Appendix G: Comments of the Chief Financial Officer

1. Context

1.1. The requirement for an Independent Value for Money (VfM) review and Value Engineering exercise for the Arena at Temple Island was agreed by Cabinet in April 2017. Given the emerging costs pressures and other social, economic changes this was intended to establish whether the project could be delivered in an affordable way, achieve an improved public / private sector ratio that is fair and demonstrates VfM to local taxpayers.

1.2. This was an important step for a project that is considered to be of strategic importance to the City. The position has changed over time with new opportunities coming to light and the scope of the VfM review has been expanded to cover further opportunities.

1.3. The two propositions being considered within this report are for the Temple Island site (Arena / Alternative-use). They are diverse in nature and at very different stages of development, making a direct comparison challenging. The assessment therefore is consideration of the best use of resources to deliver the Council's strategic priorities.

2. Assessment Approach

2.1. The first step in the assessment has been to identify a clear rationale for the Council and wider public sector intervention. This can be based on our perceived role in ensuring markets are working effectively in providing goods and / or services required, to meet our core and strategic objectives and that these cannot generally be provided by current market mechanisms. The objectives or outcomes the Council wishes to meet through the intervention needs to be clear, following which the viability of the respective propositions can be measured.

2.2. In this instance the viability has been assessed from the perspectives of:

- Strategic fit to wider policy objectives
- Potential VfM
- Affordability / achievability (in terms of the total cost of both capital and revenue)
- Dependencies and constraints (e.g. legal frameworks)

3. Public Sector Investment Rationale

3.1. The public sector should ideally only intervene when there is a market failure and when intervention will lead to an improvement or greater efficiency.

3.2. The Temple Island site given its proximity to Temple Meads Station and location within the Bristol Temple Quarter Enterprise Zone (BTQEZ) is intended to be a catalyst to private / public investors as other developments progress. The propositions could contribute to the delivery of the strategic vision of a fair and inclusive city; whether the Council is engaged as an active participant or enabler to tackle challenges posed by economic and social inequalities, ultimately with less need for intensive council intervention.

3.3. Though not mutually exclusive, the approaches reflect specific market conditions and priorities, with the role of the public sector and need for intervention required for different reasons on both propositions.

3.3.1. Alternative-use - given the challenges and constraints on the site some element of public sector intervention may still be required to develop the site for any other purpose. Assets could be used to underpin regeneration efforts or unlocking difficult sites through more coordinated and strategic citywide approaches. In addition, the alternative use includes the potential for a conference centre and hotel space which has the potential to meet the Council's specific objectives for the Temple Island, and contribute towards the BTQEZ employment targets.

3.3.2. Arena - partners are using public sector assets as a means of guiding and shaping the type of development that takes place, managing and investing in assets in order to contribute towards the wider objectives of the Council, for example economic and social connectivity and employment space that contributes towards the BTQEZ employment targets. Since the approval of the business case, a proposition has been received from the private sector (YTL) to build an Arena at the Filton site in Bristol and whilst this does not remove the need for public sector intervention, it clearly weakens the rationale.

3.4. Where taxpayers' money or assets are involved in delivering the ambition, the Council must also ensure that VfM is secured. There must be a strong clarity of purpose with regards to what the project is intended to achieve. An informed judgement on affordability must be made and the level of risk needs to be openly assessed and acknowledged.

4. Viability

4.1. Strategic Fit

4.1.1. The strategic case is covered in depth in the KPMG VfM reports Appendix I and therefore not repeated here.

4.2. VfM including Social Value.

4.2.1. KPMG was appointed in 2017 to undertake the VFM review on the proposition on behalf of the Council. This has been delivered in line with the commissioned scope and was based on the information available at the time of the review. The economic assessment (proxy for economic returns) is the heart of any viability assessment and for clarity the VfM reports can be viewed as standalone reports for each proposition supported by a summary that compares the findings and provides an optimum balance between costs, benefits and risks.

4.2.2. The VfM economic assessment has been conducted in accordance with the principles set out in the HM Treasury green book, which contains central government guidance on appraisal and evaluation. This utilises a consistent formulation to calculate the Benefit Cost Ratio (BCR) of all options. BCR is an indicator used in cost-benefit analysis that attempts to summarise the overall VfM of a proposition and reflects the ratio of the benefits of a project relative to its costs. The VfM review has outlined some key challenges in particular the maturity of the propositions and the availability of data. This will improve over time for the alternative use site and as such it should be considered an evolving / iterative model, which will be regularly refreshed in line with the development on any alternative propositions.

4.2.3. The VfM metrics of the alternative developments on Temple Island compared to an arena is outlined in the table below.

	Arena	Alternative Use
Total net GVA (in NPV terms)	£489.1m	£875.3m
Capital costs/ public sector contribution	£172.5	£38.1m
BCR	3.2:1	23.0: 1
NPV	£282.6m	£837.2

Note: public sector contribution includes the assessment of land value.

4.2.4. Based on the scope of quantified economic impacts, it is estimated that the alternative use proposals could deliver a BCR of 23.0:1 and economic NPV of £837.2m, over a 25 year period. This compares to an estimated BCR of 3.2:1 and economic NPV of £282.6m for the Temple over a 25 year period. Generally speaking, the higher the BCR, the better the investment. That for the Arena has been estimated at 3.2:1 which means that at today's prices, for every £1 spent, the estimated financial equivalent benefit is £3.20. Please see Appendix I for the full KPMG VfM reports.

4.3. Social Value

4.3.1. Social Value is understood to be the social benefits a project offers. It is inherently a subjective measure of what is thought to matter the most and to whom. This is never easy to quantify because different organisations, funders, investors and governments all have a different understandings of what is important in creating social change and consequently all value different things.

4.3.2. Measurements need to be ongoing and tailored to the Council to be meaningful, using different measures to effectively capture the changes that occur in projects developed at a local or regional basis.

4.3.3. The tender specification (2015) for the Arena at Temple Island incorporated Social Value criteria, which provided a firm basis upon which plans could be developed and performance measured. Outlined below is the commitment made by BGCL:

No.	BGCL Commitment
1	Minimum of 50% of the labour force from West of England
2	Minimum of 25% of the labour force from Bristol (BS1 to BS16)
3	48 Construction apprenticeships
4	50 work placements
5	10 graduate placements offered for new job starts
6	250 person weeks of construction training
7	3 Engagement events or initiatives per month of construction covering: • Pupil interactions with Arena Construction • Job and training opportunities for Care Leavers and young people in care. • Recruitment for the long-term unemployed and young people Not in Education, Employment or Training' (NEET) • Job and training opportunities for Individuals from groups traditionally underrepresented in the construction sector e.g. women, people from BME communities, people with learning difficulties and/or disabilities
8	1 Supply chain training/support initiative per month of construction.

4.3.4. In having a proposition that is more developed, the initial Social Value offer made can be clearly articulated and the potential social value assessment undertaken utilising tools that are now more developed, and becoming more widely used in procurement processes.

4.3.5. The Social Value assessment has been provided by BGCL subsequent to the presentation of the VfM review and has been developed utilising the Social Value Portal. This is based on a National TOMs Framework developed in conjunction with the Social Value Portal. The framework aims to provide a minimum reporting standard for measuring social value, and translates the future benefits of the change over the life of the arrangements into a notional value / currency that we all use.

4.3.6. A number of the measures used in the framework capture national level impacts, for example fiscal savings from the activity being undertaken and is then where practical adapted to capture metrics at a regionalised or local level. The assessment initially indicated that the Social Value aligned to this contract could be in the order of £52m. As an economic assessment is also being undertaken as part of this process, the supply chain impacts (measures NT18 and NT19) are GVA estimates and captured within KPMG's economic analysis, therefore to avoid double counting this should be reported as a Local Economic Value and is reflected in the paragraph below.

4.3.7. This means that the £52m initial social value offer is then adjusted to a value of £16.3m that can be classified as separately quantifiable social value (the other £35.7m is deemed to be local economic value). It should be noted that this Social Value offer relates to the construction of the arena only and as such are temporary, not long-term impacts. At this stage this notional value has not been formally agreed or contractually binding and a similar assessment has not been put forward by the arena operator.

4.3.8. Whilst we have some concerns regarding the relevance to local priorities of some of the proxy measures, we recognise that the initial offer could be seen as baseline targets for a suite of indicators (e.g. no. hours of volunteering time provided to support local community projects) that can be replicated. We have formulated an illustrative social value estimate for the operation for the arena proposition and construction and operation for the alternative use. This has been based on the National TOMs Framework– toolkit and "calculator" (the same as used by BGCL) and provides some indication of potential social value. As the same approach is used for each proposition this allows for some comparison across them.

4.3.9. Due to the early stage of the plans, the data and information available to us was limited and therefore a high level consistent approach was adopted. The social value associated with the alternative development has been calculated using the estimated supply chain spending and the principles adopted are in line with BGCL assumptions that 25% of those employed are from Bristol BS1 to BS16 postcode.

4.3.10. This indicated a combined Social Value (construction and operation) of £19.2m for Arena Temple Island and £44m for the alternative use. The analysis should be viewed as illustrative only as there has been no ability to undertake due diligence with the parties concerned.

4.3.11. The summary table below captures the results from each, along with some key notes in terms of approach and assumptions. (Appendix I contains the outputs from the "calculator").

Summary of the social and economic value of each development

	Temple Island Arena			Alternative Use Temple Island		
	Construction (Buckingham estimate)	Operation (annual)	Total	Construction	Operation (annual)	Total
Total value	£52,020,199	£6,854,422	£58,874,621	£31,488,390	£66,228,452	£97,716,842
Social Value	£16,325,047	£2,959,840	£19,284,887	£3,094,440	£41,731,560	£44,826,000
Economic Double Count	£35,695,152	£3,894,582	£39,589,734	£28,393,950	£24,496,892	£52,890,842
Summary	The social value estimates have been taken from Buckingham estimate of Social Value generated in Bristol. Buckingham have used the National TOMs Framework and proxy measures which in the estimation be based on a combination of UK indirect multipliers, regional and local rates.	The social value associated with the operation of Temple Island has been estimated using the average supply chain spending of the Arena Operator, sourced from the P&L account supplied by the Operator. We have assumed a 17.5% leakage rate at a Bristol level in line with the KPMG Temple Island Arena: value for money assessment.	Indicative - for illustration purposes only	The social value associated with the alternative development at Temple Island has been calculated using the estimated supply chain spending associated with the construction of the development. Supply chain spending has been derived from backward inducing spending from the indirect GVA. We have adopted the same approach as Buckingham, assuming that 25% of those employed are from Bristol BS1 to BS16.	The social value associated with the operation of the alternative development on Temple Island has been calculated using estimates of the supply chain spending. Supply chain spending has been derived from backward inducing spending from the indirect GVA. We have adopted a leakage rate of 25% at a Bristol level based upon the KPMG report 'Assessment of alternative development plans for the Temple Island site'.	Indicative - for illustration purposes only

Notes
All estimates have been estimated using the Social Value TOMs database. All 'operation' impacts are on an annual basis. All 'construction' impacts are for the period of construction.
For consistency and to facilitate comparisons the values and proxy measures are those utilised by Buckingham in conjunction with the Social Value Portal.

4.3.12. The measures can be refined and incorporated as obligations within the NEC3 Building Contract and detailed in full within in the Employment and Skills Plan. This could then be submitted for discharge of condition 16 of planning permission 15/06069/F, which states "a scheme for an employment and skills programme shall be submitted to and approved by the Local Planning Authority." These were in the process of being progressed. It is anticipated that if appropriate, a similar approach would be pursued for any proposition that proceeds.

4.4. Risk and Uncertainty

4.4.1. Even with robust assumptions, there will still generally be risks to consider and there will be uncertainty over the range of possible outcomes. A distinction may be drawn between a risk which is measurable and has a known or estimated probability (to which contingencies can then be applied), and an uncertainty which is more vague and of unknown probability.

4.4.2. It is impossible to guarantee precision in BCR or Social Value calculations given the scale of variable factors and contingencies affecting costs or benefits in the near and long term. Although risk adjustment is mathematically straightforward, these have not been carried out on these assessments. Primarily due to the fact that the tools used in determining the evaluations above are based on information available at the time.

4.4.3. Each proposition is unique and a simple adjusted BCR / Social Value can produce an alternative set of initiative rankings that could be useful in choosing between initiatives but it also uses another set of subjective data that could be seen to 'distort' the results. Rather than eliminate error, it introduces greater risk of error implicit in anecdotal viewpoint about net benefits.

4.4.4. Both assumptions incorporate a level of contingencies to address the point above and should a decision be made to progress the alternative use, this will need to be reviewed as part of the business case development.

This demonstrates that purely on economic terms both sites offer VfM and material social value. With the alternative use development illustrating more positive indicators (not accounting for risk, which could be considered significant, based on the stage of development and need for more in depth due diligence). BCR does not allow for unquantifiable factors which could affect a decision, such as wider Strategic fit and further social impacts which will also need to be considered.

4.5. Affordability

4.5.1. Alternative Use of Temple Island

4.5.1.1. Assessment of the alternative proposition for the Temple Island site assumes reallocation of the £25.6m (excluding land value), CIL, capital receipt and other Council contributions are retained and may be required to support site development. Overall any alternative scheme is anticipated to require significantly less public investment than that required for the Arena, and there is potential for higher economic benefit measured through the benefits cost ratio.

4.5.1.2. The VfM report highlighted the potential for annual business rates of some £2.2m based on the assumptions provided to them, compared to an estimated £400k for an Arena. In each case 50% of rates would be retained by the Council, as part of the pooling arrangement. The alternative scheme also has the potential to deliver additional CIL and New Homes Bonus (under current arrangements) but at this stage these cannot be quantified.

4.5.1.3. However this scheme is at a very early stage of conception and any comparison with the Arena proposal should be seen in that context (as set out in paragraph 1.3 above).

4.5.1.4. Should this scheme not progress then there will be sunk costs of approximately £100k, which will need to be contained within the Growth and Regeneration Directorate Budget.

4.5.1.5. In addition, significant expenditure has already been incurred on the Arena Island site (£12.8m associated with delivery of the Arena scheme). Whilst a small proportion of this will be transferable to an alternative scheme, the majority of costs to date are likely to be deemed abortive if the scheme does not progress. An initial estimate provided by project officers is that this could be as high as £12m, however this will require further due diligence. It is important to note that abortive expenditure cannot be financed through capital resources and will require revenue reversion and that no provision currently exists for this. Officers would need to explore the implications of this on the remainder of the Medium Term Financial Plan.

4.5.1.6. There will be opportunity for the Council to benefit from a capital receipt from the disposal of the site as part of the alternative use proposition.

Based on the assessments undertaken, the alternative use scheme requires significantly lower public sector investment, a potential for higher annual business rates and council tax income, however this needs to be viewed in the context of the risk and uncertainties attached to this proposal.

4.6. Dependencies and Risk

4.6.1. There is insufficient information available at this stage to provide further financial commentary on the alternative Temple Island proposition, beyond that set out in the VfM review which is appended. This is not uncommon for a proposition at this stage of development. Further development of the nature of the scheme, planning considerations, models of delivery, land disposal and procurement arrangements will all need to be considered separately, and financial analysis will need to be provided as scheme proposals progress towards greater maturity and therefore Cabinet will need to be mindful of key risks as outlined below.

4.6.1.1. With regard to the £53m Economic Development Fund, a full business case for this was considered by the LEP in July 2016 and approved with conditions. The conditions including full clarification of scope and costs have yet to be met, and no formal grant offer has yet been issued by the LEP to BCC for this project.

4.6.1.2. It should be noted that although Bristol has a right to seek substitution of the £53m EDF, any such substitution must align to City Deal objectives, and subject to submission of a new business case to be approved by the West of England LEP. EDF Funding is primarily directed at projects within the Enterprise Zones and Enterprise Areas to deliver economic growth, particularly business rate growth. Business cases proposals must also address all relevant aspects of the economic and financial case including wider infrastructure requirements, viability, cost, benefits, VfM and state aid.

4.6.1.3. There are a number of competing demands on the EDF fund, which may require re-profiling of existing funding assumptions. Furthermore the actual level of EDF is dependent on overall business rate growth across the sub-region's Enterprise Areas and Enterprise Zone being in line with original modelling assumptions, estimated to deliver £500m additional business rates over the period of the 25 years to 2038. So far, business rate growth across the sub region has been below original model assumptions (which are underwritten by each unitary authority), as key schemes have not been delivered in line with original plans. Adverse changes to anticipated business rates growth is likely to impact on the level of EDF available for all programmes that have not yet received final approval. Delays to obtaining final approval or those in developing an alternative proposition for utilisation could result in the EDF allocation being reduced in line revised business rate growth assumptions. Officers are currently exploring alternative propositions that align to the conditions outlined above, should Cabinet determine not to progress this Arena option.

4.6.1.4. The Council received facility, via the LEP, borrowing at project rate (at lower interest than PWLB prevailing rate) to the value of £19.2m to support delivery of the Arena, and this is reflected in the financing assumptions within the VfM review. It is anticipated that, for financing purposes a high proportion of this can be reassigned to other associated schemes. However, that will be subject to LEP approval, and there remains a small risk that if not utilised in line with the conditions of the City Deal, a proportion of that borrowing would have to be repaid with a penalty rate of interest.

4.6.2. There is a risk that the alternative scheme could render the Council liable for tax. A separate review will need to be taken of potential VAT and other tax implications of the alternative scheme. The working assumption is that the scheme will not have additional VAT / SDLT implications however this will be reviewed as plans progress.

4.6.3. Any public sector investment will need to be constrained to public realm infrastructure and avoid incurring any expenditure which could be at risk of not being compliant with State Aid regulations.

4.6.4. It is assumed that the alternative proposition will have the potential to deliver additional business rates however this will be dependent on the actual mix between housing and commercial development, based on viability of the site and the assessed rateable values of the commercial elements.

4.6.5. Commercial risks of pursuing this option are set out in exempt Appendix J.

4.7. Arena Temple Island

4.7.1.1. The Council has previously agreed a capital budget for the construction and associated costs for building the Arena of £123.5m, currently assumed to be funded through £31m of grant funding, via CIL, capital receipts, revenue contributions and direct capital contributions from the operator, with the balance £92.5m, to be financed through prudential borrowing. To offset the annual cost of borrowing, £53m of Economic Development Fund has been secured from the LEP (subject to conditions), which will be financed over the residual period of the Enterprise Area and Zone pooling arrangement, and an annual rental from the operator of the facility over the 25 years of the lease. Since last reported to Cabinet the operator increased their capital contribution and annual rental offer, and the key financial elements of this were reflected in the financial model for the Arena, on which KPMG undertook their assessment.

4.7.1.2. Following the PCSA process, the total costs of the scheme were estimated to be £156.3m exceeding the approved budget by £32.8m (this excludes the land value of the site). Those costs comprised a target cost estimate for construction for the Arena of £122.1m and design, client side and associated costs of £34.2m. Subsequent to finalisation of the VfM review, the contractor put forward proposals for additional savings which have been assessed by officers. It is now considered reasonable that the target cost for construction would be reduced from £122m to £119m, and that would in turn marginally reduce the overall cost by £3.1m. Assumed within overall client side cost is the net cost attributed to the need for an alternative site compound following the land disposal to University of Bristol.

4.7.1.3. Phasing of the capital spend would be as follows:

	2018/19 (£m)	*2019/20 (£m)*	*2020/21(£m)*	*2021/22 (£m)*
Revised Capital Budget	32	46	28	10
Assumed Spend	6	61	63	16
Difference (call on contingencies)	(26)	(11)*	24	6

**Assumes c/fwd of unutilised 18/19 resources*

4.7.1.4. Development of the Arena project would cost significantly more than currently budgeted with a revised capital estimate requirement of £153m, an increase of £30m from that agreed by Council, to be funded from prudential borrowing.

4.7.1.5. The current assumption at the time of writing this report are that there are £41.9m for the life of the medium term plan up to 2023 available for allocation, as set out in the table below Utilisation of the contingencies will significantly impact upon flexibility to deal with financial risks associated with other schemes and any new pressures that require capital investment.

Current Assumptions on Capital Contingencies

	2018/19 (£m)	*2019/20 (£m)*	*2020/21 (£m)*	*2021/22 (£m)*	*2022/23 (£m)*
Available Capital Contingencies	8.7	7.2	7.9	9.0	9.0
Anticipated draw from Arena			(24.0)	(6.0)	
Available Contingencies (assuming no alternative use)	8.7	15.9*	(0.2)	2.8	11.8

* *Assumes c/fwd of unutilised contingency*

4.7.1.6. In addition to the above provision within the capital programme would need to be made for development of appropriate car parking facilities. The review of parking requirements concluded the need for additional spaces, including those required as part of the agreement with the operator. Alternative arrangements would need to be sought in order to secure those spaces required for operation of the facility and this could impact upon the viability of the financial model.

4.7.1.7. The indicative additional capital costs of parking development were estimated to be some £16m. It is anticipated that a delivery model with sufficient income generation would be developed for this to become cash neutral. This was reflected in the financial model over the 25 year period.

Despite the significant additional cost the scheme is deemed affordable, and this is reflected in the VfM review conclusion. The review indicated there would be a £1.3m surplus over the 25 year period of the assessment. The reduction in estimated target cost from £122m to £119m will increase that surplus, over the initial 25 year period to £6.55m.

4.7.1.8. In reality the surplus identified above would be utilised as smoothing to offset deficits that arise over the future years, as the income from EDF ends in 2038. All other financial assumptions remain the same as reflected in the KPMG VfM report appended separately. The financial model assumes therefore that all ongoing revenue costs are matched by income from the EDF grant, operator rental streams and income from parking.