

DECISION-MAKER:	CABINET MEMBER FOR CHILDREN'S SERVICES		
SUBJECT:	CONVERSION OF THE CITY'S THREE PFI SCHOOLS TO ACADEMY STATUS.		
DATE OF DECISION:	18 JUNE 2013		
REPORT OF:	CYP STRATEGIC COMMISSIONING, EDUCATION AND INCLUSION MANAGER		
<u>CONTACT DETAILS</u>			
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STATEMENT OF CONFIDENTIALITY
None

BRIEF SUMMARY

Southampton has three PFI (Private Finance Initiative) schools in the City – Cantell, Redbridge and Woodlands, all of which are pursuing academy transfers. The Council is working hard to support the schools in their wish to become academies and to avoid any unnecessary delay. The Council makes a monthly payment to the PFI provider (Interserve) that covers the element attributable to the initial capital cost of building the facilities, the on-going cost of maintaining the facilities, an element attributable to the total financing costs for the project; and the contractor's agreed overheads and profit. The PFI concession agreement details the conditions under which the contract could be terminated and compensation payments required. The PFI arrangements would be altered as a result of the academy transfers and it is the alterations and associated risks which are the subject of this paper.

RECOMMENDATIONS:

- (i) To note and accept the risks associated with the conversion of Cantell, Redbridge and Woodlands (the three PFI schools) to academy status.

REASONS FOR REPORT RECOMMENDATIONS

1. This report is being brought forward to members to enable the academy transfers to proceed, having due regard to the changes to the management of the contractual and financial risks to the Council that will be a direct result of the transfer.

ALTERNATIVE OPTIONS CONSIDERED AND REJECTED

2. The Council have debated this issue with the DfE for several months. However, ultimately the DfE has indicated that it is not willing to change its current position and deviate from the standard wording of the PFI academy conversion documents, believing that by virtue of the DfE's ability to control the Academy, the Council would be sufficiently indirectly protected. The

Council could continue to challenge this. However, doing so would need to be considered against the backdrop that attempts thus far to get the DfE to change its position have proved fruitless and that the chances of events taking such a course as to actually trigger a termination and the Council becoming obliged to pay the associated termination sum are practically very slim. As such, there seems little point in pursuing this further.

3. The Council's independent legal advice is clear that the Secretary of State could insist on forcing these conversions through. The Council's only right of challenge would be by a judicial review to establish that the Secretary of State had acted unreasonably in insisting on these transfers on such terms despite our concerns. Notwithstanding the significant costs involved nor the other practical consequences of so doing, it is not possible to predict with any certainty how successful such a challenge would be.

DETAIL (Including consultation carried out)

4. One of the DfE's main principles on academy conversions is that broadly no party (i.e. the Local Authority or the School) should be any better or worse off after the transfer. Academy conversions are effected using DfE standard form documents which seek to adhere to that principle. Inevitably, certain consequences of the conversion process do alter the position. The PFI concession agreement itself ought to remain largely unaffected as a result of the transfer other than essential amendments. Equally, the DfE has made it quite clear that the LA cannot use the academy process as an opportunity to transfer risk to the schools nor to pass the responsibility for paying the unitary charge to the schools. The schools will continue to contribute to the unitary charge but the Council will remain primarily liable to the PFI contractor for the payment of the unitary charge.
5. However, there is one significant commercial issue in relation to the termination of the contract which poses a risk, albeit a low risk, to the Council. At present the Council could cause the contract to default by impeding the PFI contractor in its delivery of the specified services. Or the Council could break the exclusivity arrangements by directly engaging a third party to provide certain services instead of it. This could result in the termination of the PFI Concession Agreement and a requirement on the Council to pay a termination payment. It is also possible that the schools could act similarly and so trigger a termination and the requirement to make that termination payment. The chances of a school triggering this are relatively slim as the schools are under the authority of the Council. The Council could step in to prevent or stop the schools from taking any actions that could lead to termination. If a school had caused termination, resulting in an obligation to make a termination payment, the Council would have the authority to reclaim some of the compensation payment.
6. If the schools became academies, the Council loses the authority to step-in (a right which will pass to the DfE) and with that the ability to control this particular risk. The DfE model documents state that the Council can inform the DfE if it has concerns that the academy's actions could cause a default in the contract and ask the DfE to intervene to prevent this. However, the Council's view (which has been corroborated by external legal advice) is that this does weaken the Council's ability to manage this risk.

7. The DfE have pointed out that there is limited risk here in practice since there are no previous examples of a school's actions resulting in a termination of a PFI contract. It would be in no-one's interest (the DfE, Academy or local authority) to allow a situation to develop to lead to termination. The DfE would use their own powers of intervention to prevent the situation from getting to that stage. The chances of a breach occurring are low and the DfE have assured us that they will act appropriately and have appropriate powers to prevent this happening. However, the result of the PFI contract being terminated on account of any such breach could be a significant financial cost to the Council. This obligation is not new – the Council became contractually liable for such sum when the PFI contract was entered into in 2001. The difference is that the control would be indirect via the DfE rather than direct. As such, Councillors and the Chief Financial Officer have requested that the issues be presented to Cabinet, hence this paper.
8. Discussions on this issue have been ongoing with the schools and DfE over the last 12 months. The Council had sought to add a clause to the Schools Agreement and the Principal Agreement (the relevant conversion documents which detail what the PFI arrangements will be post academy transfer) which would have transferred the financial risk to the schools. This was rejected by both the schools and the DfE.
9. The Council received independent legal advice confirming that its concerns were valid but also that the Secretary of State could force the academy transfers through on imposed terms, if the Council continued to dig its heels in over the position leading to a stalemate. As such, we have accepted the DfE's view on this issue and have decided to concede this point.

RESOURCE IMPLICATIONS

Capital/Revenue

10. While the risk of a breach leading to termination occurring are low, the financial cost to the Council if the PFI contract were terminated is extremely high. If actions resulted in the contract being terminated in 2013, the Council would be liable to pay the outstanding senior debt, share capital and any redundancy payments for employees of the contractor and subcontractors reasonably incurred as a result of the termination.
11. Redundancy costs are difficult to determine at this time, however the senior debt outstanding and share capital value is estimated to be circa £45 million.

Property/Other

12. The significant property implication is that post-transfer the Council will lose the power of step-in at the schools (a right which will pass to the DfE). This is currently the way in which the Council can mitigate the risk of the PFI contract being terminated on account of the actions of the schools.
13. It should be noted that as part of the academy transfer, a 125 year lease will need to be put in place to allow the academy to occupy the site. The lease contains clauses which reflect any rights of access that have been granted to the PFI contractor and to address the fact that the PFI contractor has maintenance and other obligations (e.g. insurance) under the PFI project agreement. The lease will need to be agreed by the LA, DfE and the academy trust.

LEGAL IMPLICATIONS

Statutory power to undertake proposals in the report:

14. The Academies Act 2010 requires the local authority to process both voluntary and compulsory transfers to Academy status as quickly as possible. The process of transferring schools to Academy status is set out in the Act and requires the Council and schools involved to: dissolve the existing governing body and establish a new Academy Trust and Governing Body; provide a 125 year long-lease to the Academy Trust to occupy and be responsible for the school land and buildings; and TUPE transfer the existing school staff from the employment of the Council to the employment of the Academy Trust. The DfE provides a suite of model documents that govern the conversion process. There are additional and more complicated documents which need to be used when the conversion involves a PFI arrangement.

Other Legal Implications:

15. N/A

POLICY FRAMEWORK IMPLICATIONS

16. N/A

KEY DECISION? Yes

WARDS/COMMUNITIES AFFECTED:	Bassett, Redbridge and Harefield
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SUPPORTING DOCUMENTATION

Appendices

1.	None.
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Documents In Members' Rooms

1.	None.
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Equality Impact Assessment

Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.	No
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Other Background Documents

Equality Impact Assessment and Other Background documents available for inspection at:

Title of Background Paper(s)	Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)
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1.	None	
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