

Boardroom, Falkirk Campus at **5.30pm**
(Refreshments available from 5.00pm.)

AGENDA

FOR APPROVAL

1. Full Business Case for Forth Valley College – New Falkirk Campus – Financial Case

(Elements of paper 1 are withheld from publication on the Forth Valley College website under Section 33 Commercial Interests and the Economy of the Freedom of Information (Scotland) Act 2002.)

Uncontrolled Copy

Full Business Case for Forth Valley College – New Falkirk Campus



August 2016

16 FINANCIAL CASE

16.1 Ascertaining affordability

Undertaking a financial appraisal of the project is an essential component of the selection of an affordable option which also presents good value for money (VFM). The affordability analysis helps determine whether the College can afford the Project. It seeks to ensure that the College can both afford to fund the initial development expenditure (construction costs, fees and land) and maintain the new facilities to an acceptable standard over the longer term (soft and hard FM, lifecycle).

It is however essential to consider both affordability and value for money together, to ensure the overall structure is the best preferred solution in terms of the College's objectives, business requirements and funding constraints.

This section analyses the Preferred Option and Base Case from an economic and financial perspective and includes:

- A review of the College's forecast Income and Expenditure and how this may be used to support the cost of the Project
- A review of the proposed Project costs
- The availability of funding and resources for the Project – both upfront and operational; and
- An analysis of affordability - assessing the resources that will be available to the College to pay for the facilities

16.2 Office of national statistics and ALF

As from 1 April 2014, Scottish Further Education Colleges were brought within the Scottish Government's direct funding structure and therefore included within the public sector as defined by the Office of National Statistics (ONS). As part of this process, it was agreed that cash balances not required for working capital could be donated by Colleges to separately created Arms-Length Foundations ("ALF"). However, debt remains on the College's balance sheet and is accounted for as part of the Scottish Government's overall borrowing.

As a result of this transfer, and in accordance with the wider public sector, the College is unable to borrow on its own account, without Scottish Government consent. A consequence of this is that the College would not be able to undertake a major redevelopment project (such as was recently achieved with Alloa and Stirling campuses) without direct intervention from the Scottish Government (via the Scottish Funding Council) in the form of grant or other funding.

The funding structure proposed by SFC / SFT therefore provides an opportunity for the College to undertake a significant development of its Falkirk campus, with the majority of the capital cost being provided by the Scottish Funding Council via a capital grant.

16.3 Financial case context: non-profit distributing (NPD) model

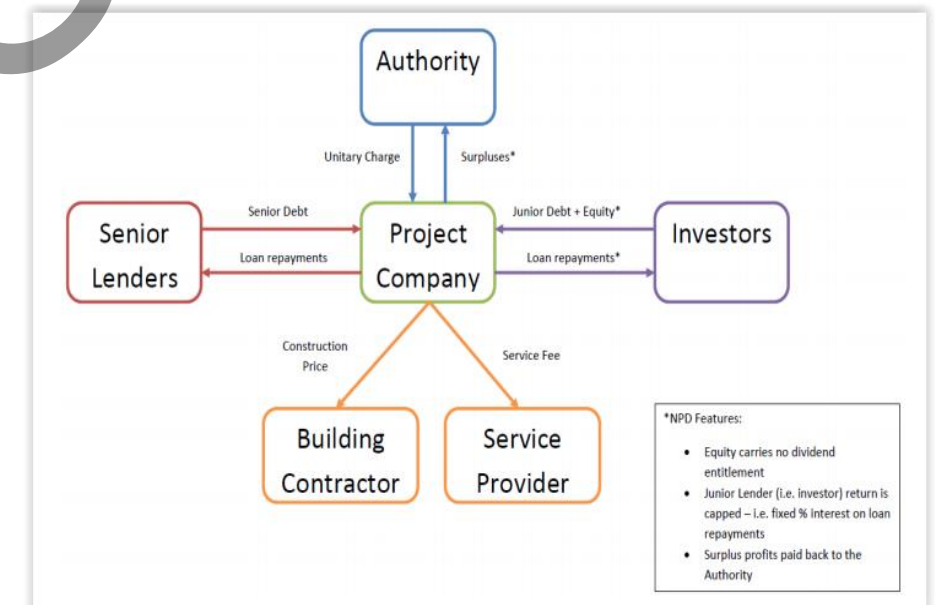
It was previously intended that the project was to be funded through the Non Profit Distributing (NPD) Model, and this was the working assumption at earlier OBC and FBC stages. The NPD project budget of £70m had defined the level of capital expenditure and design assumptions.

The NPD funding approach had previously assumed the following:

- A Special Purpose Vehicle or Company (SPV) will be appointed to design, build, finance and operate (hard FM and lifecycle) the new Falkirk Campus over a 25 year period from construction completion
- In return, the College would make an annual payment to the SPV ("Annual Service Payment" or "ASP") for provision of the building and services
- The Scottish Funding Council ("SFC") would fund all of this payment with the exception of hard FM and 50% of lifecycle costs within the project excluding Authority Maintenance Obligations ("AMOs") which account for specialist installations, wall coverings, floor coverings and ceiling finishes
- The SPV is responsible for the build, finance and basic operation of the new campus building, undertaking hard FM and lifecycle works only
- The College therefore directly funds the hard FM element of the ASP and 50% of lifecycle costs (including AMOs)
- The College continues to procure / undertake soft FM itself and meets these costs in full. It also remains responsible for utility costs incurred and rates
- College remains responsible for maintenance and lifecycle on its other buildings
- Upfront expenditure, such as design costs, advisory fees, enabling capex, land costs and some elements of fit out is not funded directly by the NPD procurement. This must instead be funded by the College or SFC

The diagram below shows a typical NPD Structure

Figure 16.1 – Typical NPD Structure



16.4 Revised approach – capital grant funding

The Scottish Government's NPD programme has been under review recently, following the introduction of the European Statement of Accounts 2010 (ESA10), to replace ESA95. It is the European System of National Accounts guidance on how public finances are presented, including public sector net debt and public sector net borrowing. ESA10 was brought into effect to better align how European nations compile and present their National Accounts.

We understand that SFT have been in detailed discussions with the Office for National Statistics & the Eurostat (official statistical office for the EU) to better understand the way that the guidance is to be interpreted and applied. The accounting treatment of the NPD model on new (post-September 2014) projects has remained uncertain, and in future amendments to NPD project terms may be required to result in an acceptable accounting treatment for these public sector projects.

However by letter of 12 April 2016 the Scottish Government informed the College that the project would not proceed under the NPD model, but would instead receive a direct Capital Grant from Scottish Funding Council (SFC Capex), providing certainty to the project structure, procurement and timetable. The other key project assumptions have remained unchanged, so besides the natural design evolution and refinement of cost assumptions, we are now assuming that the

equivalent facilities (having removed the Falkirk Council's Arts Theatre) will be funded by an equivalent capital grant from the SFC. The College will procure a construction partner and then retain responsibility for operating the building from practical completion. The relatively complex project company structure of the NPD model over the 25 year concession period is not therefore required, although some services may still be subcontracted by the College during operations.

16.5 FVC's underlying financial position

The College has provided its actual financial results for the period ending 31 July 2015 and financial forecasts for the years ended 31 July 2016 and 2017. The values used are sourced from the "FFR" or "Financial Forecast Return" which is presented annually to SFC – and are shown in table 16.1. Scottish Colleges have been advised by the Scottish Funding Council that they should revert to a 31 July year end as was previously the case (pre-ONS). As a result the College presents results for a 16 month period to July 2015 (from prior year end of 31 March 2014). This extrapolation is also shown in the table with the relevant prior year periods.

The College is not forecasting an increase in core grant funding from the new Project, and is assuming that income will remain relatively constant over the period to 2015/16. In the year 2016/17 total income is forecast to fall by c. £2m (6%), largely driven by grant funding and other income reductions. In addition, the College is proposing to utilise £637k from the ALF to support estates funding. The forecasts show that the Preferred Option produces a more favourable financial position for the College as it would have been required to spend c. £11m in backlog maintenance in order to ensure that the existing Falkirk campus is statutorily compliant. These costs are based on the Conditions Survey prepared by CBRE for the College. The longer term forecast also includes an increase in lifecycle costs at the new campuses at Stirling and Alloa

Table 16.1 therefore also summarises the base case forecasting assumptions made in the financial model, without inclusion of the Falkirk Campus project, in the right hand column.

Table 16.1: Base Case financial forecast

Forecasts - Excluding Project £'000	31 July 2013 to 31 March 2014 (8 months)	2014/15 (16m to July)	2015/16 (12m to July)	2016/17 (12m)	Forecast Assumption (thereafter)
Income					
SFC grants	17,071	31,522	23,116	23,288	2.50%
Tuition fees & education contracts	5,311	9,926	8,179	6,859	2.50%
Transfer from ALF	-	-	637	-	-
Other income	1,372	1,946	1,779	1,560	2.50%
Endowment and investment income	86	26	15	11	0.00%
Total Income	23,840	43,420	33,726	31,718	
Expenditure					
Staff costs	(14,643)	(28,925)	(23,485)	(22,950)	2.50%
Non-restructuring exceptional costs	-	(176)	(1,749)	-	-
Other operating costs	(5,632)	(11,711)	(6,671)	(6,778)	2.50%
Transfer to ALF	(4,400)	(1,100)	-	-	0.00%
Depreciation / amortisation	(1,755)	(3,542)	(2,235)	(2,014)	0.00%
Interest payable	(170)	(224)	(186)	(179)	0.00%
Total Expenditure	(26,600)	(45,678)	(34,326)	(31,921)	-
Operating (Deficit) / Surplus	(2,760)	(2,258)	(600)	(203)	-
Backlog Maintenance on existing Falkirk Campus	-	-	-	(2,200)	Remaining £8.8m over 4 years.
Operating (deficit) / surplus following backlog maintenance	(2,760)	(2,258)	(600)	(2,403)	-

In recent years non-essential maintenance and lifecycle costs at Falkirk have been scaled back in anticipation of its replacement by a new build facility. These forecasts do not assume that the current level of maintenance costs attributed to Falkirk Campus will be sufficient to fund its maintenance over its long term useful life. although it is noted that the maintenance needs of the College (revenue and capital) are supported by a maintenance grant from the Scottish Funding Council. The majority of this grant is currently spent on Falkirk campus maintenance, in addition to ongoing IT spend. In addition, the College has assumed that it will have c. £2.2m backlog maintenance costs for the five years from 2016/17.

In forecasting beyond 2016/17 we have assumed that maintenance and lifecycle costs at the Alloa and Stirling campuses will increase as the buildings age and converge with sector benchmarks. We assume that additional funding will continue to be made available in the form of SFC maintenance grant to support each facility (Falkirk, Stirling and Alloa) to an acceptable condition. This is shown below in the property cost analysis.

16.6 Property costs

The College estate includes new facilities in Stirling and Alloa in addition to the existing campus in Falkirk which is the subject of this business case. The current College estate comprises of:

Table 16.2: existing estate

Site	m ²	% Overall Estate	Comments
Alloa	5,786	16.7%	New build, capital funded – completed 2011
Stirling	7,859	22.7%	New build, capital and loan funded – completed 2012
Falkirk	21,000	60.6%	Redevelopment proposed
Total	34,645	100%	

Source: College Information

16.6.1 Existing property costs

The College estate incurs property running costs (including lifecycle costs) of approximately £ 3.1m per annum (2015/16 forecast) after demolition of Middlefield. These running costs include staff costs, utilities, general maintenance, FF&E and lifecycle costs. Staff costs are allocated by site and the College does not anticipate any change in staffing levels as a result of the new campus procurement as hard FM and some soft FM is currently out-sourced to FES and FES undertakes a proportion of the ongoing capital maintenance/lifecycle works.

The current running cost of the overall Estate is £89.3/ m² (2015/16) following demolition of Middlefield. The premises costs for the existing Falkirk estate equate to £25.38 / m² per annum in 2015/16 (excluding Soft FM, some staffing and Middlefield which incurs minor grounds maintenance costs) as can be seen in table 16.3. Adding in average soft FM rates gives a total FM cost of c. £79/ m² for Falkirk which we believe is comparable with other educational institutions at the lower end of some benchmarks thus evidencing efficiencies in the current operations. We note that Falkirk costs are lower than Alloa and Stirling in anticipation of the College moving its new campus, so the College has deferred non-essential expenditure.

Table 16.3 existing property costs

2016/17 Property Cost Summary	Alloa		Stirling		Falkirk (Main building only)		Total	
	Total	Per 5786 m ²	Total	Per 7859 m ²	Cost Heading	Total	Per 5786 m ²	Total
Hard FM (incl. water / sewerage)	42,761	7.39	43,635	5.55	84,844	4.04	171,240	4.94
Utilities	62,661	10.83	116,753	14.86	241,017	11.48	420,431	12.14
Rates	34,905	6.03	48,202	6.13	49,313	2.35	132,420	3.82
Lifecycle maintenance	28,958	5.00	42,102	5.36	157,909	7.52	228,969	6.61
Sub Total	169,285	29.26	250,692	31.90	533,083	25.38	953,060	27.51
Soft FM	357,818	61.84	486,017	61.84	1,298,683	61.84	2,142,518	61.8
Middlefield							9,665	
Total	527,103	91.10	736,709	93.74	1,831,766	87.23	3,105,243	89.63

16.7 Financial modelling approach

The financial model was prepared by QMPF with the financial forecast inputs provided by the College and project cost data provided by AECOM.

In order to undertake an assessment of affordability and VFM, it is necessary to consider the project over the longer term. This allows the project costs to be evaluated on a whole life costing basis, taking account not only of initial capital costs but also of the costs of maintaining and renewing the buildings over a longer period.

A term of 25 years from 1 August 2019 has been adopted as the assessment period, the year ending 31 July 2019 being the anticipated year of main construction completion with 60 years of operations following this.

The model assumes that the new facility will be accounted for on the college's balance sheet as a fixed asset, and depreciated over 60 years. The capital grants received for the project will be capitalised and amortised over a matching 60 year period.

16.8 Model forecast assumptions

As a base position, the model uses the College forecasts as detailed above in its 'pre-project' FFR. The specific assumptions relating to the new project, such as estates costs are then also applied in the VFM analysis. In addition, any variations to income, operational expenditure, premises costs and capital expenditure are also considered in the forecast and model when comparing the Preferred Option and the Base Case.

16.9 The preferred option

The scope of this Preferred Option is:

- Redevelopment of the Falkirk Campus, replacing 21,000m² of existing facilities with 20,148m² of new buildings
- A core capital grant from the SFC of £70m is received for the capital expenditure
- The College will be responsible for procuring Hard FM, lifecycle, Soft FM and Utilities provision at the new facility
- Project funding is also supported by land sales at Alloa and Falkirk (forecast [redacted] and [redacted] respectively) in addition to £5m funding being provided by the ALF during the development phase
- The SFC provides funding during operations of 50% of lifecycle costs at Falkirk, as continuity with the NPD approach, and ensuring proper maintenance of the new facilities over the long term

Operational efficiencies – Premises Running Costs

The Preferred Option will involve construction of 20,148m² of new College facilities on the extended Middlefield site, replacing 21,000m² of existing facilities. The estimated running cost of the new Falkirk Campus is set out in table 16.4. These benchmark rate running costs are consistent with those provided to SFT and SFC at earlier stages

Table 16.4: New Falkirk Campus Forecast Premises costs

Cost Centre	Forecast 2016/17 Falkirk Premises Costs based on 20,148m ²	
	Total (£)	£ / m ²
Hard FM	302,220	15.0
Utilities	231,239	11.48
Rates (based on Alloa and Stirling costs)	120,888	6.0
Lifecycle (AECOM benchmark rate)	490,402	24.34
Total per annum	1,144,749	56.82

Note: costs to be indexed up to year of operational commencement

Under the Preferred Option, the running costs for the existing campuses are assumed to increase to reflect lifecycle costs as the buildings start to need maintenance. Lifecycle costs at the new campus are based on information provided by AECOM. Stirling and Alloa lifecycle costs are lower than those proposed for Falkirk due to differences in the design and construction of these campuses. Hard FM costs are already evidenced through current contracts.

It can be seen that from table 16.5 (in 2016/17 prices), that the total operating cost of the new campus, excluding soft FM (which is anticipated to broadly be the same as current costs) is c. £1.1m per annum or £56.82/m². This is forecast to generate an increase in total running costs of c. £600k p.a. in 2016/17 values which is primarily caused by an increase to Rates and Lifecycle costs at the new campus. However, as noted above, should the College choose to remain at the existing campus, it shall be required to fund (or secure funding to support) c. £11m of backlog maintenance to ensure statutory compliance. The financial model also assumes that should the College remain at the existing Falkirk campus, lifecycle costs will increase to £15/m² to account for ongoing maintenance costs at the refurbished campus.

These cost assumptions result in table 16.5 which shows the running costs under the Preferred Option for all campuses – the grey shaded boxes show where changes have been made from the Base Case as set out in table 16.4.

Table 16.5 shows the revised property costs, taking into account the provision of new facilities at Falkirk, which are effective in the financial model from 2018/19. Updated assumptions which differ from recent actual expenditure are highlighted in grey. These include revised lifecycle forecasts, based on sector benchmark rates for minimum required average lifecycle expenditure. The total premises increases by around £18 per square metre, as expenditure steps up from the minimal current level at Falkirk. This slightly higher than an anticipated annual operating cost should be viewed in the context of the £11m backlog statutory maintenance at Falkirk which would be avoided with the construction of a new facility. Soft FM and central staffing costs are assumed to be unchanged, as there is no material difference in provision anticipated,

given the internal area of the new facility will be very similar to the current.

Table 16.5: Planned Property Costs – including Falkirk Campus project

Property Cost Summary - including Project (16/17 prices)	Alloa		Stirling		Falkirk		Total	
	Total	Per 5786 m ²	Total	Per 7859 m ²	Total	Per 20148 m ²	Total	per 33793 m ²
Cost Heading								
Hard FM (incl. water / sewerage)	42,761	7.39	43,635	5.55	302,220	15.00	388,616	11.54
Utilities	62,661	10.83	116,753	14.86	231,239	11.48	410,653	12.20
Rates	34,905	6.03	48,202	6.13	120,888	6.00	203,995	6.06
Lifecycle maintenance	86,790	15.00	117,885	15.00	490,402	24.34	695,077	20.64
Sub Total	227,117	39.25	326,475	41.54	1,144,749	57.16	1,698,341	50.44
Soft FM	357,818	61.84	486,017	61.84	1,298,683	61.84	2,142,518	63.63
Middlefield							9,665	
Total							3,850,524	114.36
Deduct 50% lifecycle at Falkirk funded by SFC (per NPD)					-245,201		-193,351	
Total	584,935	101.09	812,492	103.38	2,198,231	119.01	3,605,323	107.08
Increase from current costs							500,080	

Table 16.6: Summary forecast total premises costs incl. new Falkirk Campus

Cost Area	Premises Costs Comparison	
	Base Case 2016/17	Revised Costs – including new campus
Hard FM, Utilities, Rates and Lifecycle	953,060	1,698,341
Soft FM and Other	2,142,518	2,142,518
Total	3,095,578	3,850,524
Additional unfunded costs:	+ £11m backlog maintenance at Falkirk + additional LC at Alloa, Falkirk and Stirling: £291k p.a.	N/A

Pre-Financial Close Advisory Costs (up to 2016/17)

As is typical on a large-scale capital project the College will incur significant fees on design development, land site investigation, preparation of procurement documents and advisory fees during the procurement process (financial, legal and technical). These costs have reduced slightly to reflect the change from NPD to a capital funded project. It is anticipated that total costs will be c. £5.3m including VAT and a contingency on advisory costs. These costs include, inter alia, Design, Financial, Legal, Architect, Landscaping and IT. Up to 2016/17, it is anticipated that the College will incur costs of c. £4m. All efforts will be made by the College to keep these costs to a minimum by close management of advisors from within its in-house team and by rigidly keeping to the delivery programme and specification.

These costs have been included in the financial model with the College funding them from College Cash, transfers from ALF (noting that the College is not in control of these funds and will have to request them from the Foundation) with the remainder of funds being supported via top-slicing of the maintenance grant, Branshill land receipt, net depreciation, and Scottish Funding Council. It is assumed that these costs will be incurred in accordance with the programme up until the projected date for contract award of September 2017.

Capital Costs

The total anticipated construction cost for the new campus is £59.7 million excluding VAT (c. £71.6m incl. VAT). This does not include the cost of purchasing land at Middlefield (£999k) or FF&E Costs. This also excludes revenue costs which are shown in table 16.7. The construction & fit-out is forecast to be completed by September 2019 and the majority of the construction costs would be incurred in the years ending July 2018 and 2019.

Land Costs

The project involves construction of the new campus on the existing Middlefield site which is now surplus to requirements. However, a small additional parcel of land is required to provide sufficient area for development. This is expected to cost c. £1.0m in 2016/17 and details are provided elsewhere in this business case.

Subsequent to the development phase, the existing Falkirk campus will be demolished and sold for development. A receipt of £1.0m is anticipated for this land although it will not be received until 2019/20. It is currently assumed that £1.0m of total funds required to support Project costs will be provided by way of SFC capital grant. It is also assumed that the sales proceeds from the disposal of the existing Falkirk site will be returned to SFC in 2019/20.

The above costs and receipts have been included in the financial model.

16.10 College cash contribution

The College has assumed grants from the Foundation of £5m will be utilised against initial project development costs. The College also holds land at Branshill in Alloa which is in the process of being sold. It is currently assumed that these funds shall be used towards project development costs.

The financial model currently assumes that for 2015/16, £200k from maintenance grants is withheld by the College and is then used to support project development costs.

16.11 Sources and uses of funding – summary

Table 16.7: Sources and uses of funding

Uses	31 Jul 16	31 Jul 17	31 Jul 18	31 Jul 19	31 Jul 20	Total
Design Team Fees (ex FBC fees)	561	555	126	117	-	1,359
Public Sector / Technical Advisor	217	730	172	202	367	1,656
VAT	164	286	63	68	88	669
Contingency - Revenue Costs	43	146	15	21	73	331
Sub-Total - Revenue Costs	985	1,717	377	408	528	4,015
Capex	-	-	30,591	25,731	858	57,179
Contingency - Capex (4%)	-	-	1,224	1,029	34	2,287
Inflation on capex	-	-	120	101	3	224
Land Purchase	-	999	-	-	-	999
FF&E etc. incl. inflation	-	-	660	2,859	-	3,519
Contingency - FF&E (20%)	-	-	132	572	-	704
VAT	-	-	6,545	6,058	179	12,783
Sub-Total - Capital Costs	-	999	39,272	36,350	1,074	77,695
Costs Incurred to Date	1,322	-	-	-	-	1,322
Total	2,307	2,716	39,648	36,758	1,602	83,032

Sources	31 Jul 16	31 Jul 17	31 Jul 18	31 Jul 19	31 Jul 20	Total
College Cash / Net Depreciation	1,670	-	-	359	513	2,542
ALF	637	2,716	1,517	130	-	5,000
SFC - £70m Grant	-	-	37,372	32,628	-	70,000
SFC - Additional Support	-	-	760	-	330	1,090
SFC - Forward Funding Falkirk Receipt	-	-	-	2,500	(2,500)	-
Receipts - Branshill	-	-	-	-	-	-
Receipts - Falkirk	-	-	-	-	-	-
Total	2,307	2,716	39,648	36,758	1,602	83,032

Current Project costs result in the College having a funding gap of c. £1.09m. This is primarily caused by the removal of “top-slicing” of the grant funding of £200k p.a. between 2016/17 & 2019/20 and the reduction in net depreciation available to use to support Project costs. These reductions have been caused by SFC cuts to both Capital & Maintenance and Student Support funding respectively.

The financial forecasts include the prudent assumption that the sale of Branshill will generate ██████ to support Project costs. There is potential for this receipt to be up to £1m higher which would reduce required SFC support to c. £0.09m.

It is currently assumed that if sales receipts for Alloa and Falkirk are not realised, SFC shall meet any shortfall.

Financial Model Forecasts

Table 16.8 shows the forecasts under the Preferred Option which demonstrate that operating surpluses remain at reasonable levels after the Project impact is included. These forecasts show the existing Falkirk campus being fully written down in 2018/19 with the College receiving ██████ in 2019/20 from the sale of the existing Falkirk site. This reduces the College’s annual depreciation charge from 2019/20 onwards but this is offset by depreciation for the new campus. Full details of the forecast Income and Expenditure Statement and cash flow statement are included in appendix 7.

The financial forecasts indicate that the College will continue to generate cash from its operating activities during the development period and beyond (with the exception of 2019/20 when forward funding of the Falkirk sale is forecast to be repaid to SFC). Average net operating cash flow from 2019/20 to 2028/29 is forecast to be c. £350k.

Table 16.8: Financial forecasts incl. New Falkirk Campus

Forecasts (including Project)	31 July 2013 to 31 March 2014 (8 months)	2014/15 (16 months, July year end, extrapolated)	2015/16 (12m to July)	2016/17	2017/18	2018/19	2019/20	2020/21
	£'000s	£'000s	£'000s	£'000s	£'000s	£'000s	£'000s	£'000s
Income								
Funding council grants	17,071	31,522	23,116	23,288	23,791	24,321	26,257	26,831
Tuition fees and education contracts	5,311	9,926	8,179	6,859	7,030	7,206	7,386	7,571
Other income	1,372	1,946	1,779	1,560	1,599	1,639	1,680	1,722
Endowment and investment income	86	26	15	11	11	11	11	11
SFC funding received for new campus	-	-	-	-	-	-	263	271
Total Income	23,840	43,420	33,726	31,718	32,431	33,177	35,597	36,405
Expenditure								
Staff costs	(14,643)	(28,925)	(23,485)	(22,825)	(23,396)	(23,981)	(24,580)	(25,195)
Project Costs Incurred	-	(176)	(1,749)	-	-	-	-	-
Other operating costs	-	(176)	(1,749)	-	-	-	-	-
Transfer to Arm's Length Foundation	(5,632)	(11,711)	(6,671)	(6,778)	(6,947)	(7,121)	(8,099)	(8,304)
Depreciation / amortisation	(4,400)	(1,100)	-	-	-	-	-	-
Interest payable	(1,755)	(3,542)	(2,235)	(2,014)	(1,991)	(1,980)	(2,728)	(2,728)
Total Expenditure	(26,600)	(45,678)	(34,326)	(31,796)	(32,509)	(33,250)	(35,568)	(36,380)
Operating (Deficit) / Surplus	(2,760)	(2,258)	(600)	(78)	(77)	(73)	29	26
Release of SFC Provision	3,000	-	-	-	-	-	-	-
New Falkirk Campus Costs	-	-	-	(1,717)	(377)	(408)	(528)	-
SFC Support – Forward Funding of Falkirk	-	-	-	-	-	2,500	(2,500)	-
Transfers from ALF	-	-	-	2,716	1,517	130	-	-
SFC Funding – Additional Support	-	-	-	-	760	-	330	-
Branshill revaluation	-	(615)	-	-	-	-	-	-
Write down of existing Falkirk campus	-	-	-	-	-	(16,411)	-	-
Operating Surplus / (deficit) following project costs and asset disposals	240	(2,873)	(600)	921	1,823	(14,261)	(2,669)	26

16.12 Falkirk arts venue

The College had been in negotiations with Falkirk Council in relation to provision of an 'Arts Venue' within the new College facility. The College and its advisory team had explored the various technical and commercial options for its inclusion in the project, partly on the Council's behalf. The Council ultimately decided not to proceed with the Arts Venue. We expect that the College will be able to agree a recovery of the aborted costs on this element of the Project from the Council, although at the time of this Business Case a fixed settlement is not yet agreed. Once finalised, any proceeds received from the Council may be available to support project costs.

16.13 Optimism Bias and risk analysis

The Treasury's Green Book highlights that the public sector has a tendency to under-estimate the cost of projects. This can occur for a variety of reasons including:

- Pressure to keep costs down and maintain affordability
- Change in requirements
- Risk occurrence (e.g. poor ground conditions, delays, etc.); and
- Impact of inflation (construction or land costs)

The Green Book calls this tendency 'Optimism Bias' and recommends that an allowance is introduced into cost planning, with higher amounts used at the earlier stages of project appraisal. It recommends that as a more detailed understanding of the risk profile of the project develops, that the Optimism Bias is reduced and replaced with specific risk allowances.

An important aspect of project planning is therefore the identification and mitigation of identified risks, to ensure that appropriate steps are taken to avoid risks and that allowances are made where applicable for risks that might arise. The approach to risk management is dealt with later.

Rather than apply optimism bias as might be suggested by Treasury guidance, a project contingency has been provided for in the cost assumptions. This is in addition to the cost analysis which is built up from recent benchmarked costs, particularly taking account of recently procured Further Education projects in Scotland and elsewhere. As a result, the College has sufficient evidence and advice to justify a reduction in the initial level of contingency applied to the cost estimates. This is consistent with the Green Book approach where optimism bias is reduced to almost zero just prior to project commencement.

Inflation

In order to evaluate future costs and revenues, it is necessary to model the impact of general inflation, particularly where costs and revenues are not expected to increase (or decrease) at the same rate. An underlying assumption for RPI of 2.5% has been used in the financial forecast model.

16.14 Benefits appraisal

Financial Benefits

By constructing a new build facility in Falkirk, the College will benefit from avoiding the onerous maintenance spend required on its current site – noting that the base financial forecasts do not take account of the required refurbishment expenditure at Falkirk of c. £25-30m but do include c. £11m of backlog maintenance costs which will be required to be statutorily compliant with minimum health and safety standards and also the required increase to lifecycle costs to maintain the campus to a suitable standard.

With a newly built campus, the College will be in an excellent position to build on its ability to generate new income streams and strengthen its financial position. Using a discount rate of 6.0875% (as per Treasury Green Book guidance), the net present value of premises costs without and with the project can be compared to highlight the savings which will be made by the College as a result of the new Falkirk campus. Over the period 31 July 2017 – 31 July 2044, without the project, the NPV of premises costs are forecast to be c. £53m compared to c. £46m with the project – a saving of c. £7m in NPV terms.

Non-financial/qualitative benefits

In addition to the financial benefits of the Preferred Option, there are a number of qualitative benefits attributable to the redevelopment of the Falkirk Campus. These may also translate into increased student uptake and improve revenue generation. However, this has not been assumed in the economic appraisals.

The benefits of the scheme have been assessed by the College management at various stages from early project appraisal through to this FBC stage.

16.15 Conclusion and financial analysis

The College anticipates that the project will deliver benefits in terms of cash generation despite the increased premises costs associated with the new campus. As a result of increased depreciation costs associated

with the new campus, I&E surplus is reduced however this reflects accounting treatment as opposed to cash generated.

Figure 16.2 Cash surplus comparison

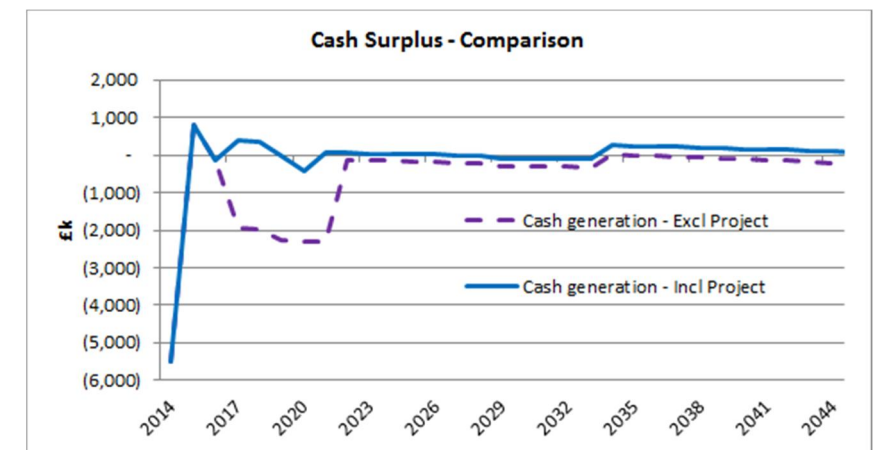
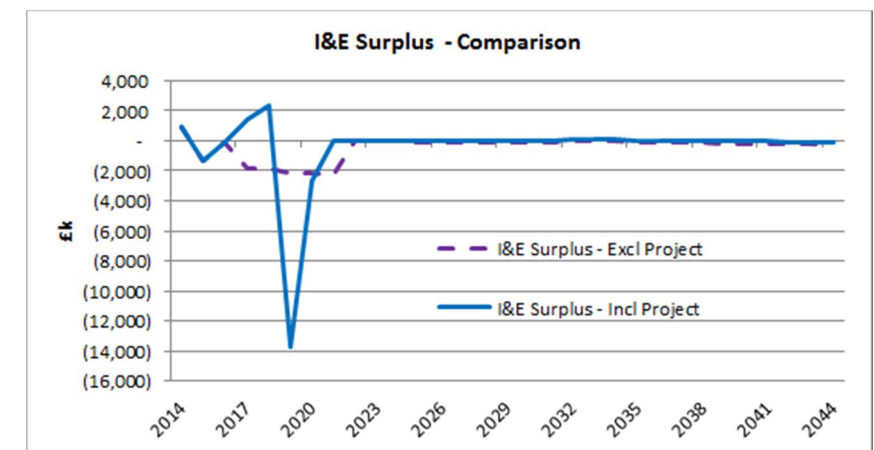


Figure 16.3 I&E surplus comparison



16.16 Risks and sensitives

The primary sensitivities which the College would be exposed to would be decreases in the level of financial support received from SFC, fluctuations in inflation and increases in operating costs.

Land sales – valuation: The College has currently made prudent assumptions in relation to both the timing and quantum of sales receipts for Branshill and the existing Falkirk site. However, there is the risk that these forecast receipts will not be generated which would result in the College having to obtain external support i.e. SFC / SFT.

16.17 Affordability conclusion

The affordability analysis demonstrates that the College can support the costs of the Project through anticipated premises cost savings during operations at the new campus and SFC support through the form of funding for College costs in the lead up to contract signing and also through the lifecycle contribution during the operations phase. In addition, should the College choose to remain at the existing Falkirk Campus, not only will it have to fund c. £11m of backlog maintenance to ensure that it is compliant with legislation (which has been included in the forecasts), it will likely incur increased ongoing premises costs in order to maintain the existing campus at a suitable standard. In addition to backlog maintenance costs, the College estimates that it would also incur refurbishment costs of c. £25-£30m. These ongoing refurbishment costs have not been included within the financial forecasts.

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