



West Lothian
Council

West Lothian Council
Schools Public Private Partnership
Revised Outline Business Case

February 2006

Contents

1.	Foreword.....	3
2.	Introduction.....	4
3.	Project Developments Post PPP2 Outline Business Case	5
4.	Ministerial Meeting.....	6
5.	Project Developments Post Ministerial Meeting	7
6.	PPP2 Preferred Bidder Status.....	8
7.	PPP2 Procurement Options	9
8.	Alternative Procurement Route.....	10
9.	Strategic Drivers.....	11
10.	Option Appraisal.....	13
11.	PPP3 Project Schools.....	14
12.	PPP Procurement Assessment	17
13.	Value for Money (VfM) Assessment Guidance	21
14.	Value for Money Assessment	23
15.	Revenue Funding Award	28
16.	PPP2 Project Funding Package	29
17.	Project Affordability	31
18.	Facilities Management	34
19.	Accounting Treatment and Balance Sheet Status.....	37
20.	Market Testing and Promotion.....	38
21.	Project Information	40
22.	Project Timescales.....	41
23.	Consultation Strategy.....	42
24.	Conclusion	43
	Appendix 1 - Revised Preferred Bidder letter July 2005.....	44
	Appendix 2 - Developments post revised Preferred Bidder letter.....	45
	Appendix 3 - Alpha Schools letter of 21 December 2005.....	51
	Appendix 4 - External Adviser Statement	57
	Appendix 5 - Optimism Bias.....	58
	Appendix 6 - VfM Assessment (HMT Model).....	60
	Appendix 7 - VfM Assessment (CPAM and Shadow Bid Model) ...	63
	Appendix 8 - HMT Model Sensitivity Analysis	65
	Appendix 9 - Shadow Bid and CPAM Model Sensitivity Analysis...	66
	Appendix 10 - Revenue Funding Award.....	67

1. Foreword

The council has undertaken procurement of the council's second schools Public Private Partnership (PPP2) in good faith and in a constructive and positive manner.

Unfortunately the council has been unable to reach agreement with the preferred bidder on key commercial terms and in recognition of certain project specific issues the council has concluded that the PPP2 project no longer represents best value for the council.

However the council recognises the opportunity and benefits of the PPP procurement process and is fully committed to utilising this procurement route to assist in addressing the priority investment requirements within the council's school estate.

This revised Outline Business Case (OBC) therefore seeks to demonstrate the business case for a revised PPP project which in conjunction with a conventionally procured project will endeavour to deliver an unprecedented level of investment to the community of West Lothian.

2. Introduction

The OBC submitted in December 2001 in support of the PPP2 project was successful in securing a conditional revenue funding award capped at £3.58million per annum in support of a project with a £50million capital value.

In seeking to progress this revised PPP project the council would be seeking to secure an equivalent revenue funding award. This would enable the council to deliver as a minimum the levels of capital investment proposed under the PPP2 project.

The revised OBC will provide an overview of the circumstances and events which have resulted in the council withdrawing the preferred bidder status from Alpha Schools (West Lothian) Ltd, and terminating the PPP2 procurement without awarding a contract.

The revised OBC has been developed in accordance with all relevant guidance and application notes issued by the HM Treasury and the Financial Partnerships Unit of the Scottish Executive.

3. Project Developments Post PPP2 Outline Business Case

Alpha Schools (West Lothian) Ltd ("the consortium"), a consortium of Morrison Project Investments Limited and Noble Fund Managers Limited, was invited as one of two pre-qualified bidders to submit a tender bid against the council's Invitation to Negotiate (ITN) issued in February 2004 for the PPP2 project.

The ITN bid submissions were received at the end of June 2004 and during the bid evaluation process both bidders were invited to submit an improved bid through a Revise & Confirm bid process. This was undertaken between September 2004 and October 2004. At the beginning of November 2004 the consortium was advised that they would be awarded preferred bidder status subject to their acceptance of the terms of the appointment, as negotiated between the parties at that time.

The preferred bidder appointment was confirmed in December 2004 and at that stage financial close was scheduled for April 2005 with construction works completion by October 2006.

In March 2005 the consortium advised the council that the bid development had not been progressing as reported and that financial close would not occur until October 2005 with works completion by August 2007. Following a period of protracted negotiation the parties reached agreement on the revised terms of the preferred bidder appointment in May 2005.

[REDACTED]

On 23 June 2005 the council received a letter from the consortium advising that the previously agreed terms would need to be re-negotiated. At the same time the council was advised that the project programme had slipped again with contract award re-scheduled for December 2005.

[REDACTED]

[REDACTED]

In light of the ongoing problems being experienced the council sought a meeting with the Minister for Education and Young People to discuss the issues at hand.

4. Ministerial Meeting

The meeting with the Minister for Education and Young People on 6 July 2005 provided the council with the opportunity to discuss the problems being experienced in progressing the preferred bidder negotiations with the consortium.

The Minister was advised of the council's difficulties in dealing with the consortium, the agreement of revised financial terms in May 2005, the subsequent revised terms submitted by the consortium in June 2005,



At this meeting the council discussed the suitability of PPP procurement route for refurbishment projects and outlined an alternative strategy for delivering an equivalent level of capital investment, which was dependent on the conditional revenue funding award of £3.58million being converted into revenue support grant to support prudential borrowing.

At this stage the Minister advised that whilst it was acknowledged that the council had undertaken all reasonable measures to ensure the project continued he would be unable to approve the diversion of the PPP2 revenue funding award in support of a conventionally procured project.

Consequently the council's preferred option at the time was to continue with the consortium on the basis of the terms previously agreed between the parties in May 2005.

The Minister did acknowledge that in the event of the consortium rejecting the council's position, and therefore the preferred bidder status being withdrawn, that the Scottish Executive and the council would need to enter into immediate negotiations to develop an alternative strategy for delivering the schools investment.

5. Project Developments Post Ministerial Meeting

Following the Ministerial meeting on 6 July 2005 the consortium were advised that the revised terms received on 23 June 2005 were not acceptable, but that the terms negotiated in May 2005 would remain on offer, and that subject to further terms the revised programme date would be acceptable.

On 13 July 2005 the council received a letter from the consortium confirming that the council's terms would be accepted. The preferred bidder negotiations and terms agreed at that time are set out in Appendix 1.

In the subsequent period the council has sought to negotiate the finalised commercial terms but revised proposals tabled by the consortium culminating in the consortium's letter of 21 December 2005 have resulted in increased costs, further revised timescales and amended specifications. The project developments post the Ministerial meeting are summarised in Appendix 2.

The consortium's letter of 21 December 2005, as detailed in Appendix 3 advised the council of the consortium's final position, which was open for acceptance by noon on 23 December 2005.

In a response issued on 23 December 2005 the council advised the consortium that the council was unable to respond in the manner requested and within the timescales set due to the nature of the information received.

The consortium was subsequently advised in a letter dated 6 January 2006 that the revised commercial terms were unacceptable and that a report would be submitted to the council's Policy, Partnership and Resources Committee recommending the withdrawal of the consortium's preferred bidder status.

6. PPP2 Preferred Bidder Status

At the council's Policy, Partnership and Resources Committee on 7 February 2006 the committee reached a decision that the revised terms on offer from the preferred bidder did not represent best value for the council.

The council has subsequently advised the consortium that the council will be terminating the current procurement without awarding a contract.

This decision was taken after a substantial period of time and resource had been devoted by the council in seeking to reach agreed terms with the consortium, and was only taken after consideration of all other available options.

A statement from the council's external financial, legal and technical advisers in support of the decision taken by the council is set out in Appendix 4.

7. PPP2 Procurement Options

Reserve Bidder

In seeking to preserve the revised PPP2 project the council considered approaching the reserve bidder, West Lothian Schools Partnership, however it is now some 14 months since the council awarded preferred bidder status to the consortium.

Furthermore the reserve bidder was a loose alliance of potential equity investors and principal sub-contractors, and following subsequent developments elsewhere with the Scottish Schools PPP market it is the council's understanding that the reserve bidder is no longer active in the Scottish Schools PPP market.

Re-tendering Revised PPP2 Project

The council has also considered re-tendering the revised PPP2 project and seeking new expressions of interest from the market.

However following the experience of the last 2 years and developments elsewhere in other schools PPP projects the council and its external advisers have concluded that there is no market appetite for refurbished schools PPP projects.

8. Alternative Procurement Route

The council and its external advisers have identified an alternative procurement route comprising of PPP and conventional procurement to deliver the required level of investment in the 5 project schools.

The council would seek to deliver 2 new secondary schools to replace the existing Armadale Academy and Deans Community High School through a revised PPP project (PPP3).

At the same time the council would seek to deliver the refurbishment and extension of the remaining 3 project schools, Inveralmond Community High School, The James Young High School and St. Kentigerns Academy through conventional procurement.

9. Strategic Drivers

The OBC for the PPP2 project identified 3 strategic drivers for the project:

- To provide sufficient schools places to meet current and proposed Edinburgh and Lothian Structure Plan and related Local Plan commitments.
- To improve building condition and suitability of accommodation.
- To support the council's social inclusion initiatives.

The strategic drivers for this revised OBC remain unchanged.

- Capacity

The recently published 2004 based population projections indicate that West Lothian's population is expected to increase to 196,439 by 2024, an increase of 33,599 (20.6%).

It is therefore essential that West Lothian establish an appropriate infrastructure to support the additional housing units scheduled for West Lothian over the next 10 to 15 years under the current Edinburgh and Lothian Structure Plan.

The PPP2 project sought to deliver an additional 550 pupil places across 3 of the 5 schools in order to meet capacity pressures. The critical strategic driver for the proposed PPP3 project remains one of school capacity and the council will now seek to deliver an additional 660 pupil places.

- Building Condition

The council's property asset management plan for schools had previously identified a requirement to invest some £106million to address issues relating to condition, suitability, capacity and risk management in the period to 2006.

The survey findings arising from the comprehensive range of structural and site investigations undertaken by the consortium have identified specific concerns of varying degree at each of the 5 project schools which confirm the risk assessment and prioritisation determined at the time of the OBC for the PPP2 project.

- Social Inclusion

The proposed PPP3 project and the conventional project will continue to support the council's range of social inclusion initiatives which will include the use of the facilities by pupils and/or community users with special educational and physical needs, multi-agency working and access by the wider community during school hours and outwith school hours through the development of flexible design solutions and multi-use facilities.

10. Option Appraisal

In seeking to determine the optimum scope for the alternative procurement route the council's strategic drivers of capacity, building condition and social inclusion have been used to rank the 5 project schools. This exercise has allowed the council to prioritise which schools should be progressed under the proposed PPP3 project.

In order to minimise the timescales to deliver the new build secondary schools the proposed PPP3 project has been progressed on the premise that the new build schools would be built on the existing schools sites. Consequently a fourth category of site suitability was included in the scored assessment.

For each category the schools were ranked in priority order, the school with the most pressing need was allocated a maximum score of 5. The exception to this rule was the category of new build site suitability where the school with the largest site area received the maximum score. Each category was allocated an equal weighting. The final project assessment score is set out below in table 1.

Table 1 - Project Assessment Score

	Capacity	Building Condition	Social Inclusion & DDA	Total Score	NewBuild Site Suitability	Revised Total Score
Armadale Academy	3	5	4	12	2	14
Deans Community High	2	4	5	11	4	15
Inveralmond Community	4	3	1	8	3	11
St Kentigerns Academy	5	2	2	9	1	10
The James Young High	1	1	3	5	5	10

The project score assessment has identified Armadale Academy and Deans Community High School as the highest priorities for replacement in both the total score, based on the strategic drivers, and the revised total score incorporating site suitability.

The council's preferred option is therefore to progress on the basis of 2 new build replacement secondary schools at Armadale Academy and Deans Community High School for the proposed PPP3 project.

11. PPP3 Project Schools

Armadale Academy

Armadale Academy, opened in 1968, is a sixth year comprehensive, non-denominational school with a current capacity of 990 pupils.

The school is, in part, single, double and three storied, set into a sloping site, which necessitates various changes in level.

- Capacity

The PPP2 project sought to refurbish and extend the school to accommodate a school roll of 1100 pupils and to meet the requirements of a modern curriculum.

Further capacity pressures arising from planned housing developments within the Armadale area have resulted in a revised school roll of 1210 pupils under the proposed PPP3 project.

Armadale Academy's accommodation requirements will be extended to accommodate the additional area requirements of the Scottish Executives reduced class sizes in S1 and S2 for Mathematics and English, increased PE provision and other curriculum and schools management needs.

- Building Condition

During the PPP2 preferred bidder negotiations the consortium commissioned an extensive range of surveys including site investigation surveys, topographical surveys, CCTV surveys of existing drainage, elevational surveys, measured surveys, roof surveys and rot/damp surveys.

Initial site investigations undertaken at Armadale Academy have identified specific concerns in relation to damp and water penetration at the school. Following a further range of extensive surveys during the summer months in 2005 the council received the survey findings which confirmed extensive damp and water penetration throughout the entire ground floor of the school.

In October 2005 the council determined the most appropriate solution to be a new build replacement for the existing school and sought to progress the new build through conventional procurement.

- Social Inclusion

A key priority for the PPP2 project was the provision of a design solution, which would release the pressure on the existing circulation routes and provide the necessary design alterations to resolve the many changes in level to meet the council's accessibility requirements and provide full access and integration of students and other users who have additional support needs.

- School Site

The existing site of approximately 61,100m² is of sufficient size to accommodate a new build school on the existing playing fields with the external facilities being relocated on the site of the existing school buildings.

Deans Community High School

Deans Community High School, opened in 1978, is a sixth year comprehensive, non-denominational school with a capacity of 1100 pupils and extensive community facilities.

The school exploits a rise in ground level within an extensive site, however the configuration of the school on a multi-winged layout means that circulation routes are extensive and incorporate many changes in levels.

- Capacity

The project sought to refurbish and extend the school to accommodate a school roll of 1100 pupils and to meet the requirements of a modern curriculum.

With Deans Community High School being one of two community high schools within West Lothian the PPP2 project sought to refurbish the community facilities to meet the requirements of the community users.

The proposed PPP3 project will seek to provide the same capacity requirements but will provide an opportunity to reassess the manner in which both school and community facilities are structured and function.

Deans Community High Schools accommodation requirements will be extended to accommodate the additional area requirements of the Scottish Executives reduced class sizes in S1 and S2 for Mathematics and English, increased PE provision and other curriculum and schools management needs.

- Building Condition

The range of surveys undertaken by the consortium identified a number of specific issues in relation to building fabric and structure. The school has serious problems with the condition of the external render, with significant areas identified as requiring urgent attention. The roof covering is reaching the end of its service life and the parapets show signs of severe deterioration with open joints leaving the roof vulnerable to water ingress.

The heating system has been another area of concern with no local controls and old plant equipment often giving rise to overheating and/or failing. Lack of adequate ventilation and cooling was also identified as another factor in overheating.

The consortium had advised that the internal fabric and finishes had deteriorated to such an extent that from the lifecycle perspective that they had deemed it more economical to opt for replacing than retaining the majority of the elements.

- Social Inclusion

The change in levels is a major problem for Deans Community High School. A key priority for the PPP2 project was the provision of a design solution, which would minimise the existing extensive circulation routes and many changes in level to meet the council's accessibility requirements and provide full access and integration of students and other users who have additional support needs.

The opportunity to redesign the entire school under a new build project would enable the school to operate as a genuine community high school with unrestricted open access to all.

- School Site

The existing site of approximately 76,900m² is of sufficient size to accommodate a new build school on the existing playing fields with the external facilities being relocated on the site of the existing school buildings.

12. PPP Procurement Assessment

In accordance with HM Treasury Guidance and the Scottish Executive's Application Note the council has undertaken the Stage 2 - Project Level Assessment to test the suitability of the PPP procurement route against conventional procurement.

Viability

Objectives and Outputs

- Can service requirements be stated in clear objective output based terms?

A clear output specification will be used as the basis for service delivery.

Operational Flexibility

- Can effectiveness of service delivery be measured and monitored?

The service will be monitored and measured on the basis of the Scottish Schools Standard PPP contract.

- Can operational flexibility be maintained over the lifetime of the contract?

The contract structure to be adopted will be the Scottish Schools Standard PPP contract.

Equity and Accountability

- Are there public equity reasons for providing the service directly?

There are none noted at this stage.

- Are there accountability reasons for providing the service directly?

There are none noted at this stage.

Regulation and Legislation

- Are there any regulatory reasons for providing the service directly?

There are none noted at this stage.

- Are there any legal reasons for providing the service directly?

There are none noted at this stage.

With reference to the above characteristics, the council and its external advisers are satisfied that there are no specific reasons as to why the service to be provided by the proposed PPP3 project require to be provided by the public sector.

The council and its external advisers are satisfied that the proposed service can be captured in an output specification and contract based approach.

Finally the council is satisfied that the Scottish Schools Standard PPP Contract will provide an operable contract with built in flexibility to overcome any strategic and regulatory issues which may arise.

Desirability

Risk Management

- Does the project involve the purchase of a capital asset?

The project will involve the purchase of the asset over the contract period.

- Are the risks of cost and time overruns likely to be significant?

Risks of cost and time overrun could be significant.

- Are there significant operational risks?

Operational risks could be significant as a result of the service specification and payment mechanism.

Innovation

- Is there likely to be scope for innovation in service delivery?

There will be scope for innovation, specifically through the design process.

Service Provision

- Are there good strategic reasons to retain soft services in house?

At this stage the position on the retention of soft services has still to be determined.

- Is soft service transfer essential for achieving improved service delivery?

The transfer of soft services will not be essential.

Incentivisation

- Is incentivisation likely to result in enhanced service delivery?

Incentivisation will be delivered via the Scottish Schools Standard PPP contract payment mechanism.

Lifecycle Costs and Residual Value

- Is it possible to integrate asset, design, construction and operation?

This will be possible.

- Is it possible to achieve significant whole life cost savings?

This will be possible.

With reference to the above characteristics the council and its external advisers are satisfied that the relevant benefits of the PPP procurement route arising from better risk management, innovative design and contractual incentives would outweigh the higher cost of private sector capital.

Achievability

Transaction Costs and Client capability

- Is there sufficient client side capability to manage the procurement?

The council has developed a dedicated project team complemented by a team of external advisers.

- Can appropriately skilled procurement teams be assembled?

The council's project team comprises of financial, legal, technical and educational professionals and is assisted by external financial, legal and technical advisers.

- Is there a sufficient budget to fund the procurement process?

The council has allocated specific resources in support of the project team and external advisers.

Competition

- Is there evidence that the private sector can deliver the required outputs?

The strength of the current market in schools PFI/PPP is evidence that the private sector can deliver new build PFI/PPP schemes.

- Is there likely to be sufficient market appetite for the project?

The council and its external advisers are satisfied that there will be sufficient market interest in the revised project.

The council is satisfied that it has an achievable project programme, appropriately resourced internal project team supported by appropriate external advisers.

The council and its external advisers are satisfied that, following the council's decision to withdraw the preferred bidder status from the consortium, there will be sufficient interest and capacity within the market for the proposed PPP3 project.

13. Value for Money (VfM) Assessment Guidance

In developing this proposal the council has considered the revised PPP project against the characteristics identified in the Scottish Executive's VfM Assessment Guidance Application Note as set out below:

- Is there a major capital investment requiring management of delivery and construction?

The proposed capital value is in excess of £50million.

- Is there evidence that the private sector can deliver this project/programme and that it is likely to be VfM?

Current market practice would suggest that the private sector can deliver the revised project, and that it is likely to prove to be value for money.

- Is the service capable of being defined in service outputs?

The service can be defined in service outputs and the council will work in conjunction with its external advisers to produce a full output specification.

- Is a whole life costing possible?

The revised project will be tendered on the basis of whole life costings in line with current market practice.

- Confirm that procurement costs are not disproportionate to total costs.

The council and its external advisers are of the view that the procurement costs are not disproportionate to the total cost.

- Is there a technology stable market?

The revised project does not incorporate any high technology aspects.

- Confirm that planning for asset use over the long term has been conducted.

The council is satisfied that there is a demand for the asset over the long term.

- Confirm that appropriate incentivisation for the private sector to perform has been considered.

The council will adopt the Scottish Schools Standard PPP contract incorporating the standard payment mechanism.

The council and external advisers are satisfied that the proposed PPP3 project is fully consistent with all of the above characteristics, and have concluded that there is a strong case for progressing the proposed PPP3 project.

14. Value for Money Assessment

In seeking to determine whether the PPP procurement route is the appropriate route for the delivery of the 2 new build secondary schools the council has undertaken a quantitative value for money assessment of the proposed PPP3 project.

In accordance with the Application Note the council has used the generic HM Treasury VfM Quantitative Evaluation Spreadsheet to test the proposed revised PPP projects VfM position.

At the same time the council has developed a bespoke Conventional Procurement Assessment Model (CPAM) and Shadow Bid Model to complement HM Treasury model assessment.

However in accordance with the VfM guidance the council has not sought to reconcile the HM Treasury model with the CPAM and Shadow Bid Models.

The quantitative assessment has considered a range of factors, including:

- Capital works costs
- Lifecycle works costs
- Facilities Management (operating) costs
- Transaction costs
- Risk and optimism bias

In conjunction with the council's external technical advisers the council has developed indicative costings for the capital works, lifecycle works and facilities management services associated with the proposed PPP3 project.

- Capital works costs

The capital works costs have been developed based on the accommodation schedules and specifications for the PPP2 project as amended to reflect increased areas to accommodate the changing curriculum and management requirements of Armadale Academy and Deans Community High School.

The revised gross internal floor areas have been multiplied by indicative market rates as amended to reflect ground conditions identified in the site investigation surveys, as well as demolition costs for the removal of the existing structures.

- Lifecycle works costs

The lifecycle works costs are based on current market rates and profiles.

- Facilities Management (operating) costs

The facilities management costs have been developed based on the service specification developed for the PPP2 project as amended to reflect the assumptions made on lifecycle maintenance costing.

- Transaction costs

The transaction costs have been developed by the council's external technical and financial advisers based on benchmark data for comparable PPP projects.

These indicative costings have been found to be comparable to benchmark data derived from other comparable PPP schemes and have been incorporated into the shadow bid model.

At the same time the council has calculated indicative costings for the above inputs under an equivalent conventionally procured project.

- Risk and Optimism Bias

The key criterion for effective risk management is that the party best able to manage a risk should carry that risk, receiving the costs and benefits associated with the risk.

In developing the business case for the revised PPP project the council has undertaken a detailed assessment of the project specific risks. The key project specific risks are set out below:

- Insurance
- Planned lifecycle maintenance costs variance from budget
- Unplanned lifecycle maintenance costs
- Construction cost overrun from tender to completion
- Design cost overrun
- Construction time Overrun
- Design time overrun

- Cost overruns in service provision
- Inadequate provision of Services resulting in reduction of fees or other losses
- General change in law
- Malicious damage
- Uninsurable risk
- Wage cost inflation
- Non wage cost inflation

At the same time, in accordance with the revised HM Treasury Green Book Guidance the council has undertaken an optimism bias assessment of the proposed PPP3 project.

The detailed optimism bias analysis is set out in Appendix 5.

Quantitative Risk Assessment

To quantify the probable cost of each of the above project specific risks the expected value of each risk have been costed and then weighted by the probability of the event occurring to arrive at the probable value of each risk.

Wherever possible the council has sought to use external objective measurements for determining the expected value and/or probability of each risk.

The calculated expected value of the above project risks is set out over in table 2.

Table 2 - Expected Value of Key Project Specific Risks

		Value	Probability of occurrence	Expected Value
1	Insurance	193,364	Medium	96,682
2	Planned Lifecycle	689,382	High	517,036
3	Unplanned Lifecycle	1,818,357	High	1,363,768
4	Construction Cost Overrun	4,839,172	Very High	4,597,213
5	Design Cost Overrun	169,452	Medium	84,726
6	Construction Time Overrun	250,913	High	188,185
7	Design Time Overrun	46,565	High	34,924
8	Cost Overruns in Service Provision	843,918	Medium	421,959
9	Inadequate provision of Services resulting in reduction of fees or other losses	781,979	Medium	390,989
10	General Change in Law	616,770	Medium	308,385
11	Malicious Damage	386,058	Very High	366,755
12	Uninsurable Risk	510,209	Low	127,552
13	Wage Cost Inflation	229,233	Medium	114,616
14	Non Wage Cost Inflation	234,364	Medium	117,182
	Total	11,609,735		8,729,973

Value for Money Assessment

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

In accordance with the Application Guidance Note the council has not sought to reconcile the results of the HMT Treasury model with the Shadow Bid Model and CPAM.

Sensitivity Analysis

The council has calculated the indifference points for capital expenditure and unitary charge under the HMT Treasury Model. The sensitivity analysis is undertaken via the indifference points scenarios modelled.



The council has undertaken a range of sensitivities of different input assumptions to the shadow bid model, including different risk scenarios, to assess the impact on the above value for money assessments.

The following sensitivities have been modelled at this stage:

- Inflation: +/- 0.5%, and +/- 1% on base assumption
- Interest Rates: +/- 50bps and +/- 100bps on base assumption
- Capital Works costs: + 2.5% and + 5% on base assumption

The results of the sensitivity testing are set out in Appendix 9.

15. Revenue Funding Award

The council has calculated that the eligible level of capital value would exceed the £50million upon which the current conditional funding award was based.

Subject to the Scottish Executive's evaluation that the PPP procurement route is a suitable procurement route for the proposed new build secondary schools, the council would anticipate a revised conditional funding award of £3.58million per annum over 30 years.

The detailed calculations are set out in Appendix 10.

16. PPP2 Project Funding Package

At the time of the preferred bidder appointment the consortium's bid price ranged from £9.52million for a bank funded unitary charge to £9.19million for a bond funded unitary charge, as against a Revise & Confirm bid affordability target of £9.3million in 2007/08.

In seeking to incorporate an appropriate provision within the council's financial model the midpoint between the consortium's bank funded unitary charge and the Revise & Confirm bid affordability target was selected as the indicative unitary charge, resulting in a provisional first full year's unitary charge of £9.41million in 2007/08.

Revenue Budget Pressure

Under the terms of the Scottish Executive's revenue funding award the council would receive £3.58million per annum for 30 years toward the cost of the PPP2 project. This would be augmented each year by £1.95million of existing revenue budgets resulting in total resources of £5.53million per annum.

At the same time the council would seek to use the relaxation of the Schools Fund capital grant in support of the PPP2 project converting the £2.62million allocation into additional revenue support grant to further increase the resources available to fund the PPP2 project cost.

The total resources available to fund the first full year unitary charge would increase to £8.15million resulting in a revenue budget pressure of £1.26million in 2007/08.

In seeking to minimise the impact on the 2005/06 and 2006/07 revenue budgets the Schools Fund would be used in part to fund the revenue budget pressure identified in each year.

Indexation

The unitary charge payment would be subject to annual contract indexation calculated at 2.5% per annum. This would equate to a further £235,000 in 2008/09 resulting in a revised revenue funding pressure of £1.49million in 2008/09, increasing to £1.98million by 2010/11.

Capital Contributions

The above position was dependent on the council making an upfront capital contribution at contract award. In seeking to minimise the first full year unitary charge, council had previously approved a £5million upfront capital contribution.

This capital contribution was increased by a further £2.53million as a result of an additional School Fund capital grant for the 3 year period to 2007/08 to address reduced class sizes in Mathematics and English in S1 and S2. At the same time the council was successful in securing New Opportunities Fund Lottery funding of some £1.18million toward the additional cost of providing synthetic pitches at 3 of the project schools.

After offsetting £930,000, toward the cost of new furniture and equipment for the 5 schools, a revised upfront capital contribution of £7.78million was identified.

The consolidated PPP2 funding package as at November 2004 is set out below in table 3.

Table 3 – Consolidated PPP2 Funding Package

	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
	£m	£m	£m	£m	£m	£m
Project Cost:						
Unitary Charge	0.00	4.70	9.41	9.64	9.88	10.13
Interim Services	2.32	0.98	0.00	0.00	0.00	0.00
Total	2.32	5.68	9.41	9.64	9.88	10.13
Funding Package:						
Revenue Support Award	0.00	(1.79)	(3.58)	(3.58)	(3.58)	(3.58)
Existing Revenue Budgets	(1.95)	(1.95)	(1.95)	(1.95)	(1.95)	(1.95)
Schools Fund	(0.37)	(1.94)	(2.62)	(2.62)	(2.62)	(2.62)
Revenue Budget Pressure	0.00	0.00	(1.26)	(1.49)	(1.73)	(1.98)
Total	(2.32)	(5.68)	(9.41)	(9.64)	(9.88)	(10.13)
Capital Resources:						
Capital Contribution -	(5.00)	0.00	0.00	0.00	0.00	0.00
Schools Fund - Class Size Reduction	(0.68)	(0.84)	(1.00)	0.00	0.00	0.00
NOF Grant	0.00	0.00	(0.83)	(0.35)	0.00	0.00
Furniture & Equipment	0.00	0.43	0.50	0.00	0.00	0.00
Total	(5.68)	(0.41)	(1.33)	(0.35)	0.00	0.00

17. Project Affordability

Proposed PPP3 Project

The council's external technical and financial advisers have assisted the council in developing a shadow bid model for the PPP 3 project. The nominal capital investment level for the 2 new build schools is estimated at £56million and the first full year unitary charge is estimated at £6.9million.

With the construction works scheduled for completion by the end of May 2009 the council would require to make a part year unitary charge payment, covering 10 months, in 2009/10 with the first full year unitary charge being payable in 2010/11. The proposed PPP3 funding package is set out below in table 4.

Table 4 - Proposed PP3 Funding Package

	2009/10 £m	2010/11 £m
PPP3 Project Cost:		
Unitary Charge	5.61	6.90
Funded By:		
Revenue Support Award	(2.98)	(3.58)
Existing Revenue Budgets	(0.65)	(0.78)
Schools Fund	(2.62)	(2.62)
Revenue Budget Pressure	(1.73)	(1.98)
Total	<u>(7.99)</u>	<u>(8.96)</u>
Funding Package Surplus	(2.38)	(2.06)
Reconciled by:		
Existing Revenue Budgets	(0.65)	(0.08)
Revenue Budget Pressure	(1.73)	(1.98)
Total	<u>(2.38)</u>	<u>(2.06)</u>

The council would seek to maximise the use of the Scottish Executive's revenue funding award and Schools Fund grant and by 2010/11, based on the PPP2 funding package, the council would have a funding package surplus of £2.06 million per annum which would be available to fund the conventionally procured project via prudential borrowing.

Conventional Project

As set out above the proposed PPP3 project would generate a funding package surplus of £2.06million in 2010/11. At the same time the existing PPP team budget of £215,000 would be available post construction completion to fund prudential borrowing. These combined revenue resources could deliver £34.13million of prudential borrowing.

This is a significant level of additional borrowing to be funded and it is acknowledged that there are risks associated with the planned levels of prudential borrowing. In particular, Scottish ministers retain the power to impose limits on borrowing although there are no indications at this stage that this is due to be introduced.

At the same time a combination of revenue and capital contributions as offset by bid procurement and maintenance costs would provide a further £20.76million, resulting in a total nominal capital expenditure of some £54.89million. This would equate to £48.03million in current day prices.

The conventional project funding package is set out below in table 5.

Table 5 – Conventional Project Funding Package

	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Total
	£m	£m	£m	£m	£m	£m	£m
Capital Investment:							
Capital Contribution - 2005/06	5.00	0.00	0.00	0.00	0.00	0.00	5.00
Schools Fund - 2005/06 to 2008/09	0.37	1.97	2.62	2.62	0.00	0.00	7.58
Schools Fund - Class Size Reduction	0.68	0.84	1.00	0.00	0.00	0.00	2.53
Survey Costs	(0.65)	0.00	0.00	0.00	0.00	0.00	(0.65)
Maintenance Reserve	(0.75)	0.00	0.00	0.00	0.00	0.00	(0.75)
PPP Project Team Costs	(0.05)	(0.20)	(0.20)	0.00	0.00	0.00	(0.45)
Revenue Funding Pressure	0.00	0.00	1.26	0.00	0.56	0.00	1.82
Prudential Borrowing	0.00	0.00	0.00	27.08	3.60	3.45	34.13
NOF Grant	0.00	0.00	0.83	0.35	0.00	0.00	1.18
Developer Contributions	0.00	0.00	0.00	0.50	1.50	2.50	4.50
Total (Nominal)	4.60	2.61	5.52	30.55	5.66	5.95	54.89
Cummulative Total (Nominal)	4.60	7.22	12.73	43.28	48.94	54.89	

With a combined nominal capital value of £110.89million the alternative procurement route would enable the council to undertake an unprecedented level of capital investment project across the 5 project schools.

Lifecycle Maintenance

The proposed PPP3 shadow bid model is modelled on the basis of the same indexation assumptions as the PPP2 project and assumes a constant indexation rate of 2.5% per annum. The differential between the PPP2 and PPP3 indexation is equal to £80,000 in the first year, increasing by an equivalent amount each year thereafter.

Based on the long term funding package developed to fund the 5 schools project the council could use the indexation differential to establish, within 6 years of the works completion, a lifecycle reserve equal to £0.5million per annum to address the lifecycle provisions of the conventionally procured project schools. This lifecycle reserve would complement the existing property maintenance budgets within the existing revenue budgets.

18. Facilities Management

Transfer of Employees

The council considers that the implementation of the revised PPP project is likely to give rise to a transfer of undertakings under the Transfer of Undertakings (Protection of Employment) Regulations 1981. The project will be structured to deliver bid submissions, which protect the employment rights of support service staff who may transfer under TUPE Regulations.

Staffing Protocol

The council will be implementing the Scottish Executive's "Public Private Partnerships Protocol and Guidance Concerning Employment issues" (the "Staffing Protocol"). As such the proposed PPP3 project staffing costs have been calculated on the basis of all staff being on similar terms and conditions with the same or broadly comparable pension benefits.

Best Value testing of Soft Facility Management Services

PPP projects have traditionally included the transfer of most soft and hard facilities management services to the PPP contractor, supported as appropriate by staff transfers.

This had been deemed necessary to achieve an appropriate level of risk transfer to establish a value for money position, maximise operational efficiency, and to avoid subsequent interface and cost problems.

However in progressing the PPP2 project, and in accordance with the Staffing Protocol, the council considered other options for utilising the council's existing in-house facilities management service providers to deliver elements of the facility management services.

In order for the council to determine whether the inclusion of all or part of the facilities management services represented best value, the council's in-house service providers were invited to submit bids for the provision of core soft elements of cleaning, grounds maintenance and waste management services.

Through a series of mandatory variant bids the council obtained a range of soft facility management bids from Alpha Schools (West Lothian) Ltd and West Lothian Schools Partnership based on the following scenarios:

- Cleaning & waste management services excluded from the PPP contract.

- Grounds maintenance services excluded from the PPP contract

At the same time the in-house service providers were required to submit bids based on the PPP service specification standards:

- Cleaning & waste management services sub-contracted to the council's in-house service provider.
- Grounds maintenance services subcontracted to the council's in-house service provider.

Alpha Schools (West Lothian) Ltd and West Lothian Schools Partnership were provided with details of the revised service specification. Both bidders were instructed to price those elements excluded from the revised service specification thus ensuring that the bid prices received from the in-house service providers could be equalised with the standard bid received from each PPP bidder.

A price and qualitative assessment of the mandatory variant bids was then undertaken using the evaluation criteria developed for the standard bids.

On the basis of the analysis undertaken the council concluded that best value would be obtained by excluding the soft elements of cleaning & waste management and grounds maintenance from the PPP2 contract.

Market Position

Throughout the PPP2 bid development and evaluation process neither bidder expressed concern at the market testing and subsequent rescoping of FM services.

The elements of cleaning & waste management and grounds maintenance are normally delivered at a level below the principal FM sub-contractor, and consequently are unlikely to be a core business issue for either the equity investors and/or principal FM sub-contractor.

It is therefore unclear as to whether there would be any specific market interest in a contract to deliver these particular services at 2 secondary schools within the context of the PPP service specification and payment mechanism.

Proposed PPP3 Scope of Services

The council is of the opinion that the best value testing undertaken at the time of the preferred bidder evaluation remains a valid assessment but is fully aware of the Scottish Executive's position on the exclusion of the above soft FM services at this stage.

In recognition of this position the council would seek to defer any final decision on the exclusion of the above soft FM services until after the prequalification of bidders.

This would enable the parties concerned to establish the extent to which there is an appetite among the pre-qualified bidders for the retention or otherwise of the above soft FM services.

For the avoidance of doubt all hard FM services covering security, building maintenance and the hard elements of cleaning (i.e. high level and deep cleaning services) and grounds maintenance of synthetic pitches would remain within the PPP project scope.

19. Accounting Treatment and Balance Sheet Status

In conjunction with the council's external financial advisers the council has undertaken a preliminary review of the accounting treatment and balance sheet status and has concluded that the project should obtain an off balance sheet status.

20. Market Testing and Promotion

In bringing the proposed PPP3 project to the market the council would seek to publish a Prior Information Notice (PIN) in February 2006 advising the market of the council's proposals to progress a revised PPP project.

Following the issue of the PIN, the council will undertake a comprehensive market testing exercise to raise the profile of the project and determine the level of interest within the market for the proposed revised PPP project.

The council is fully aware of issues of perception that will need to be addressed by promoting the project and generating the appropriate level of interest for both the proposed PPP3 project and conventionally procured projects.

The council would seek to build upon the following factors in promoting the project:

- Political Commitment

To withdraw from the preferred bidder negotiations at this stage in the process has been a major decision for the council.

The decision to re-scope and propose a revised PPP project indicates a clear and strong commitment to the PPP procurement process.

At the same time the proposal to progress a conventionally procured project illustrates an acknowledgement that the PPP procurement route does have limitations, with regard to the refurbishment projects.

- Project Scope, Value and Timescales

The council is aware of 8 new build schools PPP projects of comparable size to the proposed PPP3 project being progressed by other local authorities.

The council's external advisers have advised that the proposed PPP3 project scope, comprising of 2 new build secondary schools, project value and timescales would be attractive to the market.

- Council Project Team

The council has established a core project team with significant experience in progressing the council's first schools PPP project and most recently in progressing the PPP2 project.

At the same time the council has extended the appointment of the council's experienced external advisory team of Grant Thornton, Shepherd + Wedderburn and Turner & Townsend Project Management to assist the council in delivering the proposed PPP3 project.

- Location

The council is well placed within the central belt/M8 corridor to attract bids from existing PPP contractors in neighbouring authorities and/or new entrants to the PPP market.

- Project Affordability

The council is fully aware of mistaken concerns the market may have that the project's problems have arisen as a result of project affordability. Consequently the council will seek to give all possible assurances to the market that the decision to withdraw from the preferred bidder negotiations with the consortium was as a result of the consortium's proposals not representing best value.

The council's external advisers will play a key role in assisting the council in this process.

Upon securing the required conditional revenue funding award and the completion of the pre-OJEU Key Stage Review the council would publish an OJEU Notice seeking expressions of interest for the proposed PPP3 project.

21. Project Information

As part of the preferred bidder negotiations the council had entered into a licence agreement with the consortium's construction sub-contractor Morrison Construction Services Ltd to secure warranted survey information for the project schools in the event financial close was not secured.

The survey information available to the council is detailed below:

- Measured Surveys
- Site Investigations
- Topographical Surveys
- Elevational Surveys
- Drainage Surveys
- Rot and Damp Surveys
- Utility Detection and Mapping Surveys

The above survey investigation information will provide essential project information on site and building conditions and will be of prime importance to both the council and prospective bidders in progressing both the revised PPP project and conventional projects.

At the same time outline planning applications have been submitted for the existing sites at Armadale Academy and Deans Community High School. The council's planning department has already confirmed that environmental impact assessments will not be required and as such outline planning permission should be secured within 6 to 8 weeks.

22. Project Timescales

The PPP2 ITN project programme sought the selection of the preferred bidder by October 2005 with financial close by April 2005 and works completion by October 2006.

The events of the last 12 months have delayed the project. The project timescales for the proposed PPP3 project and conventional procurement projects are set out below in table 6.

Table 6 - Project Timescales

	PPP3	Conventional Procurement
PIN	Feb-06	N/A
OJEU Notice	Mar-06	Jun-06
Bidder Prequalification	May-06	Sep-06
Bid Submissions/Tender Period	Sep-06	Oct-06
Preferred Bidder	Dec-06	N/A
Council Approval	Apr-07	Feb-07
Contract Award	May-07	Feb-07
Construction Completion	May-09	Jan-09

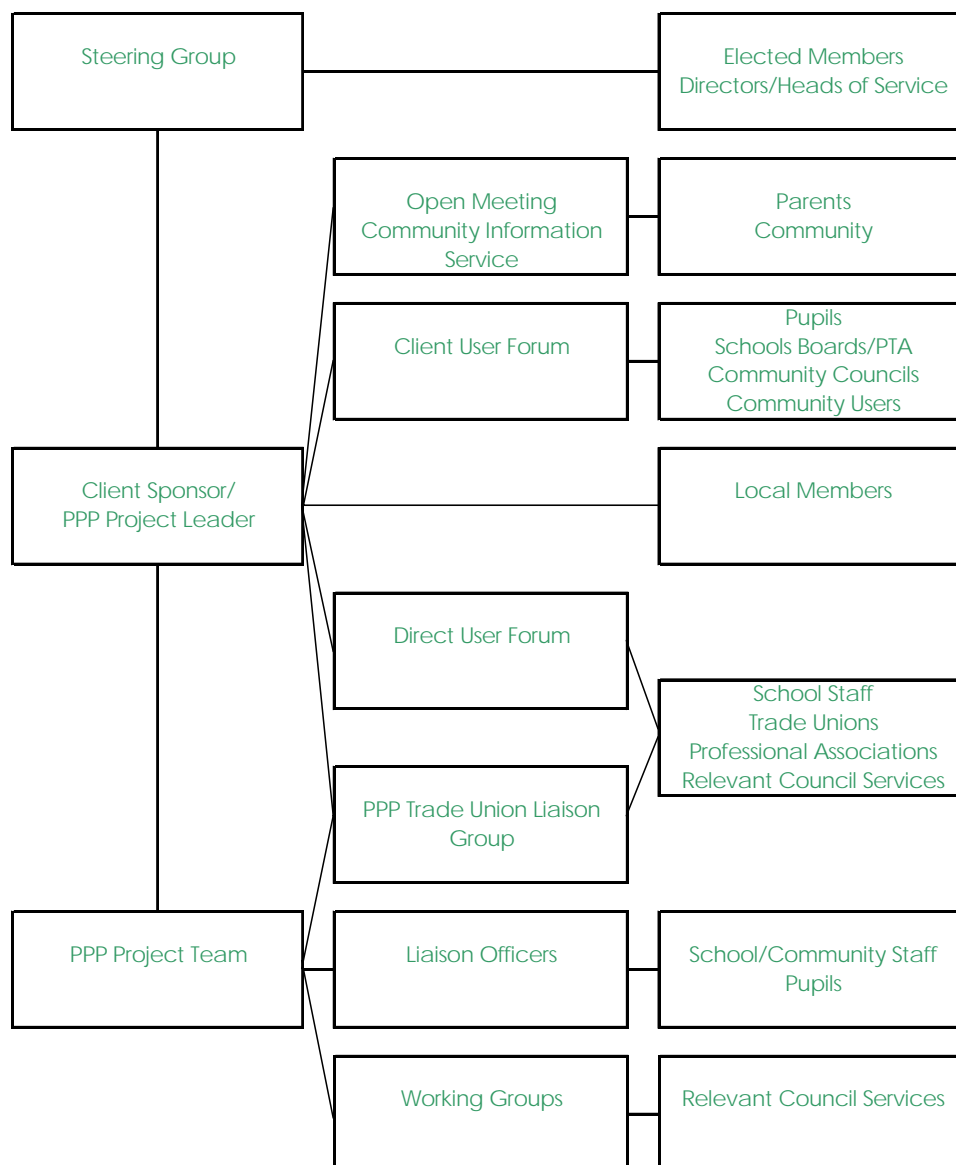
The conventional procurement programme has been developed on the premise that the council secures the existing designs and planning consent for the 3 project schools.

The council's Property Services section is presently assessing the designs for Inveralmond Community High School, The James Young High School and St. Kentigerns Academy as developed by the consortium in order to determine whether the proposed designs are deliverable within the available resources and at the same time to determine a fair value for the design work undertaken to date.

23. Consultation Strategy

The council has developed a robust and effective Consultation and Communication Strategy and in using this strategy the key project stakeholders have been consulted and informed on a regular basis as the project has developed.

Figure 1 - Consultation and Communication Framework



24. Conclusion

The appraisal process undertaken at the time of the PPP2 OBC identified a clear preferred option, which the council believed would meet its service delivery requirements and could be delivered successfully through the PPP procurement route.

The PPP procurement route has been robustly tested by the council however on this occasion the council has concluded that the PPP2 project was not suitable for this procurement route, and the revised terms offered by the preferred bidder did not represent best value for the council. Consequently the council has terminated the PPP2 procurement.

The council has developed an alternative preferred option for delivering the required levels of schools investment and is confident that this alternative is deliverable and affordable within the proposed funding package.

With specific reference to the proposed PPP3 project the council is satisfied that the revised PPP project is fully consistent with the characteristics of the PPP procurement route.

In reaching a decision on suitability of the proposed PPP3 project the council would trust that the Scottish Executive gives due consideration to the unique challenges the council has faced in seeking to deliver the PPP2 project.

Appendix 1 - Revised Preferred Bidder letter July 2005

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Appendix 2 - Developments post revised Preferred Bidder letter

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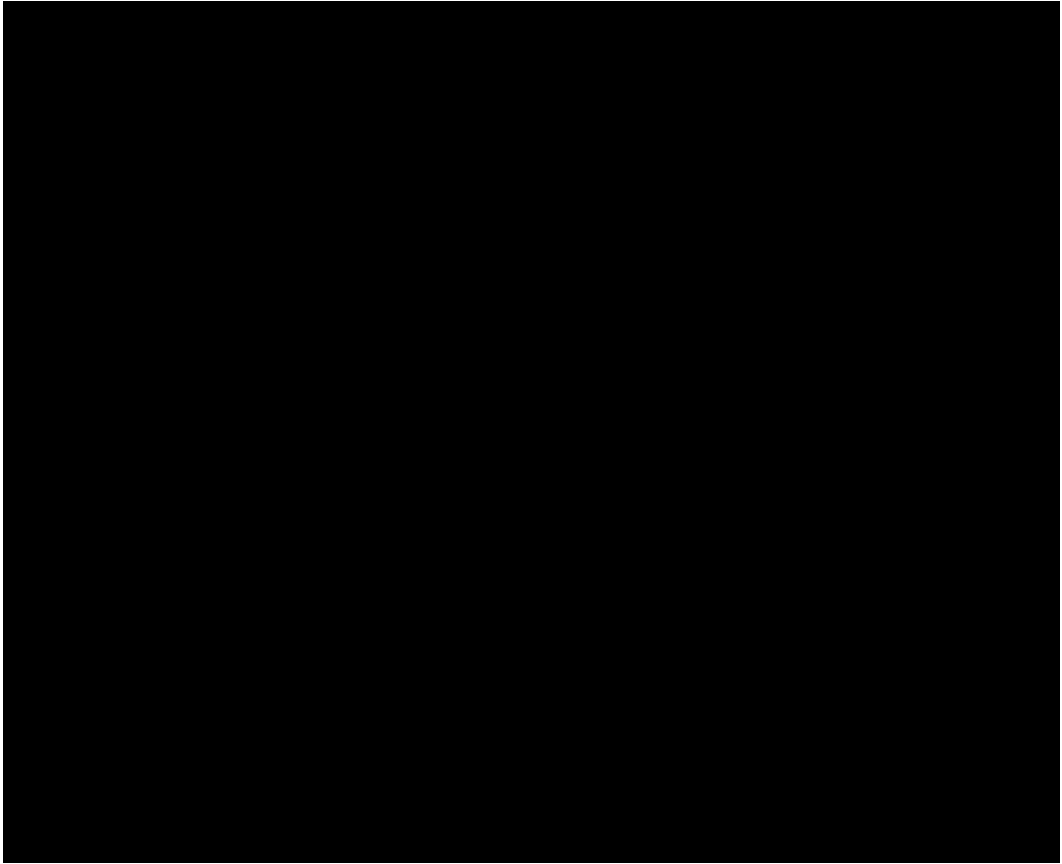
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Appendix 3 - Alpha Schools letter of 21 December 2005

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Appendix 4 - External Adviser Statement

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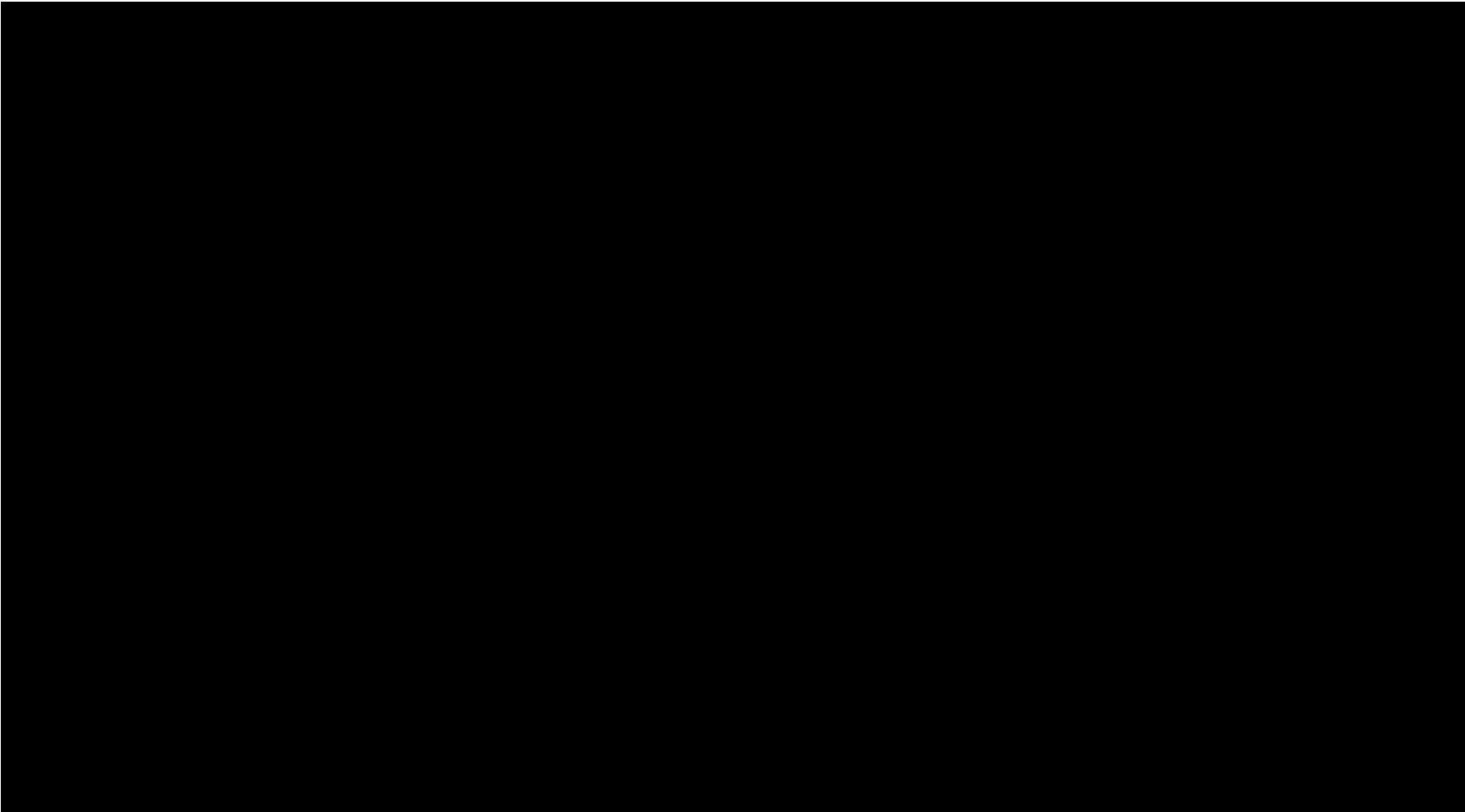
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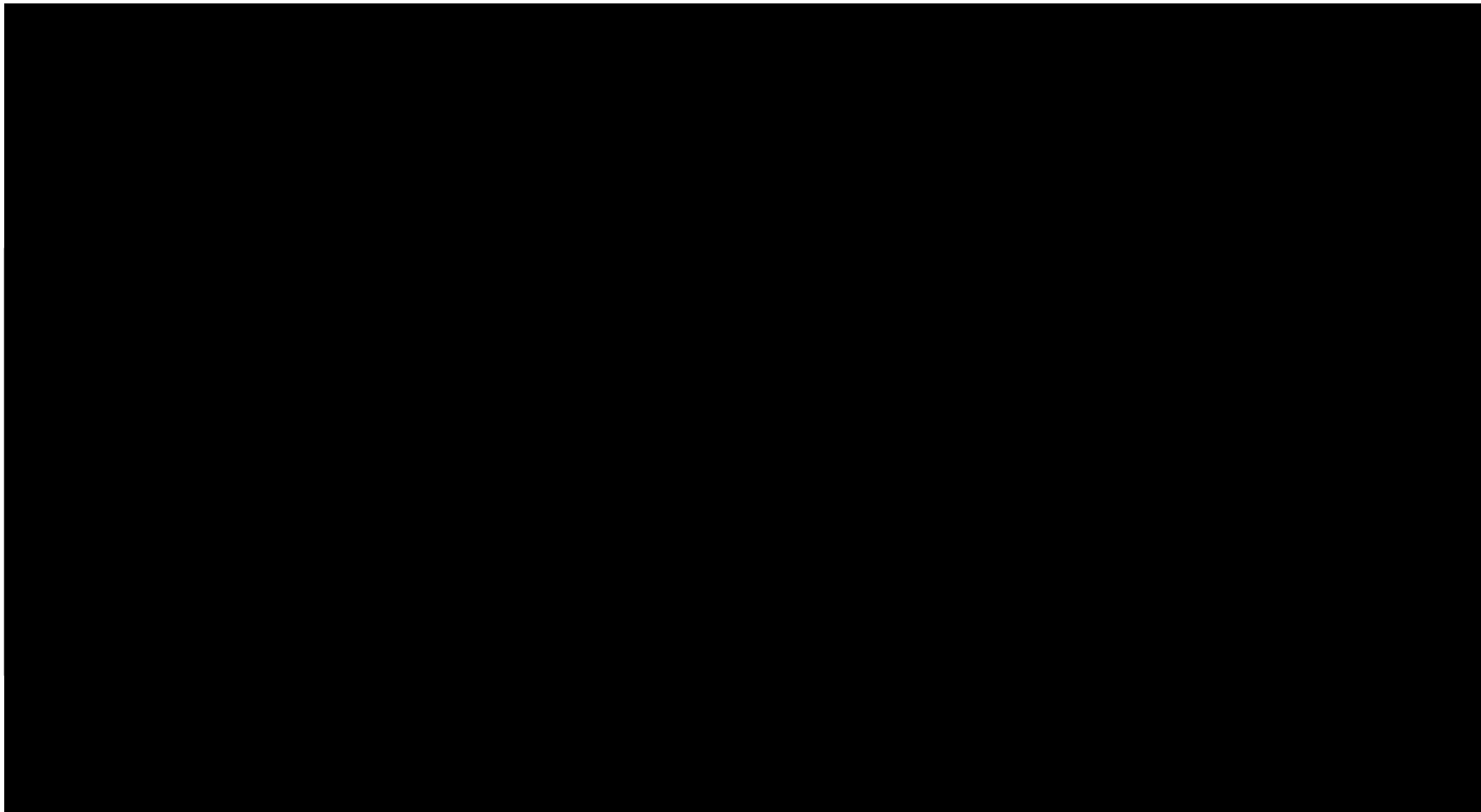
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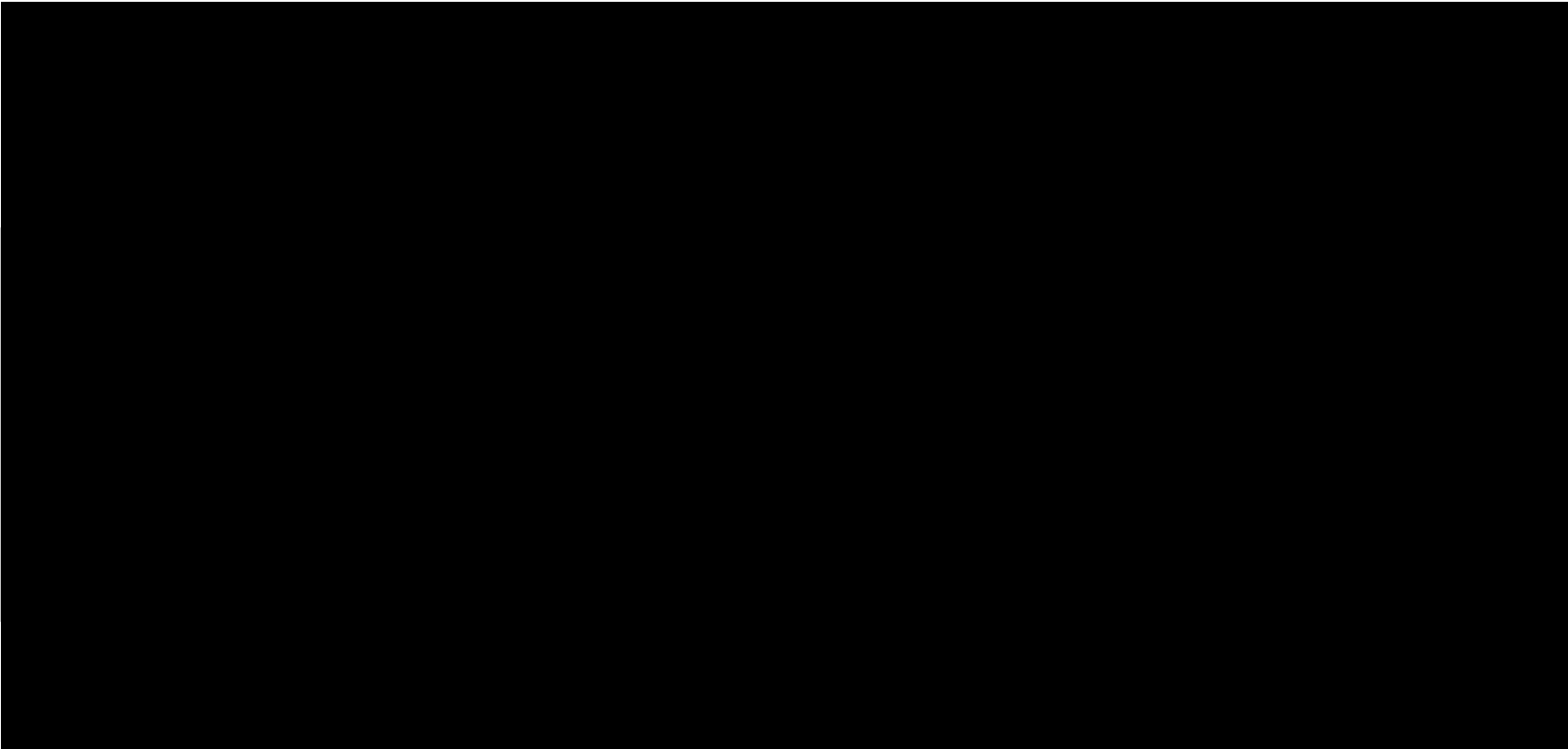
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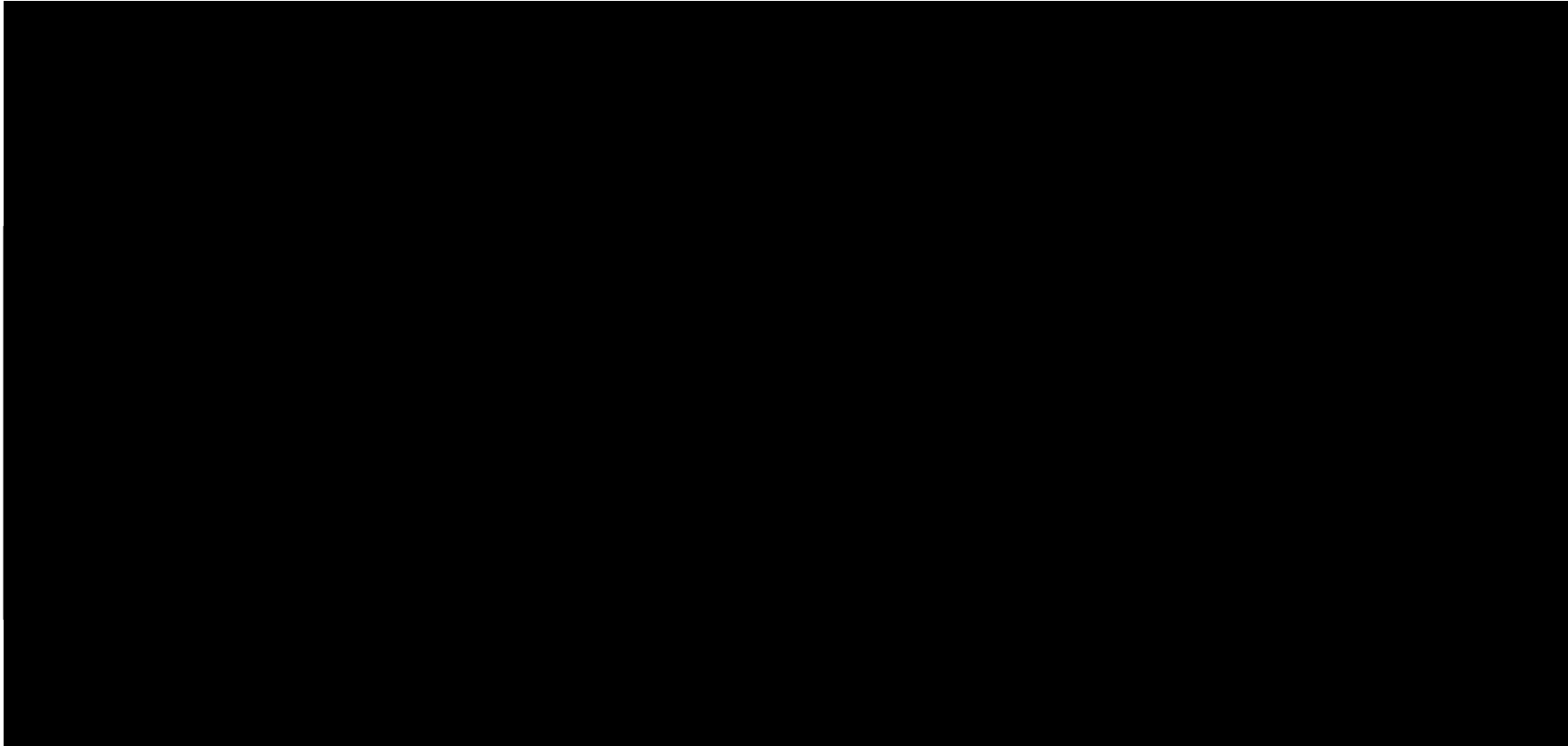
Appendix 5 - Optimism Bias

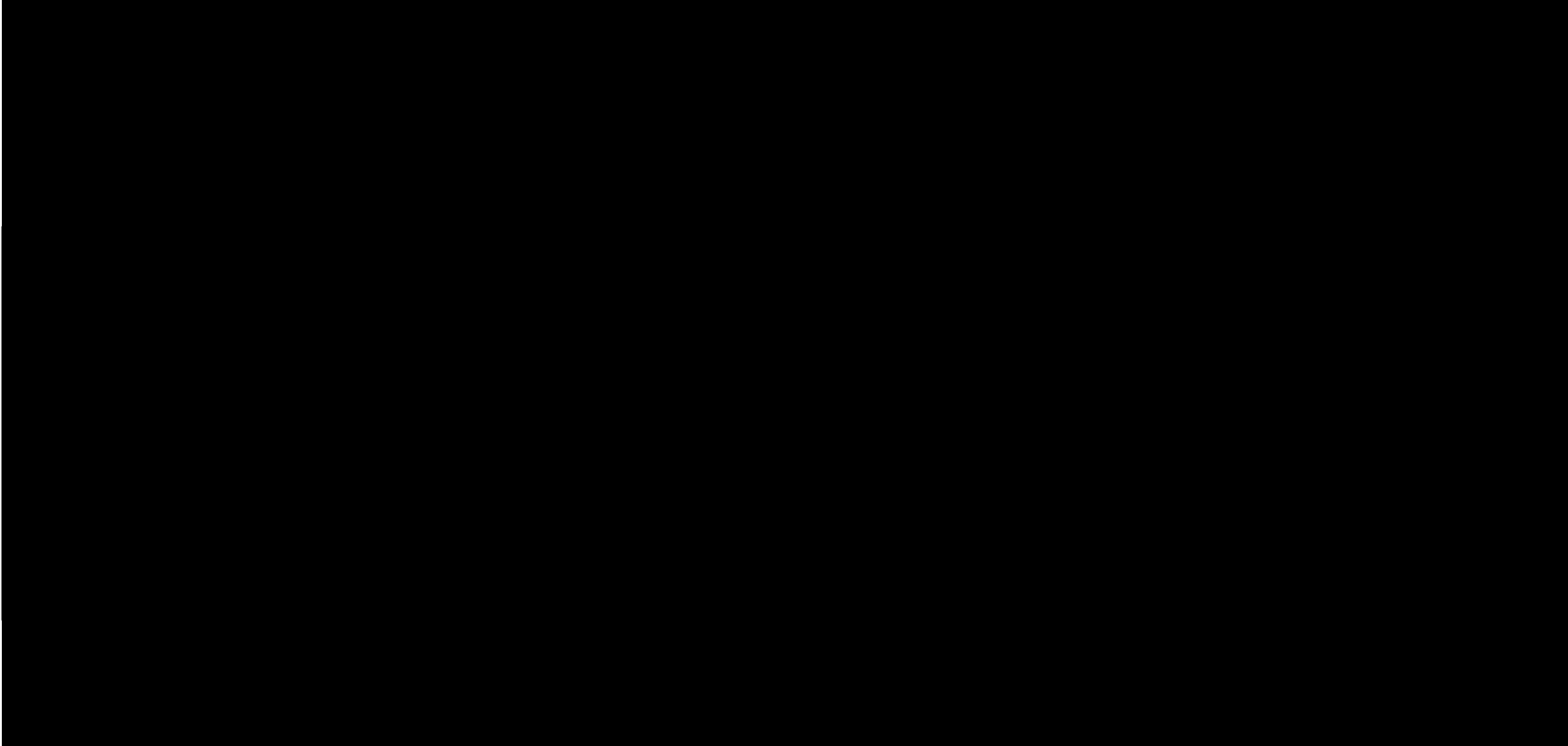




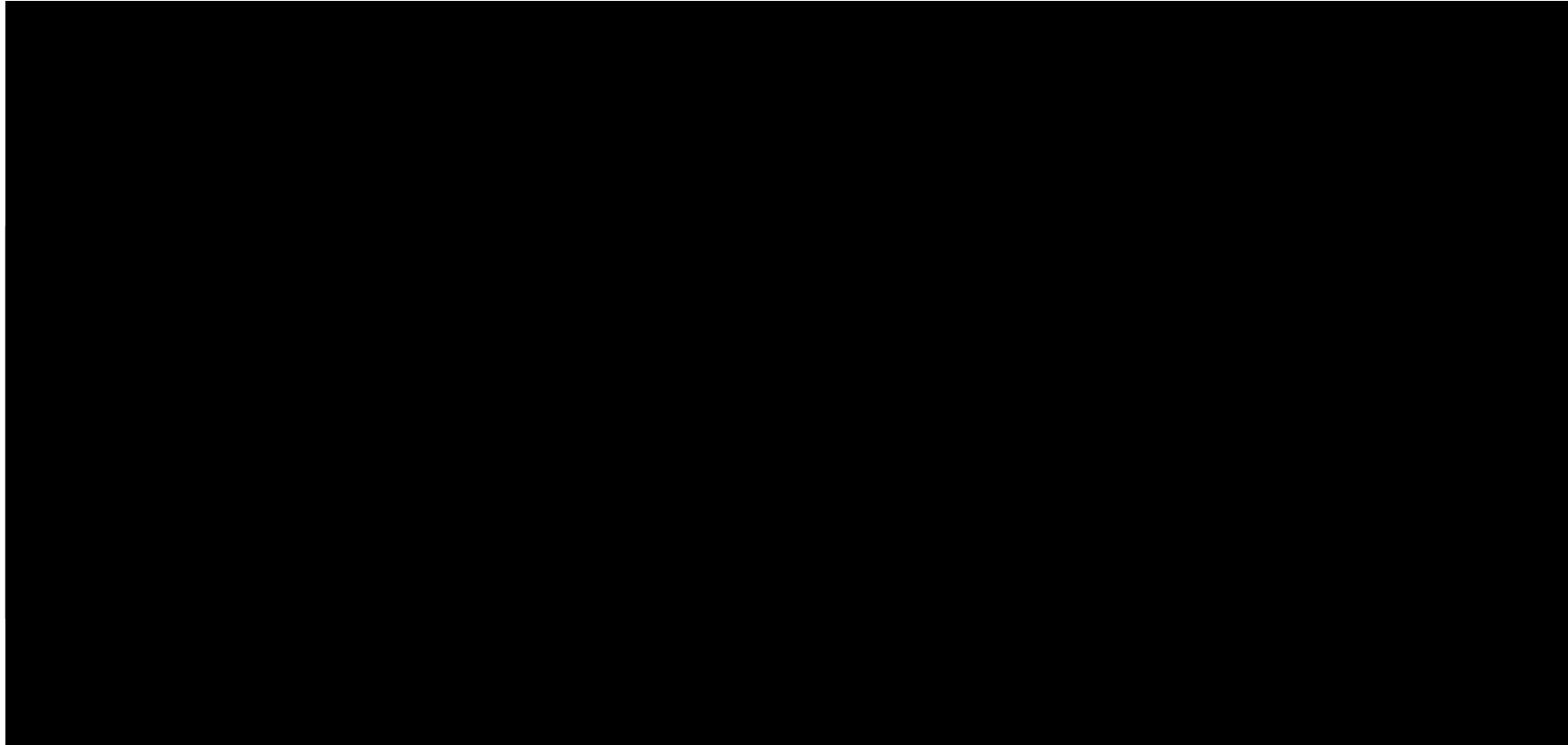
Appendix 6 - VfM Assessment (HMT Model)

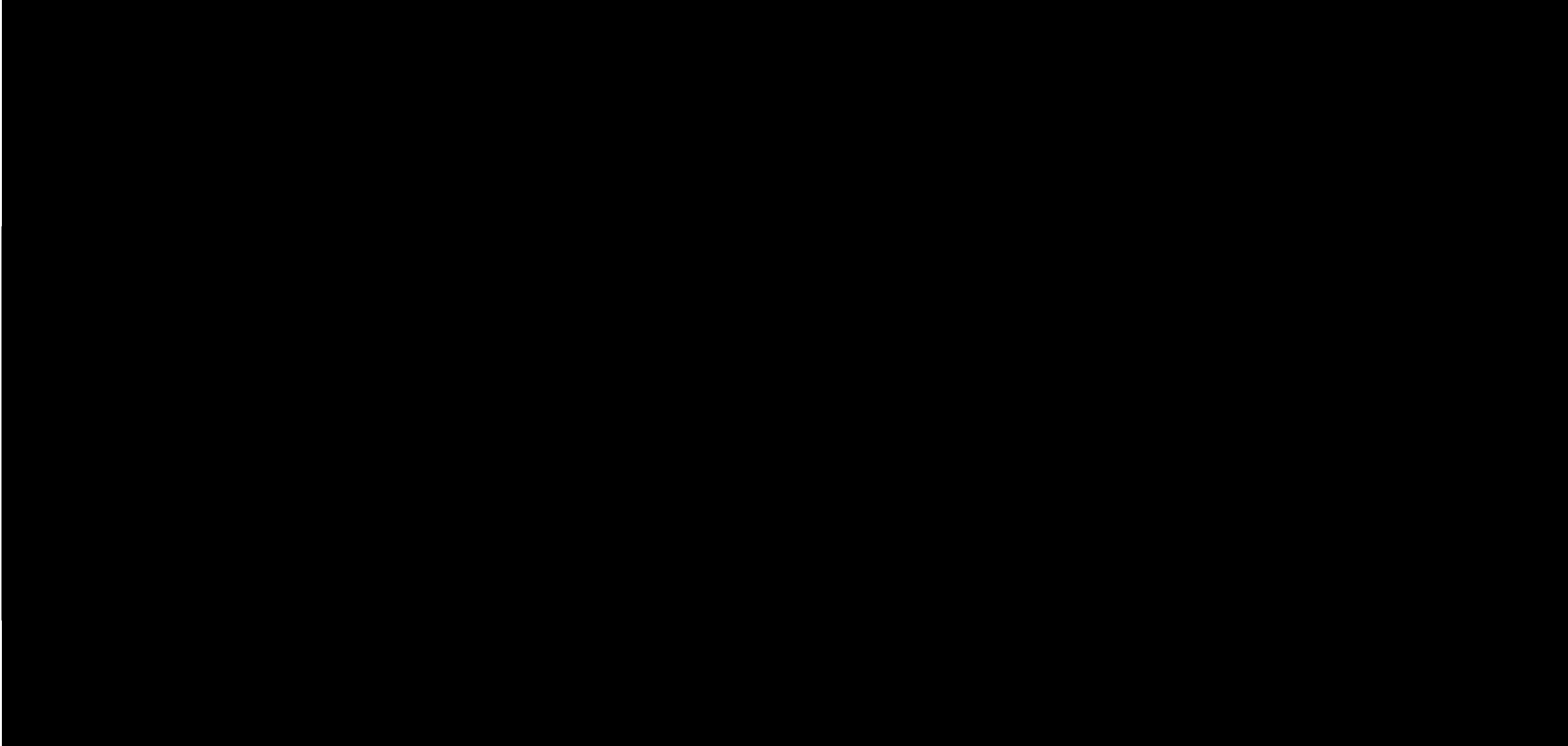




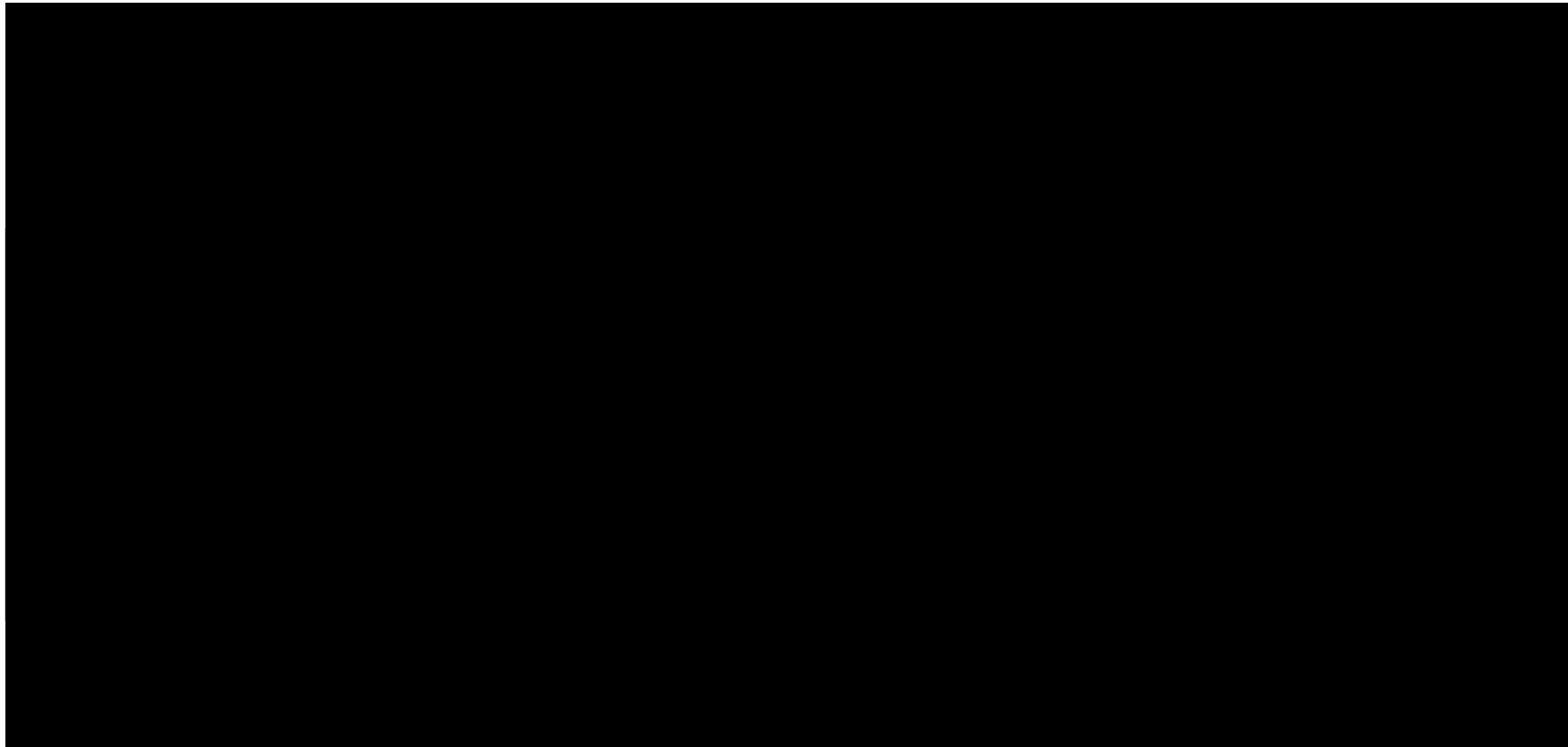


Appendix 7 - VfM Assessment (CPAM and Shadow Bid Model)





Appendix 8 - HMT Model Sensitivity Analysis



Appendix 9 - Shadow Bid and CPAM Model Sensitivity Analysis



Appendix 10 - Revenue Funding Award

Circular 8/2001 Revenue Support Input Sheet

ENTER DATA IN YELLOW SHADED CELLS

Project Name: PPP3
Local Authority: West Lothian Council

Contract length	30 years
BCR (%)	8.0631%
All inputs in real terms	1
Inflation rate	2.5%
3rd party abte %	0.0%
Month of 1st Payment	6
Year of 1st Payment	2009
% of 1st year	83.0%
% of last year	17.0%
Annual Cap (£k)	3,588

Year expenditure or receipt incurred (Year of 1st payment = year -year 0, -1, etc)	Year in which start of contract year occurs	Amount of capital expenditure or receipt (£k)	Description of expenditure or receipt (i.e. capex, capint, capmaint or receipt (enter receipt as a negative amount))	Year in model
-2		27,511	Capital Expenditure & Capitalised Interest	1
-1		25,787	Capital Expenditure & Capitalised Interest	1
0		3,328	Capital Expenditure & Capitalised Interest	1
1	1	0		1
2	2	0		2
3	3	7	Lifecycle maintenance	3
4	4	7	Lifecycle maintenance	4
5	5	7	Lifecycle maintenance	5
6	6	106	Lifecycle maintenance	6
7	7	151	Lifecycle maintenance	7
8	8	7	Lifecycle maintenance	8
9	9	7	Lifecycle maintenance	9
10	10	7	Lifecycle maintenance	10
11	11	448	Lifecycle maintenance	11
12	12	7	Lifecycle maintenance	12
13	13	151	Lifecycle maintenance	13
14	14	7	Lifecycle maintenance	14
15	15	7	Lifecycle maintenance	15
16	16	1,627	Lifecycle maintenance	16
17	17	7	Lifecycle maintenance	17
18	18	7	Lifecycle maintenance	18
19	19	151	Lifecycle maintenance	19
20	20	7	Lifecycle maintenance	20
21	21	2,970	Lifecycle maintenance	21
22	22	7	Lifecycle maintenance	22
23	23	7	Lifecycle maintenance	23
24	24	7	Lifecycle maintenance	24
25	25	78	Lifecycle maintenance	25
26	26	669	Lifecycle maintenance	26
27	27	7	Lifecycle maintenance	27
28	28	7	Lifecycle maintenance	28
29	29	222	Lifecycle maintenance	29
30	30	435	Lifecycle maintenance	30

West Lothian Council
Schools Public Private Partnership
Revised Outline Business Case - February 2006

All in £ 000's

Contract Years	Principal Repaid	Interest on principal	Unsmoothed Support on a Contract Year Basis	Smoothed Revenue Support on Contract Year Basis	Financial Year Beginning April	Revenue Support Based on Financial Years	Final Revenue Support in Accordance with Circular	Percentage of full payment		
							CAP			
1	56,626	4,566	61,192	4,179	3,469	1	2009	3,521	2,978	83%
2	0	0	0	4,179	4,179	2	2010	4,232	3,588	100%
3	7	1	7	4,179	4,179	3	2011	4,232	3,588	100%
4	7	1	7	4,179	4,179	4	2012	4,232	3,588	100%
5	7	1	7	4,179	4,179	5	2013	4,232	3,588	100%
6	106	9	115	4,179	4,179	6	2014	4,232	3,588	100%
7	151	12	163	4,179	4,179	7	2015	4,232	3,588	100%
8	7	1	7	4,179	4,179	8	2016	4,232	3,588	100%
9	7	1	7	4,179	4,179	9	2017	4,232	3,588	100%
10	7	1	7	4,179	4,179	10	2018	4,232	3,588	100%
11	448	36	484	4,179	4,179	11	2019	4,232	3,588	100%
12	7	1	7	4,179	4,179	12	2020	4,232	3,588	100%
13	151	12	163	4,179	4,179	13	2021	4,232	3,588	100%
14	7	1	7	4,179	4,179	14	2022	4,232	3,588	100%
15	7	1	7	4,179	4,179	15	2023	4,232	3,588	100%
16	1,627	131	1,758	4,179	4,179	16	2024	4,232	3,588	100%
17	7	1	7	4,179	4,179	17	2025	4,232	3,588	100%
18	7	1	7	4,179	4,179	18	2026	4,232	3,588	100%
19	151	12	163	4,179	4,179	19	2027	4,232	3,588	100%
20	7	1	7	4,179	4,179	20	2028	4,232	3,588	100%
21	2,970	239	3,210	4,179	4,179	21	2029	4,232	3,588	100%
22	7	1	7	4,179	4,179	22	2030	4,232	3,588	100%
23	7	1	7	4,179	4,179	23	2031	4,232	3,588	100%
24	7	1	7	4,179	4,179	24	2032	4,232	3,588	100%
25	78	6	85	4,179	4,179	25	2033	4,232	3,588	100%
26	669	54	723	4,179	4,179	26	2034	4,232	3,588	100%
27	7	1	7	4,179	4,179	27	2035	4,232	3,588	100%
28	7	1	7	4,179	4,179	28	2036	4,232	3,588	100%
29	222	18	240	4,179	4,179	29	2037	4,232	3,588	100%
30	435	35	470	4,179	4,179	30	2038	4,232	3,588	100%
31	0	0	0		710	31	2039	763	610	17%
						32			0	0%
	100% of NPV at E	8.063%	58,459							
	80% of NPV at BC	8.063%	46,767	46,767	46,174			46,767	39,644	