

## **Wiltshire Council**

### **Schools Forum**

**13<sup>th</sup> October 2011**

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## **Private Finance Initiative (PFI) Schools Affordability Gap 2012-13 Onwards**

### **Purpose of report**

1. To update members of the Schools Forum on the current position regarding the Schools PFI Sinking Fund and the affordability gap relating to the Fund and to recommend an increase in contributions from 2012-13 onwards.

### **Background**

2. A Private Finance Initiative (PFI) agreement was signed to build three new secondary schools in North Wiltshire in 2000. The new schools were built at Abbeyfields, Chippenham, Wootton Bassett & Malmesbury and the PFI agreement covered both the initial building costs and the running costs (Facilities Management and Lifecycle costs). In two of these schools, sixth form units have been built more recently and added to the PFI contract, though this factor does not impact specifically upon the affordability gap.
3. At the outset of the agreement a detailed model was constructed to analyse the costs over the contract period including appropriate assumptions. All of the costs were modelled over the full contract period of 32 years. The detailed model was then agreed by the parties as part of the sign off of the contract documentation. From these calculations a figure is produced, generally known as the Unitary Charge, which is the annual amount payable by Wiltshire Council to the contractor, which is adjusted annually by the Retail Price Index (RPI). In this contract the Unitary Charge is described as the Basic Access Payment (BAP).

### **Main Considerations for Schools Forum**

4. The Unitary Charge or BAP is funded as follows:
  - PFI Credit, Government Grant: this was agreed at the outset of the contract: it is paid in equal fixed instalments throughout the contract period (£3.251 million per annum). Unlike the BAP, it is not inflated through the contract period, which means that in relative terms the Grant is worth significantly more at the start of the contract than at the end of it. Therefore, looking annually at the Council's expenditure and income, the contract will generate a surplus in its earlier stages which will be offset by a deficit later on. This means that an Equalisation Fund (a type of Sinking Fund) has to be built up in the early years to cover the anticipated deficits that are inevitable in the later years of the contract.

- Local Management of Schools (LMS) & Equivalent contributions from Academies: the PFI contractor is providing a facilities management (FM) service and the BAP includes the lifecycle costs of keeping the building in a serviceable condition, for example electrical and boiler updates for the duration of the contract. In a non-PFI situation the school would be using a proportion of its formula allocation under LMS or the new academy arrangements, to cover such costs and therefore an estimate was made at the outset of the contract of an appropriate percentage of LMS budgets to put into the contract. The agreed percentage contribution was 10% and this has been maintained.
  - Affordability Gap or PFI Supplement: it was apparent at the outset that there was an “affordability gap” in the project. This gap is covered by the PFI Supplement, which is an amount provided from the Dedicated Schools Grant (DSG) budget, in order to balance the overall position over the full contract period of 32 years. This funding is top-sliced from the overall schools budget and therefore any change will impact marginally on each school in Wiltshire. Under the current funding mechanism for maintained schools and academies each PFI school receives an amount through the Local Authority School funding formula that is equal to its contribution to the fund. That amount is then recharged from the school and the contribution paid in to the fund. As stated above, this is a cost to the overall schools budget for Wiltshire. From 2012-13 this mechanism will be controlled by the DFE for the two academy schools (Wootton Bassett & Malmesbury), though the Council is waiting for clarification of how this will work in practice from April 2012 onwards, depending on the funding mechanism for academies that is put in place from April 2012.
5. The contract has now been operational for approximately 10 years and the equalisation fund has been reviewed a number of times. In the early years of the contract, the figures were generally in line with expectations, though in recent years the position has deteriorated somewhat. The main reasons for this are as follows:-
- Benchmarking: utility costs were reviewed under the terms of the contract in both April 2006 and April 2008 and the impact was an increase in the costs. This increase was not recoverable from the schools under the contract terms and therefore this has resulted in a shortfall on the Sinking Fund. More recent utilities & soft service benchmarking exercises have also had an impact, albeit a less significant one.
  - Interest Rates – as referred to above, the contract in its earlier years creates a surplus which is transferred to the Sinking Fund. Interest is added to the cumulative balance and the expectation in the original contract model is that 6% would be added to the cumulative balance. However, the economic environment has changed markedly with the credit crunch and subsequent recession, leading to a position where, at present, Wiltshire Council is only receiving an average of approximately 0.5% on its investments.
  - Pupil Numbers – this had varied over the 10 year period since the inception of the contract though the overall impact of these changes is roughly neutral.

## **The Affordability Gap**

6. The factors outlined above have clearly put pressure on the Sinking Fund and the overall annual contribution from 2012-13 onwards needs to be reviewed.
7. There is some uncertainty over the amount of increase required; in particular, there is a strip of land near to Abbeyfields School which the Council may be able to sell for primarily housing development over the next few years. Any Capital receipt from this land is currently ringfenced to the PFI Sinking Fund. However, in the current economic environment, it is difficult to give an accurate indication of land values and clearly Wiltshire Council will want to maximise the value of such a Capital receipt by timing the sale appropriately. Taking all of the factors into account, a reasonable approach is that the overall contribution from the three schools to the affordability gap be increased from £600,000 per annum to £700,000 per annum. This represents a total cost pressure of £100,000 against the Dedicated Schools Grant for 2012/13.
8. The actual cost pressure to be funded from the Wiltshire DSG, however, will be determined by how academies are funded from 2012/13. If the current recoupment methodology is retained then academies will be included in the overall DSG settlement and their budgets recouped from Wiltshire. In that instance the impact will be the full £100,000. Should recoupment cease, as has been indicated by recent consultations, then the affordability gap for the two academy PFI schools will be paid to Wiltshire by the DfE and the cost pressure on the Wiltshire schools budget will be the increased cost to Abbeyfield of £11,800.

## **Proposal**

9. It is proposed that
  - a. Schools Forum agrees to an additional amount of £100,000 be allocated to increase the contribution to the PFI Affordability Gap for the 3 PFI schools. this total will be amended if the recoupment methodology for funding academies is ceased by the DfE.

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## **Background papers**

The following unpublished documents have been relied on in the preparation of this report: None

## **Appendices**

Appendix 1: Revised Apportionment of Affordability Gap from 2012-13 onwards.

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