

EAST RENFREWSHIRE COUNCIL
AUDIT AND SCRUTINY COMMITTEE

24 September 2020

Report by Clerk

NATIONAL EXTERNAL AUDIT REPORT – PRIVATELY FINANCED INFRASTRUCTURE
INVESTMENT: THE NON-PROFIT DISTRIBUTING (NPD) AND HUB MODELS

PURPOSE OF REPORT

1. To provide information on the Audit Scotland report *Privately Financed Infrastructure Investment: The Non-Profit Distributing (NPD) and Hub Models*.

RECOMMENDATION

2. It is recommended that the Committee considers the report.

BACKGROUND

3. A copy of the Audit Scotland report [Privately Financed Infrastructure Investment: The Non-Profit Distributing NPD and Hub Models](#), published in January 2020, has already been circulated to all Audit and Scrutiny Committee Members. Under the Committee's specialisation arrangements, the Members leading the review of this particular report are Councillor Miller and Councillor Grant. The Director of Environment has provided comments on the Audit Scotland report and a copy of those comments is attached (see Appendix A).

RECOMMENDATION

4. It is recommended that the Committee considers the report.

Local Government Access to Information Act 1985

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Background Papers:-

1. Audit Scotland Report – *Privately Financed Infrastructure Investment: The Non-Profit Distributing (NPD) and Hub Models*.

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EAST RENFREWSHIRE COUNCILAUDIT AND SCRUTINY COMMITTEE24 September 2020Report by Director of EnvironmentNATIONAL EXTERNAL AUDIT REPORT – PRIVATELY FINANCED INFRASTRUCTURE
INVESTMENT: THE NON-PROFIT DISTRIBUTING (NPD) AND HUB MODELS**PURPOSE OF REPORT**

1. This report provides comments to the Audit and Scrutiny Committee in response to the Audit Scotland report *Privately Financed Infrastructure Investment: The Non-Profit Distributing (NPD) and Hub Models*.

RECOMMENDATION

2. It is recommended that the Committee notes the report.

BACKGROUND

3. Audit Scotland's report on *Privately Financed Infrastructure Investment: The Non-Profit Distributing NPD and Hub Models* was published in January 2020. A report was due to be submitted to the Audit and Scrutiny Committee earlier this year, but its submission had to be delayed to allow other priorities, principally linked to addressing issues relating to the Covid-19 emergency, to be addressed.

4. The report contains 5 key messages as follows:-

- Since 2005, Non-Profit Distributing (NPD) and hub private financing have supported £3.3 billion of additional investment in public assets. Another £5.7 billion of investment is also being supported under earlier Private Finance Initiative (PFI) contracts. Private finance costs more than traditional forms of financing, affecting future budgets for many years. The Scottish Government has accepted these costs to enable additional investment to take place. However it is not clear enough how decisions have been taken about which projects will use private finance, or how well this is achieving the best balance of cost and benefits in practice.
- The structure of NPD removes the ability of the companies involved to obtain dividends. Nevertheless, companies can generate returns by selling their rights to future contract payments. The Scottish Government does not monitor the extent to which this is happening, making it more difficult to know how effective its policy of profit capping has been in limiting overall private sector returns.

- The hub model has enabled private finance to be obtained for smaller community-based projects, but some aspects of competition are limited. Hub structures and governance are complex, and councils and other public bodies have mixed views about how well hubs are supporting their aims.
- Changes to the interpretation of national accounting rules mean the Scottish Government has now stopped using the NPD and hub forms of private financing for new projects. To contribute to meeting its National Infrastructure Mission commitment to raise annual infrastructure investment by £1.6 billion by 2025/26, the Scottish Government is developing a Mutual Investment Model (MIM) of private financing. This contains many features of both the NPD and PFI models.
- Councils have used NPD and hub private financing to improve local infrastructure. This has enabled projects to proceed that would not otherwise have been affordable. However by focusing on affordability, it is not clear how public sector organisations have assessed the value for money of using private finance, or whether the implications of entering into these contracts have been fully considered. A new schools funding model has the potential to continue Scottish Government investment in the school building programme, without a private finance cost premium. It remains to be fully developed and tested in practice.

5. The report clarifies that the Scottish Government is developing its approach to using private finance under the MIM, the replacement for NPD and hub forms of private financing. It makes a number of recommendations aimed at assisting the Scottish Government, the Scottish Futures Trust and the wider public sector, including Councils, as new funding models are introduced.

6. Comments on the recommendations pertaining to councils are provided in Appendix 1.

RECOMMENDATION

7. It is recommended that the Committee notes the report.

BACKGROUND PAPERS

Audit Scotland Report: *Privately Financed Infrastructure Investment: The Non-Profit Distributing (NPD) and Hub Models.*

Report Author: Andy Cahill, Director of Environment

Audit Scotland Recommendations	Comments
<p>Councils, and other public sector organisations, should:-</p> <ul style="list-style-type: none"> • Systematically assess the implications of participating in the financing and contract approaches led by the Scottish Government, before going ahead with individual projects (Paragraphs 30–32) • Clearly report current commitments under privately financed contracts, and the ongoing commitments related to these, as part of their annual budget setting (Paragraph 32) • Review all projects and services procured through the hubs to assess the costs, savings and benefits against other procurement options (Page 29). 	<p>The Council has entered into only one NPD/hub project so far which was Barrhead High School. Given the competing demands on our capital programme for replacement of existing poor condition schools, new schools to serve the growing population and other essential infrastructure, it would have been impossible to fund a new Barrhead High School using conventional capital funding in a reasonable timescale. Such a delay would have resulted in increased maintenance & running costs for the existing school and eventually a much higher capital build cost due to rising cost inflation which outstrips Council capital funding increases.</p> <p>The NPD/hub funding offer was carefully considered together with both capital and revenue funding availability and local benefits. Given the lack of suitable Council owned sites in the area, there was no feasible option other than the existing site, so this was not a factor in the funding decision. The NPD/hub approach also gave us the opportunity to use our capital funding more flexibly to improve facilities at Crookfur Primary School, assisting with both primary and future Early Learning Centre demands, and to provide enhanced sports facilities for Barrhead High School and the local community.</p> <p>The Council's budget setting process takes account annually of all privately financed project commitments and recognises that there is less flexibility in these lines. As such, these committed areas are disregarded when budget savings options are being considered.</p> <p>The Barrhead HS NPD/hub scheme (as mentioned in point 1 above) allowed the school to be replaced much more quickly than would otherwise have been possible and the funding flexibility allowed the Council's capital funding to be used to upgrade Crookfur PS/nursery facilities and improve the sports facilities adjacent to Barrhead HS at the same time. In addition to the enhanced facilities for local residents, hubWestScotland has also tracked the employment benefits of the project. The hub approach does provide opportunities for joint working and sharing best practice with the private sector and other Councils/public bodies, but can be more complex than normal procurement. In this case the Barrhead scheme was particularly complex due to changes in international accounting rules during the course of the project, but this should not be such a problem for any future schemes.</p>

Audit Scotland Recommendations	Comments
<p>The Scottish Government and councils should:-</p> <ul style="list-style-type: none">• Continue to work together to develop arrangements for the new schools investment funding model, ensuring opportunities and risks are fully understood and properly managed (paragraph 93).	<p>More recently, the Scottish Government has consulted with Scottish Local Authority Education, Property and Finance representatives in designing its latest schools funding model which is to be used for our Neilston campus. This is ongoing.</p>