MERSEYSIDE FIRE AND RESCUE AUTHORITY

MEETING OF THE:	**AUTHORITY**		
DATE:	**11 NOVEMBER 2021**	**REPORT NO:**	**CFO/061/21**
PRESENTING OFFICER	**CHEIF FIRE OFFICER**		
RESPONSIBLE OFFICER:	**STEWART WOODS TEL: 4518**	**REPORT AUTHOR:**	**STEWART WOODS**
OFFICERS CONSULTED:	**IAN CUMMINS RIA GROVES JUSTINE GUY**		
TITLE OF REPORT:	**PFI CONTRACT - RE-FINANCING OF THE SENIOR DEBT**		

APPENDICES:	

Purpose of Report

1. To inform Members that the new owners of the PFI Contract Bilfinger Berger Global Infrastructure (BBGI) have initiated a scoping exercise to consider refinancing of the senior debt within the PFI Contract.

Recommendation

2. That Members;
   a. note the contents of the report
   b. agree for the signing of any re-financing deal is delegated to the Director of Finance and Procurement, following consultation with the CFO and Chair of the Authority. A subsequent Authority report to be submitted detailing the outcome of any re-financing.

Introduction and Background

3. MFRA procured 7 new Fire Stations through a joint PFI project between Merseyside, Lancashire and Cumbria, providing a total of 16 Fire Stations across the 3 Services.

4. The first station was completed in November 2011 and the associated PFI contract runs until July 2038. During this time each Authority pays a monthly fee to the contractor, currently £574,770 per month across all three Authorities, known as the Unitary Charge.

5. The Unitary Charge covers the financing and capital costs of the construction of the buildings, plus their maintenance costs until July 2038. The construction of the buildings was financed by borrowing from banks, and the majority of the costs covered by the charge relate to the repayment and servicing of this debt. The Unitary Charge is currently funded by a PFI grant from government and contributions from each Authority.

6. Following the sale of the project Company (ProjectCo) from Balfour Beatty's investment to BBGI on 6th July 2021, BBGI have initiated a scoping exercise to consider the refinancing of the Senior Debt within the PFI Contract. Most PFI contracts contain standard provisions whereby if the debt used to finance the initial construction phase of a project can be refinanced at a lower cost, then the benefit (after transaction costs, advisory fees and disbursements) is split between the Authority and the PFI Contractor. In these arrangements, the debt to be refinanced is often referred to as Senior Debt and the providers of it are known as Senior Funders.

7. The interest rate charged to the PFI Contractor broadly comprises two elements:
    a. The underlying interest (swap) rate
    b. A profit margin charged by the Senior Funder

8. Refinancing opportunities generally exist where the market rate for the profit margin element falls below that currently charged by the incumbent Senior Funder. However, any refinancing exercise attracts significant early redemption penalties as well as legal and advisory fees. The reduction in margins must therefore be significant enough to offset these costs.

9. The approach from BBGI has been made at this time because of the historically low level of interest rates available at present.

10. The original Senior Debt was approximately £50.4m, of which approximately £40.6m remains outstanding. The current Senior Debt Lenders are DZ Bank and Nord LB. The PFI contract includes provision for payments to be made upon termination. If the contracts were terminated by the choice of, or through default by the Authorities, then the Authorities would have to make a termination payment, one element of which would be a requirement to pay early redemption penalties, i.e. the cost for prematurely ending the existing funding arrangement between the Project Company and the Senior Debt Provider.

11. Although there would be an increase in the outstanding debt on the scheme, it is expected that the total value of the remaining repayments will be lower than those currently planned, due to the expected reduction in the interest rate charged on the new loan debt.

12. At this stage BBGI have approached the market to seek terms. Based upon their work, BBGI have advised the Authorities that the draft terms being offered by prospective funders are likely to result in a net gain.

13. Any net gains from the refinancing would be split between the Authorities and the Project Company, in line with the relevant provisions in the Project:

    a. Up to £1million - benefit of 50% (with 50% payable to the Project Company)
    b. Between £1million and £3million - benefit of 60% (with 40% payable to the Project Company)

    c. Over £3m - benefit of 70% (with 30% payable to the Project Company)

14. Any net gain would then be split across the 3 Authorities using the percentages agreed in the Co-operation agreement
    a. Lancashire 25.014%
    b. Cumbria 33.071%
    c. Merseyside 41.915%

15. The gain can be paid either as a one-off lump sum payment, or as a reduction to the Monthly Unitary Charge, but all three NW Authorities must agree on what option.

16. The financial and legal arrangements in PFI deals are extremely complex. With this in mind Finance Advisors and Legal Advisors have been approached to provide advice to the Authorities to ensure the Authorities achieve optimum value for money from any refinancing but to also protect the Authorities interests throughout the negotiations.

17. It is not clear at which precise point and on what date the Authorities will be required to enter into contractual arrangements to finalise any refinancing arrangement, however, it is expected that the refinancing transaction will be executed in late November – mid December.

18. In the event the refinancing stops due to the Authorities not approving the transaction at the final stage (i.e. there is no change in lending terms, just the Authorities not satisfied with their refinancing gain) the Authorities will need to cover their advisory fees, with the ProjectCo covering the rest.

19. In order to proceed with the re-financing the Authorities need to sign Heads of Terms Document with the ProjectCo and the 3 Authorities have agreed to sign up to Memorandum of Understanding in terms of the arrangements of the refinancing between them prior to agreeing to any Heads of Terms.

20. Each Authority needs to agree its approval process and timeframe for any eventual Re-financing option. It is recommended that signing of any re-financing deal is delegated to the Director of Finance and Procurement, following consultation with the CFO and Chair of the Authority. A subsequent Authority report detailing the outcome of the re-financing will be submitted to Authority.

Equality and Diversity Implications

21. There are no direct implications arising from this report. .

Staff Implications

22. No staff implications have been identified as a result of this re financing exercise.

Legal Implications

23. A memorandum of Understanding will need to be signed by all 3 Authorities prior to agreeing to the head of Terms.

24. The PFI contract has an established governance structure in place with Merseyside taking the lead authority role. Any Refinancing will be reported back via the PFI project liaison group meetings.

25. External legal advice will be required due to the volume of work and specialist nature of the contract.

Financial Implications & Value for Money

26. Authorities potential costs
    a. Legal Advisors   Cost approx. £30k
    b. Financial advisor's costs   £30k.

27. ProjectCo potential costs
    a. Legal Advisors   Cost   £60k
    b. Lenders Legal Advisors   £43k
    c. Model Auditors   £13k

28. The ProjectCo have indicated that the potential share from the Refinancing Gain to the three Authorities after all the fees, charges and penalties could be in the range of £400k to £620k. This could result in the following share:

If the three Fire services achieve a £400k saving: -
Cumbria - 33.071% = £132,284
Lancashire - 25.014% = £100,056
Merseyside - 41.915% = £167,660

If the three Fire services achieve a £620k saving: -
Cumbria - 33.071% = £205,040
Lancashire - 25.014% = £155,086
Merseyside - 41.915% = £259,874

Risk Management, Health & Safety, and Environmental Implications

29. Expert Legal and financial advisors have been approached to carry out due diligence on the refinancing.

30. If the Authorities decide not to continue or accept the new refinancing deal, they will be liable for their share of the Authorities advisory costs.

Contribution to Our Vision: *To be the best Fire & Rescue Service in the UK.*

Our Purpose: *Here to serve, Here to protect, Here to keep you safe.*

31. Any savings from any reduction in the unitary change could be used to contribute to the Authority vision to be the best Fire and Rescue service in the Uk.

BACKGROUND PAPERS

N/A

GLOSSARY OF TERMS

BBGI Bilfinger Berger Global Infrastructure

MFRA **M**erseyside **F**ire and **R**escue **A**uthority.

MFRS **M**erseyside **F**ire and **R**escue **S**ervice

PFI. Private Funded initiative