provides a natural hedge. The financing elements of the UC are not costs that are subject to indexation.

3.1.3 Depreciation

Depreciation of £152.7k relates to capital equipment equating to £1.527m including VAT and is depreciated on a straight line basis over an assumed useful life of 10 years.

3.1.4 HL&P, Rates & Domestic Costs

HL&P costs are derived from existing Health Centre costs and a rate of £22.57/m2 has been used.

Rates figures of £19.00/m2 have been provided.

Domestic costs are derived from existing Health Centre costs and a rate of £23.87/m2 has been used.

3.1.5 Client FM Costs

A rate of £5.29/m2 has been provided by the Boards technical advisors, based on their knowledge of existing PPP contracts.

3.1.6 Costs with regard to Services provided in new Health Centre

Staffing and non-pay costs associated with the running of the health centre are not expected to increase with regard to the transfer of services to the new facility.

3.1.7 Recurring Funding Requirements – Unitary Charge (UC)

A letter from the Acting Director – General Health & Social Care and Chief Executive NHS Scotland issued on 22nd March 2011 stated that the Scottish Government had agreed to fund certain components of the Unitary Charge as follows:

100% of construction costs,

100% of private sector development costs

100% of Special Purpose Vehicle (SPV) running costs during the construction phase

100% of SPV running costs during operational phase

50% of lifecycle maintenance costs.

Based on the above percentages the element of the UC to be funded by SGHD is £2,609.2k which represents 76.5% of the total UC, leaving NHSGG&C to fund £271.4k (8%) and GCC the remaining £529.8k (15.5%). This split is detailed below.

UNITARY CHARGE	Unitary Charge £'000	SGHD Support %	SGHD Support £'000	NHSGGC Cost £'000	GCC Cost £'000
Capex including group 1 equipment, development & SPV Costs	2,960.3	100 of NHS	2,500.4	0	459.9
Life cycle Costs	257.6	50 of NHS	108.8	108.8	40.0
Hard FM	192.5	0	0	162.6	29.9
Total	**3,410.4**		**2,609.2**	**271.4**	**529.8**
			76.5%	**8%**	**15.5%**

3.1.8 Sources of NHSGG&C recurring revenue funding

The table below details the various streams of income and reinvestment of existing resource assumed for the project.

NHSGG&C Income & Reinvestment	£'000
Existing Revenue Funding – Depreciation	**140.4**
Existing Revenue Funding – HL&P, Rates & Domestic NHSGG&C	**212.4**
Revenue Funding –GPs, Dental & Pharmacy contribution	**202.0**
IFRS – Depreciation	**1,258.6**
Additional Revenue Funding	**681.1**
Sub-Total	**2,494.5**
Glasgow City Council running costs	**150.4**
Glasgow City Council unitary charge	**529.8**
Total Recurring Revenue Funding	**3,174.7**

Depreciation
Annual costs for depreciation outlined above relate to current building and capital equipment. The budget provision will transfer to the new facility.

HL & P Rates & Domestic
All heat, light & power, rates and domestic budget provision for current building will transfer to the new facility. This is reflected above in the two contributions being NHSGG&C and via GPs.

Additional Revenue Funding
This relates to indicative contributions from GPs within the new facility.

3.1.9 Summary of Revenue position:

Summary of Revenue position	£'000
SGHD Unitary Charge support	**2,609.2**
NHSGG&C recurring funding per above	**2,494.5**
NHSGGC funding from GGC per above	**680.2**
Total Recurring Revenue Funding	**5,783.9**

Recurring Revenue Costs	£,000
Total Unitary charge(service payments)	**3,410.5**
Depreciation on Equipment	**152.7**
IFRS – Depreciation	**1,258.6**
Facility running costs	**811.7**
GCC recurring costs	**150.4**
Total Recurring Revenue Costs	**5,783.9**
Net Surplus/Deficit at FBC Stage	**0**

The above table demonstrates that at FBC submission, the project revenue funding is cost neutral.

3.2 Capital Costs & Funding

Although this project is intended to be funded as a DBFM project, i.e. revenue funded, there is still requirement for the project to incur capital expenditure. This is detailed below.

Capital costs and associated Funding for the Project

Capital Costs	£'000
Land purchase & Fees	**336.0**
Group 2 & 3 equipment Including VAT (NHS)	**1,527.0**
Sub debt Investment	**307.4**
Total Capital cost	**2,170.4**
Sources of Funding	
NHSGG&C Formula Capital	**2,170.4**
Total Sources of Funding	**2,170.4**

3.2.1 Land Purchase

A capital allocation for the land purchase of £336k, including the cost of survey fees, has been incorporated in NHSGG&C's 2016/17 capital plan.

3.2.2 Group 2 & 3 Equipment

An equipment list amounting to £1,785.2k including VAT has been collated for the Gorbals and Woodside Projects, with NHS GG&C providing £1,527.0k and GCC providing £258.2k. The equipment list is currently being reviewed which will also incorporate any assumed equipment transfers.

3.2.3 Sub Debt Investment

The Board will be providing the full 10% investment. The value of investment at FBC stage is £307.4k for which NHSGG&C has made provision in its capital programme.

3.2.4 Non Recurring Revenue Costs

There will be non-recurring revenue costs of £213.2k in terms of advisers' fees. These non-recurring revenue expenses have been recognised in the Board's Financial Plans.

3.2.5 Disposals of Current Health Centres

The FBC's are predicated on the basis that the existing Health Centres, which are not fit for purpose, will be disposed of once the new facilities become available. There will be a non-recurring impairment cost to reflect the rundown of the facilities. The Net Book Values as at 28th November 2016 are £2,808.5m. Following the disposals, any resultant capital receipt will be accounted for in line with the recommendations contained in CEL32(2010)

3.2.6 Overall Affordability

The current financial implications of the project in both capital and revenue terms as presented above confirm the projects affordability.

3.3 Financing & Subordinated Debt

3.3.1 hubco's Financing Approach

hub West Scotland will finance the project through a combination of senior debt, subordinated debt and equity. The finance will be drawn down through a sub-hubco special purpose vehicle that will be set-up for the two projects.

The senior debt facility will be provided by Aviva, the remaining balance will be provided by hWS' shareholders in the form of subordinated debt (i.e. loan notes whose repayment terms are subordinate to that of the senior facility) and pin-point equity. It is currently intended that the subordinated debt will be provided to the sub-hubco directly by the relevant Member.

3.3.2 Current Finance Assumptions

The table below details the current finance requirements from the different sources, as detailed in the financial model submitted with hubco's Stage 2 submission.

	£'000
Senior Debt (£000)	36,539
Sub debt (£000)	3,599
Equity (£000)	0.01
Revenue (£000)	116
Total Funding	40,254

The financing requirement will be settled at financial close as part of the financial model optimisation process.

3.3.3 Subordinated Debt

Our expectation is that subordinated debt will be provided in the following proportions: 60% private sector partners, 20% Hub Community Foundation, 10% NHS Greater Glasgow & Clyde and 10% Scottish Futures Trust.

The value of the required subdebt investment injected at financial close is as follows:

	NHS GG&C	SFT	HCF	hubco	Total
Proportion of subdebt	10%	10%	20%	60%	100%
£ subdebt	307,342	307,342	614,684	1,844,054	£3,073,422

NHS Greater Glasgow & Clyde confirms that it has made provision for this investment within its capital programme.

It is assumed the sub-ordinated debt will be invested at financial close, and therefore there would be no senior debt bridging facility.

3.4 Financial Model

The financial model at Stage 2 has been prepared on the basis that Woodside and Gorbals are bundled together but enables sufficient transparency over the costs relating to each scheme so as to ensure that the model's consistency with the affordability analysis can be monitored and clarity over those savings in relation to bundling are obtained. The key inputs and outputs of financial model are detailed below:

Output	Woodside &

	Gorbals
Capital Expenditure (capex & development costs	£37,087k
Total Annual Service Payment (NPV)	£36,370k
Nominal project return	5.39%
Nominal blended equity return	10.50%
Gearing	91.03%
All-in cost of debt (including 0.5% buffer)	2.50%
Minimum ADSCR[1]	1.15
Minimum LLCR[2]	1.165

The all-in cost of senior debt includes an estimated swap rate of 2.00%, and an interest rate buffer of 0.50%. The buffer protects against interest rate rises in the period to financial close. The current (28 November 2016) Aviva 4.25% 2032 Gilt is 1.80%, therefore with the interest rate buffer included, there is cover for 0.70% of increase in the underlying gilt rate before financial close.

The financial model has been reviewed by NHS GG&C's Financial Advisors and will be subject to model audit by another firm as part of the funder's due diligence process.

3.5 Risks

The unitary charge payment will not be confirmed until financial close. The risk that this will vary due to changes in the funding market (funding terms or interest rates) sits with NHS GG&C. This is mitigated by the funding mechanism for the Scottish Government revenue funding whereby Scottish Government's funding will vary depending on the funding package achieved at financial closed.

A separate, but linked, risk is the risk that the preferred funder will withdraw its offer or that funding will be otherwise unavailable at terms which are affordable. This will be monitored by means of ongoing review of the funding market by NHS GG&C's financial advisers and periodic updates from hubco and their funders of the deliverable funding terms (through the Funding Report). This will incorporate review of the preferred lender's commitment to the project as well. This will allow any remedial action to be taken as early in the process as possible, should this be required. Hubco's financial model currently includes a small buffer in terms of the interest rate which also helps mitigate against this price risk adversely impacting on the affordability position.

At financial close, the agreed unitary charge figure will be partially subject to indexation, linked to the Retail Prices Index. This risk will remain with NHS GG&C over the contract's life for those elements for which NHS GG&C has responsibility (100% hard FM, 50% lifecycle). NHS GG&C will address this risk through its committed funds allocated to the project.

[1] Annual Debt Service Cover Ratio: The ratio between operating cash flow and debt service during any one-year period. This ratio is used to determine a project's debt capacity and is a key area for the lender achieving security over the project

[2] The LLCR is defined as the ratio of the net present value of cash flow available for debt service for the outstanding life of the debt to the outstanding debt amount and another area for the lender achieving security over the project

The affordability analysis incorporates that funding will be sought from GP practices who are relocating to the new health centre. This funding will not be committed over the full 25 year period and as such is not guaranteed over the project's life. This reflects NHS GG&C's responsibility for the demand risk around the new facility.

The project team will continue to monitor these risks and assess their potential impact throughout the period to financial close.

4 Bundled Programme

The programme for the projects is currently anticipated as follows:

Gorbals Health & Care Centre - Project Phases

CIG Meeting for FBC	**10 January 2017**
Financial Close	**31 January 2017**
Start on site	**February 2017**
Completion date	**September 2018**
Services Commencement	**October 2018**

Woodside Health and Care Centre- Project Phases

CIG Meeting for FBC	**10 January 2017**
Financial Close	**31 January 2017**
Start on site	**February 2017**
Completion date	**September 2018**
Services Commencement	**October 2018**

The clear similarity of intended timescales compliment the financial benefits detailed above and align fully with the proposed to bundling of the Gorbals and Woodside projects.

5 Conclusion

NHS GGC & Glasgow City HSCP has carried out a complete, evidence based review and analysis of the existing and future health requirements of the current users of health facilities in the Gorbals & Woodside area of Glasgow. The Outline Business Case and the Full Business Case represents the collective input of the HSCP, the Clinical and Community Staff at existing health facilities, their advisors and a wide variety of consultees and stakeholders.

The current facilities for patients, staff and visitors in the current sites area are inadequate. The facilities do not comply with various statutory requirements including Disability Discrimination Access (DDA). The existing buildings currently fail to meet modern healthcare standards, in terms of functional requirements, special needs, and compliance with current clinical guidance, fire regulations and infection control measures. Accommodation tends to be cramped and is characterised by inadequate GP consulting rooms, limited community staff accommodation and overcrowded/ noisy waiting areas. Furthermore, there is a significant backlog in maintenance. The plant and equipment are well beyond their design life, and hence are inefficient in terms of energy use and carbon footprint.

Benefits of Bundling

This paper clearly demonstrates the significant efficiencies that result from bundling the two facilities and as a result this is the recommended approach as reflected in the Business Cases.