

Birmingham City Council

Report to Cabinet

8 June 2021



Subject: Highway Maintenance and Management PFI Contract

Report of: Acting Director, Inclusive Growth and Interim Director of Council Management

Relevant Cabinet Members: Councillor Waseem Zaffar, Transport and Environment
Councillor Tristan Chatfield, Finance and Resources

Relevant O&S Chairs: Councillor Liz Clements, Sustainability and Transport
Councillor Mohammed Aiklaq, Resources

Report author: Kevin Hicks, Assistant Director, Highways and Infrastructure, Telephone No: 0121 303 7939
Email Address: kevin.hicks@birmingham.gov.uk

Are specific wards affected?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No – All wards affected
If yes, name(s) of ward(s):		
Is this a key decision?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
If relevant, add Forward Plan Reference: 008501/2021		
Is the decision eligible for call-in?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Does the report contain confidential or exempt information?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Exempt Appendix (D): Exempt information paragraph 3: Information relating to the financial or business affairs of any particular person (including the Council).		

1 Executive Summary

- 1.1 On 16 March 2021 Cabinet was advised of challenges in delivering the outcomes from the Council's Highway Maintenance and Management Private Finance Initiative (PFI) contract and the implications for future services delivery. Officers have consequently been working to develop solutions to optimise the investment and the value for money that the Council gets from a future long-term contract.
- 1.2 A commercial agreement between the complex structure of stakeholders in the project is now required to take the contract forward as a PFI contract. In its decisions in March 2021, Cabinet delegated authority to officers to negotiate an agreement regarding the future approach to the contract. This report recommends decisions to Cabinet based on the outcome of those negotiations.

2 Recommendations

That Cabinet:

- 2.1 Delegates authority to the Acting Director Inclusive Growth, in consultation with the Cabinet Members for Transport and Environment and Finance and Resources and the Interim Director of Council Management and the City Solicitor to enter into a commercial agreement to extend the Restructuring Period, as set out within the Heads of Terms described in Exempt Appendix (D), subject to:
 - 2.1.1 The agreement remaining within the commercial parameters approved by Cabinet on 16 March 2021 and the Heads of Terms; and
 - 2.1.2 Approval from Department for Transport (or confirmation that approval is not required).
- 2.2 Authorises the Assistant Director, Highways and Infrastructure to:
 - 2.2.1 Develop and implement programmes of capital investment works as described in paragraph 3.16 below;
 - 2.2.2 Develop and take all actions necessary to implement the commercial agreement reached;
 - 2.2.3 Approve payments by the City Council or on behalf of Birmingham Highways Limited in accordance with the commercial position of the City Council as approved by Cabinet; and
 - 2.2.4 Undertake all actions necessary to transfer and / or novate ownership of project systems and components of the Management Information System to the City Council. Following transfer undertake a competitive re-procurement for the supply and configuration of these systems and appoint a new vendor as appropriate; and
- 2.3 Delegates authority to the City Solicitor to execute, seal and complete all necessary agreements and documentation to give effect to the above recommendations.

3 Background

Context

- 3.1 The Council's Highway Maintenance and Management PFI contract commenced on 7 June 2010 and is a 25-year contract to rehabilitate and maintain the Council's highway infrastructure to defined standard. Its key features are described and shown in Appendix B.
- 3.2 As was set out in the Cabinet report of 16 March 2021 (see Background Reports in section 9 below), the Council entered into a commercial settlement regarding the PFI contract on 29 June 2019. That settlement provided a period of up to two years to 29 June 2021 to enable the Council and Birmingham Highways Ltd (BHL) to seek to restructure the contract for its remaining duration until June 2035 (called the "Restructuring Period"). A restructuring would require approval by all project stakeholders and requires:
 - 3.2.1 The Council and BHL to agree revisions to the contract;
 - 3.2.2 The proposed future contract to meet pre-specified criteria for the lending banks and the Council (or to waive those criteria); and
 - 3.2.3 Continuation of the Council's PFI grant funding being approved.
- 3.3 If any of the above requirements for restructuring are not met, then the contract may end.

Commercial agreement

- 3.4 The Council submitted its Updated Business Case to DfT on 1 March 2021. The document was included within Exempt Information to the report to Cabinet on 16 March 2021. The response from DfT is awaited.
- 3.5 The project structure and parties are described in Appendix B. In parallel to consideration of the business case, negotiations are ongoing with relevant parties to seek to reach a commercial agreement within the parameters approved by Cabinet on 16 March 2021. The purpose of negotiations is to agree the commercial terms on which a future project is taken forward between the Council, lenders, BHL and BHL's investors.
- 3.6 The 16 March 2021 report explained that a revised set of long-term arrangements will not be completed by the end of the Restructuring Period on 29 June 2021. It is presently anticipated that this will be completed by the end of August 2023, although it should be noted that this remains subject to a number of factors. To ensure that the PFI contract does not end, an extension to the Restructuring Period is required. The commercial agreement will provide this extension.
- 3.7 Through negotiations to date, the Council has agreed Heads of Terms to extend the Restructuring Period that fall within the parameters agreed by Cabinet. Further negotiation is expected to conclude a long-term commercial arrangement.

Operational Services

- 3.8 Following Cabinet's decision on 16 March 2021, BHL extended its Interim Services Contract with Kier Highways Ltd to 30 December 2021. This ensures that the Council has continued provision of services to ensure that its highways are kept safe and available.
- 3.9 The Council's preference is that these services are extended for a longer period and Cabinet has already approved an extension to that effect. The approach to providing these services beyond 30 December 2021 will be agreed as soon as possible.
- 3.10 As part of the approval by Cabinet of the 2019 Settlement Agreement, the Council has taken responsibility for the systems comprising the contract's management information system. Further actions are proposed within the recommendations with how these systems are owned and procured to ensure that the Council is able to have such services provided in the most competitive way going forward.

Programmed Maintenance

- 3.11 Continuing investment in Programmed Maintenance has been recognised as a priority given the significant backlog that has arisen, particularly on surfacing. It is important to emphasise that whilst the Council is investing significantly in Programmed Maintenance, improvements will be seen through sustained investment over time, delivered in tandem with effective Routine and Reactive Maintenance.
- 3.12 Under the 2019 settlement the Council committed to £50m of investment in Carriageway and Footway by June 2021. Schemes continue to be completed but from June 2019 to May 2021 completed works were as shown in Table 1 below.

Table 1: Surfacing Programmed Maintenance delivered (to 25 May 2021)

Asset / component	Schemes	Planned Works	Value completed on site ¹	Quantity Delivered
Priority Schemes (Carriageway and Footway)	25 / 25	£ 3.36m	£ 3.36m	58,912m ²
Carriageway	139 / 162	£ 22.15m	£ 19.62m	374,512m ²
Footway	86 / 156	£ 20.92m	£ 14.2m	137,835m ²
Surfacing Design		£ 3.83m	£ 3.63m	
Total	250 / 343	£ 50.26m	£ 40.81m	571,259m²

Notes:

¹ The Council is invoiced upon certification of completion of works. In an ongoing programme the amount paid to date will therefore always be less than the volume of work completed on site.

- 3.13 In addition to surfacing, 1,808 street lighting columns have been replaced so far of 2,023 planned replacements, at a cost of £ 2.8m.
- 3.14 Some schemes have been deferred due to impact on other works (including schemes relating to the Commonwealth Games and the A34 SPRINT route, while some schemes are being reviewed. 11 carriageway and 5 footway schemes have been added to the programme (included in Table 1 above). It is anticipated that the remaining carriageway and footway schemes will be completed by August 2021 to complete the £50m investment.
- 3.15 There is some way to go with improving the condition of the network as a whole. The investment to date has been important in arresting the deterioration of the network but considerable further investment is required to improve condition.
- 3.16 Subject to confirmation that the Council will remain in receipt of its PFI grant, further Programmed Maintenance is proposed in 2021-22 as follows:
- 3.16.1 *Carriageway and Footway Surfacing (£40m)*: Officers have developed a list of potential schemes, which has been validated with video survey and site visits. This is prioritised and has been developed from:
- Completion during 2021 of schemes from the 2020-21 programme (where it is appropriate to do so); and
 - Analysis of survey information, condition maps, complaints, recommendations from Local Engineers and highway stewards and other Council priorities.
- 3.16.2 *Street Lighting (£3m)*: Proposals have been developed based on priorities for asset replacement and specific energy / carbon reduction priorities. These comprise:
- Major Programmed Maintenance to replace lighting on the A38(M) Aston Expressway and Five Ways Underpass; and
 - A small number of local lighting replacement and upgrade schemes.
- 3.17 Programmes will be developed as follows. Consultation on a provisional list of schemes will be undertaken with Members and Local Engineers. An indicative programme will then be developed. There may be changes in this indicative programme due to other activity on the network. The estimated timeline is given in Table 2 below.

Table 2: Programme development

Activity	Period	Output
Consultation with Councillors on provisional list	Early to mid-July 2021	Revised provisional list of schemes
Confirm construction feasibility of provisional list	Mid- to end July 2021	Indicative programme / Draft Forward Planning Notice
Amendments / confirmation of the provisional list	Early August 2021	Provisional programme

Activity	Period	Output
Book road space	Mid-August 2021	Traffic orders etc.
Commence design	Mid-August 2021	Design programme
Commence construction	Late October to early November 2021	Construction programme (3-month forecast)

3.18 It should be noted that this Programmed Maintenance is in combination with Routine and Reactive Maintenance to keep the highway infrastructure safe and resist deterioration in the condition of the asset. This means that smaller / localised repairs will continue where appropriate and in line with the Council's Safety Inspection Strategy. Where schemes are not taken forward as Programmed Maintenance they may still be addressed by Routine and Reactive Maintenance.

Implementation of the commercial agreement

3.19 The route forward with implementation will depend upon the agreed way forward with the project. The different permutations and the Council's proposed approach to those permutations are in Exempt Appendix (D).

4 Options considered and Recommended Proposal

4.1 The recommended proposal is that the Council:

4.1.1 Enters into a commercial agreement to extend the Restructuring Period and continues negotiations regarding the future approach to the contract on the terms described in Exempt Appendix (D); and

4.1.2 Undertakes capital investment as detailed above.

4.2 The alternative option to entering into the commercial agreement is that the Restructuring Period is not extended and / or the project is not restructured. In this position, the contract will end and the Council would lose its £50.311m per annum PFI grant. This would necessitate a full restructuring of how the Council delivers its Highways services, based on a significantly reduced budget.

4.3 The alternative to investing in capital works is that the Council's highway asset will continue to deteriorate significantly and there is a risk that either the cost of keeping the Council's Highways safe increases or that the Council may not be able to comply with its statutory duties.

5 Consultation

5.1 Since the 2019 settlement senior officers from the Council have worked with DfT, advisors to project lenders, BHHL's administrator and the chairman of BHL as part of a steering group regarding the way forward with the project.

5.2 External legal advice, including expert financial and commercial advice, has been obtained from DLA Piper.

- 5.3 DfT as the Council's sponsoring Government department for the project and HM Treasury have also been consulted directly throughout discussions. DfT has worked with the Council to enable alternative solutions to project issues to be considered.
- 5.4 At the request of the Cabinet Member for Transport and Environment an informal, cross-party member working group has been briefed and consulted regarding proposed changes to the service specification. The response from the Chair of the group (Councillor Mike Leddy) is attached as Appendix C, with the detail on how matters are proposed to be dealt with under procurement guidelines and regulations within Exempt Appendix (D).

6 Risk Management

- 6.1 An analysis of risks is contained within Exempt Appendix (D) – section 5 and Appendix D5).

7 Compliance Issues:

7.1 How are the recommended decisions consistent with the City Council's priorities, plans and strategies?

- 7.1.1 The Council has adopted the *Council Plan 2018 to 2022 (2019 update)*. This identifies six outcomes for the city, the first of which is "*Birmingham is an entrepreneurial city to learn, work and invest in.*" Priority 4 under this outcome is that "*We will develop our transport infrastructure, keep the city moving through walking, cycling and improved public transport.*"
- 7.1.2 This decision directly affects investment in and maintenance of the Council's 2,500km highway network and Council-owned infrastructure on it. Such investment will directly reduce the percentage of carriageways that should be considered for structural maintenance; this is a measure for Outcome 1 / Priority 4 of the Council Plan.
- 7.1.3 Citizens' priorities also reflect that road and pavement repairs are the fourth highest priority in the city for citizens.

7.2 Legal Implications

- 7.2.1 The Council has a statutory duty to maintain highway infrastructure, primarily under the Highways Act 1980 and the New Roads and Street Works Act 1991.
- 7.2.2 Under Section 111 of the Local Government Act 1972 the Council has power to do anything that is calculated to facilitate, or is conducive or incidental to, the discharge of any of its functions.
- 7.2.3 The information contained within Exempt Appendix (D) is considered exempt under Schedule 12A of the Local Government Act 1972, as it relates to the financial / business affairs of parties to the Highway Maintenance and Management PFI contract, including the Council.

- 7.2.4 Disclosure of the information within Exempt Appendix (D) would adversely affect the Council's ability to negotiate the best value outcome in relation to the contract and disputes by disclosing its strategy to those with whom it is negotiating. It is therefore not in the public interest to make this information available publicly.
- 7.2.5 Legal documentation will be required to implement (i) the Heads of Terms; and (ii) the finally determined commercial position. This latter category of documents is likely to include amendments to the contract and new sub-contract arrangements.

7.3 Financial Implications

- 7.3.1 The Council has an annual revenue budget for highways maintenance of £50.628m which is currently supplemented by Government PFI grant of £50.311m. Continued provision of this grant is subject to Government determination of the Council's revised business case (as detailed above) and restructuring proposal. The Council has, as part of the original PFI business case proposal, ring-fenced its highways revenue budget and has accumulated a revenue reserve of £181.975m at 31 March 2021 which is ringfenced to support future investment and facilitate the restructuring of the contract.
- 7.3.2 Ongoing receipt of annual PFI grant is dependent on a number of factors including the Council reaching an agreement with the DfT on the revised business case and the Council, BHL and its stakeholders entering into the commercial agreement. The loss of PFI grant would be replaced by annual bidding for grants, which could result in a significantly reduced amount of funding for investment in the City's highways network. Whilst this potential of reduced funding would have an impact on the Council's ability to invest in the network, the Council would still have available its existing revenue budget and reserves to ensure a safe network but at a reduced level of investment.

7.4 Procurement Implications

- 7.4.1 Implications for the wider procurement are set out in paragraph 6.3 of the Exempt Appendix (D).
- 7.4.2 The procurements relating to components of the management information system will be conducted and reported through the existing Council processes.

7.5 Human Resources Implications

- 7.5.1 As advised on 16 March 2021, Cabinet should note that there will be different human resource implications relating to the potential future scenarios. These are also described within Exempt Appendix (D).

7.6 Public Sector Equality Duty

- 7.6.1 A copy of the initial equality assessment screening (reference EQUA682) is shown in Appendix A.

8 Appendices

- 8.1 Appendix A: Equality Assessment
- 8.2 Appendix B: Project Structure
- 8.3 Appendix C: Response from Member Working Group
- 8.4 Appendix D: Exempt Appendix (D)

9 Background Documents

- 9.1 Report of the Acting Director, Inclusive Growth and Interim Chief Finance Officer to Cabinet, 16 March 2021: Highway Maintenance and Management PFI Contract.

Appendix A

Equality Assessment

Title of proposed EIA	Highway Maintenance and Management PFI Contract
Reference No	EQUA682
EA is in support of	Amended Function
Review Frequency	Annually
Date of first review	07/06/2022
Directorate	Inclusive Growth
Division	Highways & Infrastructure
Service Area	PFI Contract Management
Responsible Officer(s)	<input type="checkbox"/> Jenny Bent
Quality Control Officer(s)	<input type="checkbox"/> Janet L Hinks
Accountable Officer(s)	<input type="checkbox"/> Ravinder Sahota
Purpose of proposal	The Highway Maintenance and Management PFI contract delivers investment, maintenance and management services for the council's highway infrastructure to June 2035. This is a decision regarding the commercial management of the contract.
Data sources	relevant reports/strategies; relevant research
Please include any other sources of data	N/A
ASSESS THE IMPACT AGAINST THE PROTECTED CHARACTERISTICS	
Protected characteristic: Age	Not Applicable
Age details:	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Protected characteristic: Disability	Not Applicable
Disability details:	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Protected characteristic: Sex	Not Applicable
Gender details:	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Protected characteristics: Gender Reassignment	Not Applicable
Gender reassignment details:	

	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Protected characteristics: Marriage and Civil Partnership	Not Applicable
Marriage and civil partnership details:	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Protected characteristics: Pregnancy and Maternity	Not Applicable
Pregnancy and maternity details:	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Protected characteristics: Race	Not Applicable
Race details:	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Protected characteristics: Religion or Beliefs	Not Applicable
Religion or beliefs details:	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Protected characteristics: Sexual Orientation	Not Applicable
Sexual orientation details:	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Socio-economic impacts	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Please indicate any actions arising from completing this screening exercise.	There is no specific adverse impact on any of the groups and therefore this will not be applicable.
Please indicate whether a full impact assessment is recommended	NO
What data has been collected to facilitate the assessment of this policy/proposal?	This is a proposed change to the arrangements under which highway maintenance and management services will be delivered. The means by which those services are delivered in so far as they might impact upon protected characteristics is unchanged. The relevant data for this assessment is the commercial and financial information as identified within the report.

Consultation analysis	Feedback from consultation has been included within the report as appropriate.
Adverse impact on any people with protected characteristics.	Not applicable
Could the policy/proposal be modified to reduce or eliminate any adverse impact?	Not applicable
How will the effect(s) of this policy/proposal on equality be monitored?	Not applicable
What data is required in the future?	Not applicable
Are there any adverse impacts on any particular group(s)	No
If yes, please explain your reasons for going ahead.	Not applicable
Initial equality impact assessment of your proposal	This is a proposed change to the arrangements under which highway maintenance and management services will be delivered. The means by which those services are delivered in so far as they might impact upon protected characteristics is unchanged.
Consulted People or Groups	Consultation has taken place with Cabinet Members and elected members, senior officers and Department for Transport, as described in the decision report.
Informed People or Groups	
Summary and evidence of findings from your EIA	The Highway Maintenance and Management PFI contract delivers investment, maintenance and management services for the council's highway infrastructure to discharge the council's statutory duties to maintain and manage the public highway and ensure that it remains available. This decision affects the way in which these services are contracted for and does not change how they are delivered in respect of the potential impact on anyone with a protected characteristic.
QUALITY CONTROL SECTION	
Submit to the Quality Control Officer for reviewing?	Yes
Quality Control Officer comments	
Decision by Quality Control Officer	

Submit draft to Accountable Officer?

No

Decision by Accountable Officer

Date approved / rejected by the Accountable Officer

Reasons for approval or rejection

Please print and save a PDF copy for your records

Yes

Julie Bach

Person or Group

☐ Domenic De Bechi

Content Type: Item

Version: 3.0

Created at 30/04/2021 11:46 AM by ☐ Jenny Bent

Last modified at 30/04/2021 11:46 AM by Workflow on behalf of ☐ Jenny Bent

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Appendix B

Project Structure

The Council's contract (the Project Agreement) is with **Birmingham Highways Ltd (BHL)**. The Council gets circa half the funding for its contract from Government via a PFI Grant, for which **Department for Transport** is the sponsoring government department. The remainder is funded from the Council's revenue budget for Highways, which was ring-fenced in 2010 and continues to be indexed in line with Council budgets.

BHL is a Special Purpose Vehicle (SPV) owned by **Birmingham Highways Holdings Ltd (BHHL)**. BHHL is owned by its shareholders, **Equitix** and **Foresight Group**.

BHL has borrowed c.£193m from a lending group of banks (**Senior Lenders** or **Creditors**), under a lending Facilities Agreement. Of this, c.£153m remains outstanding.

Equity in BHL was funded by a c.£69m loan from its three investors, Amey Ventures, Equitix and Foresight Group. This loan remains in place and ranks behind the debt to Senior Lenders referred to above.

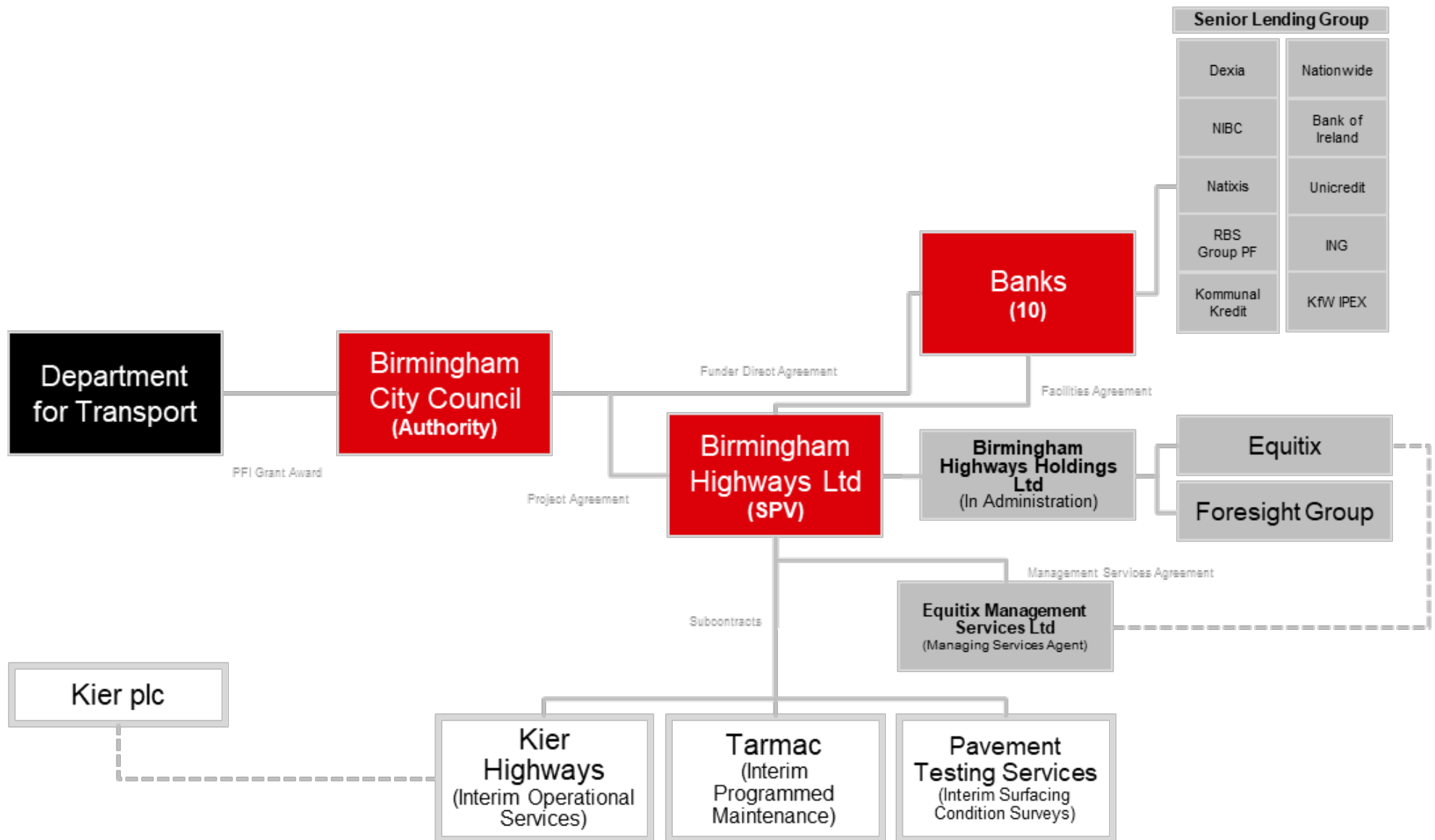
BHL has obligations to deliver the services according to its contract with the Council and repay its borrowing and carries the risks of non-performance under both.

BHL delivers services under its contract with the Council through subcontracts. The current interim principal subcontracts are with:

- **Kier Highways Ltd** (owned by **Kier plc**) for operational services;
- **Tarmac** for interim surfacing schemes; and
- **Pavement Testing Services (PTS)** for condition surveys.

BHL employs **Equitix Management Services Ltd (EMS)** to manage these subcontracts on its behalf. EMS is owned by Equitix.

Until 1 April 2020 BHL's subcontractor was Amey Local Government (Amey LG), owned by Amey plc. The 2019 settlement agreed Amey's exit from the project; BHL was formerly called Amey Birmingham Highways Ltd (ABHL). Amey LG is not shown in the structure because it is no longer in the project.



Appendix C

Response from Member Working Group



BIRMINGHAM CITY COUNCIL

Councillor Mike Leddy

The Council House

Victoria Square

Birmingham B1 1BB

Tel: 0121 303 2039

Email: mike.leddy@birmingham.gov.uk

7 April 2021

Councillor Waseem Zaffar

Cabinet Member for Transport and Environment

Dear Waseem,

Member Working Group – Highway Maintenance and Management PFI

I am writing to report back to you on the work of the informal Member Working Group for the Highway Maintenance and Management PFI contract.

You requested that the all-party group was set up in the Autumn of 2019. Our role was to act as a member sounding board for the development of proposals for the new contract.

I was pleased to be joined by Councillors Timothy Huxtable, Zafar Iqbal, Karen McCarthy and Paul Tilsley. My colleagues brought extensive understanding of the Highways service through their involvement in both Executive roles and as chairpersons and lead members on Overview and Scrutiny Committees. We were assisted by service managers from within Highways and Infrastructure. I would like to thank all for their positive contributions.

As members we had all been disappointed with the behaviour and performance of Amey and the poor condition in which they left our roads and pavements through their lack of investment. We were keen to understand how the issues that the council experienced can be taken forward within a new contract.

We have identified with officers the important issues for members and the citizens that we represent. We recognise that highway services are challenging to deliver and that some of these issues are complex. Many of these issues result from poor behaviour and do not have solutions that can be written into a contract. Our observations and findings to report back you are as follows:

1. Where the council has been let down by a poor provider it is important that the council has managed this contract well. We are beginning to stabilise delivery with an interim provider. We are looking forward to the future positively but are keen to ensure that we don't experience previous problems.
2. Continuing investment in our network is essential and we are pleased that you have recognised this priority. We have clearly learned from the approach to how investment is directed and are working to correct problems experienced. We acknowledge that there is still some way to go to improve our network but a promising start has been made.

3. We accept that things will go wrong occasionally with operational highway services and that the process of making changes is not an overnight solution. We ask that officers and our providers continue to learn from problems experienced and look to prevent them re-occurring.
4. The role of stewards with our services providers in liaising with the council's Local Engineers is important and provides for a responsive service to people. It is also important in identifying specific local solutions to problems that blight our streets such as damage to grass verges. I would also ask that you give consideration to asking a member to act as 'champion' for highway services delivery in the future to liaise on such issues.

With the support of officers, we identified what can be taken forward practically. Many of these points have already been responded to positively in the proposed future contract specification. I attach a summary of these issues for your reference. I am also sharing this with Councillor Liz Clements as the Chair of the Sustainability and Transport Overview and Scrutiny Committee, as this will be helpful in her role.

I trust you find our feedback helpful and I would like to thank you for the opportunity of chairing this group.

Yours sincerely

A handwritten signature in blue ink that reads "Mike L." with a stylized flourish at the end.

Councillor Mike Leddy

Chair – Member Working Group – Highway Maintenance and Management PFI

Appendix D

Exempt Appendix (D)