Annex 3

Excellent Homes For All – Project Agreement and Back to Back Agreement

Principles of Risk Share

1 Introduction

1.1 KCC will be the sole signatory to the PFI contract but this contract is being procured on behalf of KCC and five District Council partners. Therefore, in order to reflect the true relationship of the partnership a Back to Back agreement will be signed between KCC and the District Partners to ensure that the risks and benefits in the Project Agreement are shared. The Back to Back Agreement will be signed prior to KCC signing the Project Agreement and will tie the District Councils to the contract as though they are part of the main PFI contract. The Back to Back agreement covers the governance of the project, nomination rights, risk sharing and contract management requirements for the project.

2 Benefits

2.1 Through the EHFA project the six partners will receive 35 years of nomination rights to new specialist social housing secured through a £66.8 million grant from central government. The nomination rights are set out in the Nominations and Allocations Protocol.

3 Risks

3.1 This new social housing will be developed, run, and managed by an independent consortium (Galliford Try Investments and West Kent Housing Association) and maintained to a high standard.

3.2 The consortium will be responsible for the ongoing running of the housing, and the major risks associated with that, for instance:

- Design and construction risk
- Collection of rents and service charges
- Ongoing maintenance
- Demand
- Tenancy management
- Void management
- Specific change in law relating to Housing

3.3 However, as the procuring Authorities, through the PFI contract the County Council and District Councils will share some risks. The risk profile has been assessed by the Treasury and the risks the Councils will take are standard risks for the public sector to take under these contracts. Where possible we have tried to achieve a better position for the Authorities than the Treasury guidance, although our ultimate risk position has to be approved by them before the project can close.

4 Managing Authority Risks

4.1 Appendix A is a list of potential risks and areas for decision making that the Authority will manage under the contract. The Back to Back Agreement outlines how those risks and decisions will be dealt with between partners, according to who is best able to manage them.

5 Principles of Risk Share

5.1 The Back to Back Agreement will contain a number of key principles which will prevent any single partner from taking action which has a cost implication for other partners without all affected parties agreeing. It will ensure that:

- Any decisions under the Back to Back which may result in an increase of risk or cost to any of the partners must be taken as a unanimous decision between all partners through the Project Board (which will have one representative per partner).

- if a risk occurs under the contract which is the result of a choice made by all of the partners or is the fault of no partners then a mechanism should be applied to share those costs.

- if a risk occurs as a consequence of the actions of one party, that party should be responsible for the cost

6 Shares

6.1 The share of any increase in cost falling on all partners has been agreed between the Project Board (District Council Heads of Housing and KCC's Director of Commissioning and Provision for Older People). The share was agreed as KCC taking a fixed percentage of the cost and the remaining amount being shared between the partners on the basis of the number of tenanted apartments they expect to gain from the project. This has taken into account land contributions and also KCC's Authority Contribution to the Unitary Charge. The share is therefore intended to reflect a) what each partner stands to gain from the project and b) what each partner is contributing to the project.

The shares of any costs associated with future risk are proposed as follows:

	No of units	**Share**
		%
KCC	**-**	25.0
Ashford	52	17.7
Dartford	40	13.6
Dover	40	13.6
Thanet	49	16.6
Tunbridge Wells	40	13.6
	221	100.0

Key Project Agreement Risks and Decisions and their Treatment in the Back to Back Agreement

The Back to Back contains a number of key principles which will prevent any single partner from taking action which has a cost implication for other partners without all of the affected parties agreeing to such action. It will ensure that:

- if a risk occurs under the contract as a consequence of the actions of one party, that party should be responsible for the cost (**Direct Costs**)

- if a risk occurs under the contract which is the result of a choice made by all of the partners *or* is the fault of no partners then a mechanism should be applied to share those costs (**Shared Costs)**

Potential risks.

The risk allocation set out in the table below shows the profile that reflects the Project Agreement with the Contractor and how the risk is then shared between the County Council and District Council partners through the Back to Back Agreement.

Key potential risk or decision areas	Likelihood of risk occurring and ways to manage risk	Treatment in Back to Back
Ground Condition Risk Under the Project Agreement the Contractor takes the risk for site condition on the basis that detailed investigations and surveys have been carried out prior to financial close. Where there are existing buildings which require demolition, to the extent that there are problems with ground condition beneath such buildings which could not reasonably have been discovered from the surveys carried out this risk falls to the Authority.	In relation to site condition under existing buildings the risk can be mitigated by ensuring that ground investigations very close to the existing building are carried out. The bidder has already carried out surveys on all of the sites. This will enable the bidder to take most of this risk and therefore leave the partners less exposed.	**Direct Cost (KCC or ABC)** - risk should be borne by the party who owns that site. In this case all but one of the sites are provided by KCC.
Specific Change in Law Risk Specific Change in Law is a change in law which refers specifically to the service area to which the contract relates. The cost of a Specific Change in Law falls to the Authority under the Project Agreement, however the contractor has	It is likely that, where a Project runs for 25 years, there will be specific changes in law which directly affect the Services being provided under the Agreement. Changes in Law can be monitored but	**Direct Cost (KCC)** – For specific change in law risk relating to care,

Key potential risk or decision areas	Likelihood of risk occurring and ways to manage risk	Treatment in Back to Back
agreed to take Specific Change in Law relating to Housing. Kent is one of few projects that have successfully achieved this transfer of risk to the Contractor.	not controlled. It is unlikely that this risk will arise without prior warning and if it does occur, it will also affect other care projects in the same way. It will therefore be an issue that KCC faces across a range of facilities.	KCC will be the responsible party.
Employee Default Risk Any staff visiting the accommodation causing damage or preventing the contractor from carrying out their duties will be the responsibility of either KCC or the relevant District. KCC's responsibility for provision of the Care Services means that it is liable for the acts or omissions of Care Providers acting in the course of their duties.	Both KCC and each DC will be responsible for its own staff and any damage they may cause. Therefore it is the responsibility of KCC and each DC to train and supervise staff accordingly. District Councils may have occasional visiting staff to the sites but will not have on site staff.	**Direct Cost (KCC or the DCs)** – the party responsible for the staff who created the problem will be responsible for the cost.
Insurance claim made where the Authority acts as insurer of last resort. Where a risk becomes uninsurable through no fault of the Contractor the cost falls to the Authority.	The likelihood of significant changes in the insurance market is difficult to predict. However, a sudden change that renders areas of a Housing PFI Project uninsurable is relatively unlikely. KCC and the DCs are only required to cover a share of this risk in the event that a risk that has become Uninsurable through no act or omission of the Contractor and this limits the likelihood of costs falling to KCC and the DCs in this regard.	**Shared Cost** - if a risk occurs under the contract which is the result of a choice made by all of the partners all partners should share the cost partners all partners should share the cost.

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Insurance Premium Risk Sharing This mechanism ensures that both the benefit and burden of significant fluctuations within the insurance market are shared between the Contractor and the Authority. To the extent that it follows a review of actual insurance costs against the base insurance costs if there is a cost increase of more than 30% for a period, 85% of such cost shall be covered by KCC and the DCs in accordance with the agreed Back to Back sharing mechanisms.	It is difficult to manage the risk in relation to an increase in insurance costs which is so significant that a share of the increase is required to be covered by KCC and DCs. Fluctuations in the cost of insurance can occur at any time and over the term of the Project it is possible that certain insurances could rise or fall significantly. The contractor takes the first 30% of the burden of any increase. It is intended that these costs will be funded through the project account, where there are sufficient funds.	**Shared Cost** - if a risk occurs under the contract which is the result of a choice made by all of the partners all partners should share the cost partners all partners should share the cost.
Termination on Authority Default Termination for Authority Default can only occur in very specific circumstances for example non-payment of a specific sum etc. which can all be managed and avoided by KCC and the DCs. In the event that this head of termination occurs there is a significant cost implication for KCC and the DCs.	This is within the control of KCC and the DCs because providing they comply with their obligations under the contract this should not occur.	**Shared Cost or Direct Cost** – depending on the scenario that leads to Authority Default. If a risk occurs under the contract which is the result of a choice made by all of the partners all partners should share the cost. If, however, Authority default was triggered by one party, that party would bare the cost.
Termination on Force Majeure Termination in the event of Force Majeure would lead to significant cost implications for the Authority and the DCs.	The occurrence of a Force Majeure even is not within anyone's control. However, it is reasonably unlikely to occur as it is limited to specific extreme events.	**Shared Cost** - if a risk occurs under the contract which is the result of a choice made by all of the partners all partners should share the cost.

Key potential risk or decision areas	Likelihood of risk occurring and ways to manage risk	Treatment in Back to Back
Voluntary Termination Where the Authority needs to terminate the agreement on a voluntary basis there is a significant cost implication.	This is completely within the control of KCC and the DCs who, under the Back to Back agreement, will need to agree unanimously to Voluntary Termination.	**Shared Cost** – this would have to be agreed by the Project Board. if a risk occurs under the contract which is the result of a choice made by all of the partners all partners should share the cost.
Termination on Contractor Default or for corrupt gifts and breach of the refinancing provisions. The Authority may terminate the agreement for default by the Contractor in specific defined circumstances and if the Contractor is found to have given a corrupt gift to a Council officer or breaches the contractual requirements with regards to refinancing its funding for the project. In the event that this head of termination occurs: a) for termination due to Contrator Default the project is retendered if there is a liquid market available. The new contractor pays to the outgoing Contractor the sum bid for the contract by way of compensation. If there is no liquid market an expert determines the value of the contract and this value is paid by the Authority as compensation to the Contractor. Given the nature of the facilities (Social Supported Housing) it is highly likely that that a Liquid Market will be available. The test of the availability of a liquid market is only 2 bidders able and willing to bid. Therefore in this case no compensation will need to be paid to the contractor. b) on termination for corrupt gifts and breach of the refinancing provisions all outstanding debt is paid as	The default of the Contrator is outside of KCC's and the DCs control. There is a direct agreement between KCC, the Contractor and the bank which allows the bank to step in if the Contractor is underperforming and likely to be in default to rescue the project by running it itself or finding another contractor to run it. This would occur before the termination scenario occurred and would be likely to solve the problem.	**Shared Cost** - If a risk occurs under the contract which is the result of a choice made by all of the partners all partners should share the cost.

Key potential risk or decision areas	Likelihood of risk occurring and ways to manage risk	Treatment in Back to Back
compensation by KCC and the DCs. However by the Authority can choose not to terminate the agreement and to solve issues by other means to ensure that no compensation for contractor default is payable by partners.		
Requests for changes to works or services There is a protocol for making changes to the project. Where KCC or a DC requests changes to the works and or Services these may attract an increase in price which must be covered by KCC and the DCs. Where the Contractor requests changes to the works and or services, KCC and the DCs may agree to such changes which may have an impact on pricing.	This is within the partners' control because it requires the Authority to raise a change, or to accept a change proposed by the Contractor. Amongst the Local Authority partners, If a party wishes to propose a change to the works then that party must support the cost. If however, the change has a wider application where all councils will benefit then all those benefiting will agree on the proportions to be paid by each partner. This is to include small works changes. This is manageable because the partners can reject the contractors request for changes to the works and services provided they are not required pursuant to a change of law.	**Shared Cost or Direct Cost** – this would have to be agreed by all partners through the project board. If costs are incurred under the contract as a result of a choice made by all of the partners a mechanism should be applied to share those costs. If one partner requires a change but others do not – a decision could be made to allow that change subject to the party in question picking up the cost.
Authority Step In The Authority may step into the place of the Contractor under the Contract in the event that it is required to discharge a statutory function or there is a serious risk to health or safety of persons or property or to the environment. Where there is a step in but the Contractor is not in breach of its obligations the Authority must indemnify the Contractor against losses incurred as a result of this.	KCC has a right to step in under the contract which may need to happen very quickly. The need to step in would be agreed unanimously by the project board and the costs would be shared in accordance with the mechanism in the back to back agreement.	**Shared Cost** - this would have to be agreed by the Project Board. If a risk occurs under the contract which is the result of a choice made by all of the partners all partners should share the cost partners all partners should share

Key potential risk or decision areas	Likelihood of risk occurring and ways to manage risk	Treatment in Back to Back
		the cost.
Emergencies Decision The Authority has the ability to take over the facilities in the event of an emergency. The Authority will be responsible for ensuring that the Contractor is in a no better no worse position as the result of the authority needing to take over or use the facilities being contracted in an emergency. Where the Contractor is required to provide additional services these must be paid for.	It is possible that some form of emergency will occur and such events are difficult to foresee. However, it would be an authority decision to undertake this action. It is unlikely that the cost impact would be excessively high in the event of an emergency.	**Direct Cost (KCC or DC)** – the party (or parties) who require the use of the facility for emergency purposes should be responsible for the cost
Maintenance Surveys Decision The Authority has the right to carry out maintenance surveys every two years if it reasonably believes that the Contractor is in breach of its maintenance obligations. In the event that a survey is undertaken and the Authority finds that the Contractor is not in breach of its maintenance obligations then the cost of the survey falls to the Authority.	The risk in connection with this clause is within the control of the partners as decisions to carry out maintenance surveys will need approval by the project board.	**Shared Cost –** partners would have to agree that a survey was required**.** If a cost is incurred under the contract which is the result of a choice made by all of the partners all partners should share the cost.
Disputes Procedure Where there is a dispute, the costs of pursuing a dispute are to be shared by all parties involved in such dispute.	Costs can be mitigated through endeavouring to resolve any dispute through early ADR measures.	**Shared Cost –** If a cost is incurred under the contract which is the result of a choice made by all of the partners all partners should share the cost.