

STATES OF JERSEY

Future Hospital Review Panel

MONDAY, 13th NOVEMBER 2017

Panel:

Deputy S.M. Brée of St. Clement (Chairman)

Deputy R.J. Renouf of St. Ouen (Vice-Chairman)

Deputy T.A. McDonald of St. Saviour

Deputy J.A.N. Le Fondré of St. Lawrence

Deputy K.C. Lewis of St. Saviour

Senator S.C. Ferguson

Witnesses:

The Minister for Treasury and Resources

Director for Financial Planning and Performance

Director of Treasury Operations and Investments

Director, States Department for Infrastructure

[9:31]

Deputy S.M. Brée of St. Clement (Chairman):

Good morning, Minister, ladies and gentlemen. This is the second public hearing of the Future Hospital Review Panel where we are looking at P.107/2017, the Future Hospital: Approval of Preferred Scheme and Funding. As I said, this is a public hearing. Minister and witnesses, I will draw your attention to the notice in front of you explaining how the procedure works in a public hearing. Members of the public and press, if I could ask you to ensure that all mobiles and phones are set to silent, at least. If we can ensure the same, panel, just to make sure we are. All right. For the purposes of the tape we will go round and introduce ourselves. My name is Deputy Simon Brée, I am chairman of this panel.

Deputy R.J. Renouf of St. Ouen (Vice-Chairman):

Deputy Richard Renouf, vice-chairman of the panel.

Deputy T.A. McDonald of St. Saviour:

Deputy Terry McDonald, member of the panel.

Deputy J.A.N. Le Fondré of St. Lawrence:

Deputy John Le Fondré, member of the panel.

Deputy K.C. Lewis of St. Saviour:

Deputy Kevin Lewis, panel member.

Senator S.C. Ferguson:

Senator Sarah Ferguson, panel member.

The Minister for Treasury and Resources:

Senator Alan Maclean, Minister for Treasury and Resources:

Director for Financial Planning and Performance:

Alison Rogers, Director for Financial Planning and Performance.

Director of Treasury Operations and Investments:

Simon Hayward, Director of Treasury Operations and Investments.

Director, States Department for Infrastructure:

Ray Foster, Director of the States Department for Infrastructure.

Deputy S.M. Brée:

Thank you very much. Before we get on to the actual specific details of the proposition a question for you, Minister. In the public hearing last Friday, that is 10th November, we were advised that in drawing up the Outline Business Case and the whole basis of this proposition no health impact assessment had ever been done on the project. We were advised by your advisers that this is considered at the moment to be best practice in the U.K. (United Kingdom), will shortly be coming a legal requirement, but it just had not been bothered to be done on this project. As you are the Minister, who has lodged this proposition, are you content with the fact that the Project team in putting this together have not followed best practice?

The Minister for Treasury and Resources:

As far as I am aware, best practice has been followed by those involved in the overall project. The point you have raised, I will certainly look at and happy to give further consideration to you in due course.

Deputy S.M. Brée:

Sorry, Minister, I do not mean to press you on this but it was confirmed to us that no health impact assessment had been done. That is best practice in the U.K. and should have been extended to this project. For you to say that as far as you are concerned everybody has followed best practice is being somewhat incorrect in what you are saying. What I am asking is: are you satisfied, as the Minister for lodging this proposition, that everything contained within it you are happy as representing to the States, even though best practice has not been followed. A fact confirmed to us by the Minister for Infrastructure, the Minister for Health and Social Services and the advisers.

The Minister for Treasury and Resources:

I think what I was saying was as far as I am concerned in every aspect of the project best practice has been followed apart from the point you have just raised, and that is something I am prepared to have a look at and give you ...

Deputy S.M. Brée:

Were you aware that a health impact assessment had not been done?

The Minister for Treasury and Resources:

No.

Deputy S.M. Brée:

Yet you lodged this proposition hoping the States would debate it without even understanding that a health impact assessment (1) was required and (2) had not been done, is that not correct?

Deputy S.M. Brée:

I think, Chairman, what you are saying is that it is best practice in the U.K. As far as I was aware, I was not aware that one had not been done as far as this particular project in Jersey was concerned. I do not know, Ray, if you can add to that.

Director, States Department for Infrastructure:

Yes, Minister. I was also at the meeting on Friday and I think the panel in discussion over the need for a health impact assessment recognised that one is not required in Jersey. It is considered to be best practice, and I am not going to dispute the chair about best practice, and one is being currently undertaken.

Deputy S.M. Brée:

Exactly. We are aware one is being undertaken. I merely wanted to ascertain with the Minister who had lodged the proposition whether he was fully aware of the facts. If we now move on to look at the actual proposition in more detail itself. Now, Minister, your funding strategy involves issuing a bond of £275 million and funding the balance of the hospital budget from the Strategic Reserve. What is the rationale for proposing this particular blend of bond and Strategic Reserve funding?

The Minister for Treasury and Resources:

It is the same rationale as that which we previously presented, and that is simply to take into consideration what is a reasonable balance between borrowing and use of reserves to ensure we maintain our reserves at a sufficient level to ensure that they are there for the primary purpose of some form of crisis, whether that be economic or otherwise. We believe that to have used all of our reserves would have left the Island potentially in a compromised position in the case of an economic shock or something similar, which is what the Strategic Reserve's primary purpose is.

Deputy S.M. Brée:

So you are confirming that there is no essential difference between what you have lodged in P.107 and what you previously lodged as a funding proposal, which you then withdrew at the last minute? So there is no essential difference between the rationale and the structure?

The Minister for Treasury and Resources:

The rationale and the structure are principally the same as what was lodged previously.

Deputy S.M. Brée:

Okay. Now the proposition, in reading the report, states that your advisers and the Treasury Advisory Panel have recommended a higher level of borrowing. So why have you deemed it appropriate not to follow this advice?

The Minister for Treasury and Resources:

The Treasury Advisory Panel who advise in these matters, and have considered the work of the external advisers that were appointed, namely EY, and also as far as investment returns are concerned, Aon Hewitt. They, at the outset, were of the view that the maximum amount of borrowing should be undertaken and at that stage the proposal was to borrow up to £400 million. It was presented in that way at that initial stage because of the early stage in the project where there were a higher degree of uncertainties as time has passed and at the stage we were at, back in May, when we were almost to debate the project, the funding amount was capped at £275 million as there was

greater clarity about the exact amount that was going to be required and further work had been done looking at reserves and all aspects of the borrowing.

Deputy S.M. Brée:

The point I think I was trying to get to is that your advisers, and if I may quote from page 30 of P.107: “The advice the Minister for Treasury and Resources has received from expert advisers and from the Treasury Advisory Panel suggests a preference for a higher level of borrowing than this funding strategy proposes.” Now I merely ask the question: why did you go against the advice you have received?

The Minister for Treasury and Resources:

I took into consideration other factors and that was the level of borrowing, concerns about the level of borrowing that was necessary. We have obviously had improved returns over the last period, certainly the outturn from 2016 was significantly better than anticipated, and taking that into consideration I have always stated that a blend was the preferred option. The blend originally would have accounted for around about £66 million of reserves but of course the reserves are in far better condition now than they were at the time that was originally contemplated. So taking into consideration the view that the level of borrowing should be kept as low as possible we looked at the fact that an issuance below £250 million was going to be less preferable from a market dynamic perspective. The ability to borrow sums below that causes other issues, which I am sure we will touch on. Therefore the range of borrowing between £250 million and £275 million and hence the wording “up to £275 million” is the preferred level of borrowing and that kept the level of debt down to a more manageable level, from my point of view.

Deputy S.M. Brée:

We cover the specifics of the proposed bond issue a little bit later on. I was merely trying to ascertain the rationale and the decision-making process that you would have gone through to go against the advice of 2 sets of advisers.

Deputy J.A.N. Le Fondré:

Just a question, Minister, in terms of what you said. You referred during your response to the first question, I think it was, that you did not think it was appropriate to use all of our reserves on the project and you did use the expression “all of our reserves”. Now the reserves, as I understand it, are in the order of £800 million and the project is stretched over a number of years, in fact we “only” use £160 million in the first 3 years of the project, according to your cash flows, in 2018, 2019 and 2020. So when was there ever a risk that we were going to use all of our reserves on this project?

The Minister for Treasury and Resources:

I can correct that point. It was a large proportion of reserves as opposed to a lesser proportion of reserves. I was not being specific to suggest that all of the Strategic Reserve would be used, because clearly it would not have been, so I am happy to clarify that.

Deputy J.A.N. Le Fondré:

So would it be fair to say “a larger proportion” versus “a smaller proportion”?

The Minister for Treasury and Resources:

That would be a more accurate way of describing it.

Deputy J.A.N. Le Fondré:

Thank you, Minister.

Deputy K.C. Lewis:

Minister, the Corporate Services Scrutiny Panel advisers earlier this year drew attention to the need to review the investment strategy for the Strategic Reserve to align it with the bond requirements. This is because the funding realised on the Strategic Reserve returns being above the coupon rate. Initial indications are that our advisers still have the same concerns. What are doing to ensure the 2 are aligned?

Director for Financial Planning and Performance:

Our investment advisers are Aon Hewitt, so if we get a decision in December ... I think we have sent through to Scrutiny Officers the investment strategy as it is, but we would be talking to Aon Hewitt about whether a change to that strategy might help. So we accept that there is a cost of carry element which is the other thing that I think Opus talked about would be limited but agreed we would talk to Aon Hewitt about a new strategy if it would be advisable.

[9:45]

Deputy K.C. Lewis:

Just to clarify that: will you need to invest in less risky assets in the Strategic Reserve, thereby reducing the return?

Director for Financial Planning and Performance:

Not necessarily. As I say, we would look to our external advisers. We have a relatively heavy allocation to equities but we have had that for some time and we have been busy diversifying out of equities to try to alleviate that issue without the hospital funding come from the Strategic Reserve. So it is something that is actively being looked at anyway.

Deputy J.A.N. Le Fondré:

Just a quick question. You refer to the cost of carry and it is up to £275 million as the figure. What is the cost of carry for the bond?

Director for Financial Planning and Performance:

We have a cash flow at the moment from the Department for Infrastructure but obviously it depends on how quickly they go out to market and get tied up into a contract to know exactly when that cash flow might settle. At that point we would certainly be looking at how quickly the money will be going out of the project and then we will have a better idea in terms of what that cost of carry might be.

Deputy J.A.N. Le Fondré:

For example, Andium is around £6 million a year, I think, at the moment, is it not?

Director for Financial Planning and Performance:

So in terms of the interest charge, so in terms of the coupon, at the moment it would be about £7 million, £7.2 million, I think, for the £275 million.

Senator S.C. Ferguson:

How will you ensure that your investment strategy generates enough returns to meet the coupon payment each year?

The Minister for Treasury and Resources:

The oversight for the investment strategy is managed by the Treasury Advisory Panel. The advice has been based on some historic data, going back over the last 40 years back to 1986, looking at average returns during that period. The average has turned out to be 4 per cent. That is over R.P.I.(Y) (retail price index excluding indirect tax and mortgages). We have then taken advice from the investment advisers. Aon Hewitt have been involved in the process as well, looking forward in doing a much more conservative projection as to what likely returns would be and on that basis in the changing investment environment those are estimated at 2 per cent of R.P.I.(Y). and as such very much more conservative than historic data. Indeed, we can look at just the last year or 2 where substantially higher returns have been achieved in the short term but clearly we are very conscious of focusing on the long term, which is why we focused back over the last 40 years, which shows that there have been peaks and troughs clearly. But the average of 4 per cent above R.P.I.(Y). and looking forward we are working on 2 per cent, which is half the historic average over the last 40 years, which we believe is a sensible, prudent and conservative way of approaching the modelling. I should caveat all of that by saying it will be short term peaks and troughs. It will be very helpful if we did not have a trough in the early 2 years but that is clearly impossible with investment markets

and we have seen exceptional returns over the last year or 2. No doubt there will be a trough coming at some point.

Senator S.C. Ferguson:

You will be reviewing the strategy how frequently?

The Minister for Treasury and Resources:

The strategy gets reviewed on a regular basis. It is reviewed in year, not that one expects significant changes to occur, particularly in year, but it is fully and actively managed.

Senator S.C. Ferguson:

So you will only be reviewing it once a year?

Director for Financial Planning and Performance:

No, the Treasury Advisory Panel meets quarterly so at the very least they would be meeting quarterly. I think if we thought that markets were moving in a direction that might put the strategy at risk or if there were other matters. Brexit of course is something that the markets are very aware of and the impact of that is unknown as yet, so we already talk to the Treasury Advisory Panel outside of those quarterly meetings and we would absolutely be talking to them if we thought there was some sort of shock on its way.

Senator S.C. Ferguson:

Yes, I am sorry, can you remind me who comprises the Treasury Advisory Panel?

Director for Financial Planning and Performance:

So we have a chair, who is an independent, which is ...

Director of Treasury Operations and Investments:

The chair of the panel is Philip Taylor, ex senior partner at PwC. The 2 independent members are a gentleman called Paul Dentskevich who predominantly has a risk background. He is currently the risk director at Crestbridge locally. And we have Gordon Pollock who is an actuary by background and is the chair of the Public Employees' Pension Fund and the Treasurer of the States is the final member of the panel.

Deputy S.M. Brée:

I would like to go on now and talk about or ask questions about the specifics of the bond issue. We are obviously seeking a bit of clarity here or a bit further understanding of exactly what is being proposed. Now the proposition refers to an estimated price of the bond at between 2.64 per cent to

2.74 per cent. It also then refers to a coupon rate of 2.625 per cent. Can you explain what this will mean in practice in terms of the actual amount of funds raised from the issue and then the actual rate of interest, i.e. the coupon, paid to bondholders? What are the details that you are looking at, at the moment?

Director for Financial Planning and Performance:

As you would expect, we have been refreshing the numbers on an ongoing basis so that we are aware of any changes that might be significant. The bond coupon is discounted to the nearest eighth. That is what the market does so that bonds can be compared across different organisations.

Deputy S.M. Brée:

Sorry, you are saying the bond coupon is discounted?

Director for Financial Planning and Performance:

Sorry, the amount that we receive is discounted.

Deputy S.M. Brée:

So it is not the coupon being discounted, the price of the bond shows either a discount or a premium below or above the coupon rate of the issue?

Director for Financial Planning and Performance:

Yes. Sorry, what I am trying to say is that the bonds all have a price that are the same across the board, so that there is comparability across organisations. So where your price of your bond might land is not necessarily the coupon rate.

Deputy S.M. Brée:

No, I am aware of that because you will be issuing the bond at probably a discount. That is what we are trying to establish.

Director for Financial Planning and Performance:

Within the report we recognise that and suggest hopefully on a fairly pragmatic approach is that £275 million might give us £265 million in terms of cash.

Deputy S.M. Brée:

Just to confirm, and this is where we are just seeking clarity, you would be looking to issue £275 million worth of bonds at what coupon rate? Because the coupon rate affects your future cash flows and projections. I was just asking: what is the coupon rate that you are currently looking at issuing the bond at? It is not the price, the coupon.

Director of Treasury Operations and Investments:

2.625 per cent.

Deputy S.M. Brée:

Right. Are you perfectly sure that a quasi-Government bond such as this can be issued in eighths and not quarters?

Director of Treasury Operations and Investments:

Our advisers have told us that it will be rounded down to the nearest eighth.

Deputy S.M. Brée:

Okay, so your advisers are telling you it is an eighth. Okay, so you are looking at issuing a bond of £275 million face value, at a coupon rate of 2.625 per cent. You are going to have to discount the price of the bond to raise, you believe, is it correct, £265 million?

Director for Financial Planning and Performance:

We have used that in our planning. Our advice is we might get a bit more than that but we wanted to use a number for planning purposes and £265 million was deemed to be ... it would be no worse than £265 million.

Deputy S.M. Brée:

How has the recent change in base rates affected the coupon rates that your advisers are telling you you would have to affix to such an issue?

Director of Treasury Operations and Investments:

So it has had very little change because it had been signalled well by the M.P.C. (Monetary Policy Committee), and the underlying gilt markets have responded accordingly in advance of the change. So as we have been pricing the bond over the last few months against the underlying gilt rate that has already risen to reflect the change in the market conditions. So we have seen ...

Deputy S.M. Brée:

Because obviously this proposition was lodged on 31st October, which was prior to the base rate increase. So you are saying there has been very little, if any, impact on the coupon rates of similar bonds?

The Minister for Treasury and Resources:

Largely because it has been signalled ...

Deputy S.M. Brée:

So the market had already discounted the base rate, that is what you are saying?

Director of Treasury Operations and Investments:

Yes, over the previous couple of months.

Deputy S.M. Brée:

With regards to coupons and pricing, how has or what impact has effectively the 6-month delay caused since you withdrew the funding proposal earlier this year, which you have already admitted was virtually exactly the same. So what impact has that had on the coupon rate and the price that you are being told by your advisers you will need to issue the bond now?

The Minister for Treasury and Resources:

It is quite interesting because the point I was making at the time, and in fact earlier in the year when this was first presented, was my concern about volatility and that is exactly what we have seen over the period of time. There has been quite a lot of volatility with a fair movement in the rates and the margins. Ironically, where we sit now, we are more or less where we were at the beginning of the year. So although it has fluctuated by about 40 basis points fluctuation over that period of time but we are currently back to more or less where we were at the beginning of the year.

Deputy S.M. Brée:

So what you are saying is that your decision to delay the funding proposal, and therefore delay any issuance of a bond or anything else, has not had any cost impact on the Island whatsoever?

The Minister for Treasury and Resources:

Well, I think to be fair, once this decision is taken and if the States had taken the decision back in May, then of course we would have moved through the bond issuance process. As you know that would have taken several months in order to undertake. It is possible that a strike rate at that time may have been slightly lower than it currently is now but I think it would have been fairly marginal, is probably a fair way of describing it. So we do not think there was or has been to date a significant difference despite the fluctuations that have occurred over the course of the year as a whole.

Deputy S.M. Brée:

But potentially then, if you are talking about volatility, if you get this proposal approved by the States and then you go out to issue the bond, you potentially stand the risk of being affected by further market volatility, is that correct? That is what you are trying to say.

The Minister for Treasury and Resources:

What I am trying to say now and what I said previously, and was the substance of my concerns at the time, was that we needed to proceed because of the extraordinary levels of volatility that we are seeing, the environment that we are currently living in at the moment, and we have seen that over the last 9 months or so.

Deputy S.M. Brée:

In the previous funding proposal that you put forward, Minister, you talked about hedging a certain amount of the issue. Now that was when the issue was potentially going to be a much higher level. I cannot see, although I may have missed it, any proposals within the new proposition relating to hedging. Could you explain why?

The Minister for Treasury and Resources:

We will take advice on whether to hedge or not on the assumption that a decision is taken after that particular point. As I have said, it can be over 2 months but I think in the report it does still refer to hedging.

Director of Treasury Operations and Investments:

On page 5 in the executive summary there is a repetition of the Treasury Advisory Panel's advice from April, which did include a point that once the Assembly has confirmed that a bond will be issued a hedging arrangement should be implemented. That advice still stands today.

Deputy S.M. Brée:

That is what you would do should this proposition be successful? You would still intend to take advice on hedging?

The Minister for Treasury and Resources:

We would still intend to take advice on hedging and the rationale behind that would be one which has been consistent throughout, and that is around certainty. In fact that is at the very heart of the proposal to issue a public rated sterling bond.

Deputy S.M. Brée:

This time you would be willing to follow the advice of your advisers?

The Minister for Treasury and Resources:

Ministers always take note of advice from advisers. Sometimes Ministers have to take a view on these matters but, as I have said, we would certainly be taking advice in this regard.

Deputy S.M. Brée:

Have you or did you consider using the Strategic Reserve initially and only issuing a bond when the money that will be required for the project has further clarity on the actual amount required?

[10:00]

Rather than issuing the bond in the first instance and then topping up from the Strategic Reserve?

The Minister for Treasury and Resources:

It refers to my point on certainty and also my earlier comments about volatility. We were pretty clear the market was likely to be volatile, which it has proven to be, and there are also concerns about the cost of borrowing rising, which again it could do. Of course a certain amount of money has already been apportioned to the project, £23.6 million, to allow it to progress to the point that it has now, and that funding is still available and will be in place and has not been exhausted through into the early part of next year. However, to delay before issuing a bond further just increases the level of risk and that is why I do not believe that to be appropriate.

Deputy S.M. Brée:

But however you did believe that to be appropriate when you withdrew your previous funding proposition, which was exactly the same as this one.

The Minister for Treasury and Resources:

I think I made the point at the time as to the fact that I believed that that was the appropriate funding mechanism. It was the view of Treasury that that was appropriate funding and, as it happens, although other options are being considered in the intervening period, and have been reviewed by advisers, and in particular the Treasury Advisory Panel, the conclusion of that work and review is that what we were proposing back in May is still the most appropriate source of funding.

Deputy S.M. Brée:

So we go back to this question then, Minister, that I think certainly this panel, and probably many States Members and members of the public, are still very confused as to the reasoning behind why you withdrew your original funding proposition when effectively you are telling us today you still stand by it, the Treasury Department still stand by it, your advisers still stand by it as being the most flexible and cost-effective solution for providing the level of funding you need and yet you withdrew it. Could you explain? Because you do talk about in the proposition other options being reviewed but I think there is still confusion that still we seek clarity. Why did you pull your other proposition when this one is virtually identical?

The Minister for Treasury and Resources:

A number of other options in the intervening period have been looked at and I think I made the point at the time that for the single largest capital project that the States would have undertaken it is, in my view, important that you get as close to a unanimous view on this as you can possibly achieve and that was not the case in May this year. So I took the view that, together with colleagues on the Council of Ministers, it was appropriate to withdraw and to consider some of the other options in more detail. But more importantly as well to also bring back other areas which have been a matter of concern for some States Members and that was around improving or developing, more to the point, the budget and the Outline Business Case and bringing it all back as one package, which is indeed what is going to happen.

Deputy S.M. Brée:

You used the word “unanimous”.

The Minister for Treasury and Resources:

Almost. As near as possible.

Deputy S.M. Brée:

Among who?

The Minister for Treasury and Resources:

It was important that there was a full agreement within the Council of Ministers about the funding proposal. There were other views being expressed by some other Members as well and I thought it was important that there was a greater understanding of the proposal. It was clear that there were one or 2 individuals who were not comfortable with what was being proposed and that was at the heart ...

Deputy S.M. Brée:

If I may ask: your original proposition ... sorry, it is trying to seek clarity here and to understand the process. Your original proposition that you lodged and then withdrew, are you saying that proposition did not have the unanimous support in the Council of Ministers?

The Minister for Treasury and Resources:

It is not unusual not to have unanimous support on matters to go to the Council of Ministers. That is the whole purpose.

Deputy S.M. Brée:

But you believed it to be the best funding solution and the best solution for the Island at that time?

The Minister for Treasury and Resources:

I and Treasury believed that to be the case or we would not have put that forward. We still believe it to be the case and have done in the intervening period but we have also taken the time to look at some other proposals that were being suggested and we have pushed those in front of our advisers and the Treasury Advisory Panel has reviewed them and the conclusion ...

Deputy S.M. Brée:

So who was suggesting these other options?

The Minister for Treasury and Resources:

The conclusions of all of that is what is before you.

Deputy S.M. Brée:

Sorry, who was suggesting these other options because surely any funding required by the Island, particularly for such a large capital project, is the responsibility of the Treasury Department to look at, investigate and put forward an option? You, as Minister for Treasury and Resources, then effectively lodged a proposition outlining that, so who put forward other options if it was not from within the Treasury Department?

The Minister for Treasury and Resources:

There have been, not surprisingly, a number of other suggestions put forward by individuals who have extensive experience ...

Deputy S.M. Brée:

Sorry, I need to clarify here, individuals who are not States Members or who are not Ministers?

The Minister for Treasury and Resources:

There are individuals who have experience within this particular field ...

Deputy S.M. Brée:

So these individuals are not currently States Members and not currently Ministers?

The Minister for Treasury and Resources:

Chairman, if I may, can I complete what I am going to say and then you can question me after that if you do not mind? There are individuals who have extensive experience within this area of financing who have put forward, via representatives within the States Assembly and Ministers,

options for funding of the hospital and I believed it was incumbent upon us to look in some additional detail at what those proposals were and that has been undertaken.

Deputy S.M. Brée:

So which Ministers or States Members put forward these propositions to you to look at? Who was it?

The Minister for Treasury and Resources:

I am not prepared to go into details. Quite simply there are discussions within the Council of Ministers, not just on this issue but on a number of issues, and healthy debate is absolutely appropriate before arriving at an agreement. In the majority of cases it would be the majority and then a position would be taken which would be cemented with collective responsibility. I do not believe, or did not believe, in this particular case, being the largest capital project the Island will undertake, that there should be any concerns still being raised by Ministers or others and that is why we took the decision to withdraw and it is not just about the funding, as I said a moment ago. It is also about bringing greater clarity to the budget by bringing greater clarity by developing the O.B.C. (Outline Business Case) and I think that ... or the States will be much better informed when this is debated in December than would have been the case, perhaps, in May earlier this year. But, as Minister for Treasury and Resources, my concern at that point was volatility in market and the likely outcome of the cost of borrowing rising.

Deputy S.M. Brée:

So you are not prepared to say who brought forward propositions from individuals, as you call them, from outside the Treasury Department and yet at the time you obviously had concerns about the impact of the market volatility on the cost of issuing a bond, similar to the one you are now proposing. Would you say, Minister, that you have in fact been extremely lucky that market volatility has not affected the cost greater than it has?

The Minister for Treasury and Resources:

I think "we" have been probably fortunate. It is impossible to forecast, with any degree of certainty, what will happen in the future. It is about certainty that is at the very heart of the proposal that we put forward in May and it remains the proposal we are putting forward now, which is certainty over the period of the life of the hospital. The life of the hospital is a bit longer than the bond issuance, which will be 30 or 40 years, but 30 or 40 years at a historically low rate of borrowing fixed with a mechanism to repay ...

Deputy S.M. Brée:

Well, it is no longer historically low, is it? It has just gone up.

The Minister for Treasury and Resources:

Okay. Well, around historically low levels of borrowing. It, nevertheless, is a low rate that can be fixed for the term, 30 or 40 years ...

Deputy S.M. Brée:

We are not questioning that side of things at this moment in time. We are trying to seek clarity on why the original proposal was withdrawn as there seems to be little, if any, difference between what you have now lodged. At the time ...

The Minister for Treasury and Resources:

But there could have been, Chairman. That is, I guess, the point from some people's perspective. There are, and you will appreciate with your background, the point here; that there are a number of ways in which a capital project of this nature could be funded and so ...

Deputy S.M. Brée:

Well, that was the question I was asking, that at the time there was talk of a short-term funding option being looked at and yet that does not seem to be one of the options that is mentioned in the proposal or the report.

The Minister for Treasury and Resources:

I think it is.

Deputy S.M. Brée:

Well, this is where, perhaps, you can point us towards the short-term funding model.

The Minister for Treasury and Resources:

I think the reference to "asset backed commercial paper", which is typically used by banks or corporates was the particular option that was one of those that was given some consideration in the intervening period since May.

Deputy J.A.N. Le Fondré:

Could the Minister identify where?

Deputy S.M. Brée:

I was going to say, if you could point in the right direction.

Director for Financial Planning and Performance:

Page 36.

Deputy S.M. Brée:

Page 36, thank you. Again, the purpose of the public hearing is to try and expand and seek clarity on things.

The Minister for Treasury and Resources:

Yes, sure. I have no problem.

Deputy S.M. Brée:

Asset backed commercial paper. Asset backed commercial paper, as you say, is not something that would be suited to this sort of project at all. It is purely designed to manage short-term liquidity issues by large corporates. I would be concerned if you had looked at that as a serious alternative, let us put it that way. I am hoping you will tell me you discounted it quite quickly.

The Minister for Treasury and Resources:

Yes, but it was still looked at and I suppose you need to tie into it a view, if you have such a view, of a macroeconomic view, perhaps, about the future pressures, inflationary versus deflationary, and indeed the future long-term potential for rates to remain low for a number of those reasons and that was at the heart, I think, of that particular proposal.

Deputy S.M. Brée:

Okay. Moving on slightly. As we have understood the proposition, the monies received from the issuance of the bond will initially be held in the Strategic Reserve and then transferred to the hospital construction fund. We have areas on the hospital construction fund we want to talk about a little later on but will the proceeds from the bond be invested on the same risk profile as the other money sitting in the Strategic Reserve?

The Minister for Treasury and Resources:

No, is the short answer. I do not know. Do you want to pick that up?

Director of Treasury Operations and Investments:

I think that was touched on earlier when we talked about ongoing review of the investment strategy of the Strategic Reserve. So the Treasury Advisory Panel, which met last Friday, has a standing agenda item that once a decision has been made about issuance of a bond and proceeds being received for investment they will reconsider the investment strategy for the Strategic Reserve.

Deputy S.M. Brée:

Yes, but I am talking about the capital risk to the bond receipt if you invest it as a sum into the overall investment strategy of the Strategic Reserve Fund. What we are trying to say is: are you going to put any procedures in place to ensure that the funds raised from the bond issuance, while sitting within the Strategic Reserve Fund, are effectively ring-fenced with a completely different investment strategy so as to avoid any risk to their capital and how are you going to do that?

The Minister for Treasury and Resources:

Chairman, you will never get a scenario where you have no risk clearly but the investment strategy for the funds to be deployed for the hospital project ...

Deputy S.M. Brée:

Well, you can have no risk if you put it on deposit with a AAA rated bank but I am sure your investment director here will explain that to you if you do not understand that principle.

The Minister for Treasury and Resources:

I do not think, Chairman, it is necessary to be condescending in that way.

Deputy S.M. Brée:

I am not but there is a situation where you can get no risk.

The Minister for Treasury and Resources:

I do not believe there is ever a situation where you get absolutely no risk but that is another ...

Deputy S.M. Brée:

Well, many an investment adviser would disagree with you then.

The Minister for Treasury and Resources:

Yes, and that could be a long discussion, I am sure.

[10:15]

In any event, the strategy for the funds for the hospital project will not be at the same level from a risk profile as they would be for, for example, the Social Security Reserve Fund, which is very much long-term or the Strategic Reserve which is longer term because this money is going to be needed over the short term horizon up to a maximum of 8 years. In fact it is less than 8 years if you look at the spend profile where the maximum is required.

Deputy S.M. Brée:

So have you worked on any form of investment profile or risk profile or investment strategy for the proceeds of the bond should the States approve this proposition, i.e. have you already looked at that and said: "Right, we know exactly what sort of yields we will be able to achieve if we receive the money"?

The Minister for Treasury and Resources:

That is a matter that the Treasury Advisory Panel will opine upon at the time when the decision has been taken but there has been some clear advice and experience, if I can put it that way, around the housing bonds. So we have seen and we have touched ... I think Senator Ferguson was referring to ...

Deputy S.M. Brée:

We are not talking about the housing bond here. We are talking specifically about the money received from this as to whether or not you can advise us of the sort of work that you have done, number one, and there is, (2) the sort of yields that you might look to receive on the money sitting in the Strategic Reserve specifically relating to the issuance of the bond because it goes to the previous question asked by Deputy Le Fondré about cost of carry.

The Minister for Treasury and Resources:

The assumed rate, because it is going to be a long and very conservative route, as I have just outlined, is 1 per cent. But I think, Alison, you might be able to expand on that.

Director for Financial Planning and Performance:

Yes. So what we will do is make sure that the strategy for the Strategic Reserve is clear in terms of the proceeds coming into it. We do this similarly with the Consolidated Fund in terms of looking at the element of it that you might want to invest and the element of it that you might want in cash or cash equivalent. So we will have a base ... we have already got a set-up for the Consolidated Fund on that basis so we will replicate that for the Strategic Reserve.

Deputy S.M. Brée:

Sorry, Sarah, did you want to ask ...

Senator S.C. Ferguson:

Is it the Long Term Investment Fund? Is that the only one where you run this umbrella fund structure?

Director of Treasury Operations and Investments:

The Common Investment Fund? The pooling arrangement across many of the ... so a number of funds invest through the Common Investment Fund, one of which is the Strategic Reserve.

Senator S.C. Ferguson:

Yes. So that, in effect, you would just be creating another class in the Common Investment Fund.

Director for Financial Planning and Performance:

It will access classes that already exist in the Common Investment Fund, yes. So we already have a set-up there for it to get an element of that.

Senator S.C. Ferguson:

Right, which I think is an answer to your question, is it not? Presumably this is a class which is very low risk, cash and near cash.

Director for Financial Planning and Performance:

Yes.

Director of Treasury Operations and Investments:

Yes. There is a number of asset classes that have capital preservation at their heart and that would be where you would expect these funds to be invested.

Deputy S.M. Brée:

Okay. No, it was just to understand the process and how you were looking at managing that area.

Okay. Do we have any other specific questions about the bond before we move on?

Senator S.C. Ferguson:

Yes, please. It is a very simple one. You were talking about raising £265 million. What is the face value of the bond that you were listing to get that?

Director for Financial Planning and Performance:

So our aim is a £275 million bond.

Senator S.C. Ferguson:

So that £10 million difference is cost and discount? There will be fees to the issuer.

Director for Financial Planning and Performance:

I think the fees will be paid by the Strategic Reserve. The difference between the £275 million or £265 million is just the discounting.

Director of Treasury Operations and Investments:

Also book runner fees.

Senator S.C. Ferguson:

So your fees are on top of that? So you are saying we are going to issue bonds at a face value of £275 million, we are only going to get £265 million, so we have got a £10 million discount and on top of that we are going to have £5 million, £6 million, £7 million in fees.

The Minister for Treasury and Resources:

No, the fees are not at that level. The fees are around about ... well, estimated at £1.25 million, £1.5 million.

Director for Financial Planning and Performance:

The £265 million is a prudent number so that on the latest numbers that we have had ...

Deputy S.M. Brée:

I think the question we are trying to ask is, if you issue bonds with a face value of £275 million what will be your estimated net proceeds after discounting and all fees or commission?

Director of Treasury Operations and Investments:

Okay. Well, that is down to the mathematics of the market on the day you issue.

Deputy S.M. Brée:

However, you will have a very good estimate at the moment.

Director of Treasury Operations and Investments:

We do, which will depend on the differential between the yield and the bond coupon. I think the case that Alison was making is that the worst ... the largest element of discount will be approximately £10 million and that includes book runner fees over and above that. As the Minister has just alluded to, other fees would be in the region of about £1 million but they would not be discounted from the amount you received for the bond. They would be paid for separately.

Deputy S.M. Brée:

Yes, but I said "the net proceeds" from the issuance, right? We understand the discounting banding which, as you say, can - not always - but can include book runner fees. You then have lead manager fees and commission on top of that which you are estimating is £1.5 million. At the moment that is

what you are giving an indication of. Obviously, I appreciate you have to rely on the information received. So the net proceeds available for investment in the Future Hospital is, say, £263 million?

Director of Treasury Operations and Investments:

Yes, although I understand the million ...

Deputy S.M. Brée:

Not the £265 million.

The Minister for Treasury and Resources:

Well, £265 million was quite a reasonably conservative discounted number. The additional costs that we have referred to would be taken not directly from the bond money.

Deputy S.M. Brée:

No. We are talking about the amount of money that will be available because even if the Strategic Reserve were to pay, out of its own pocket, if you want to call it that, any additional fees and commission that may be included on top of the £10 million. It is still saying that bond issue raised as net proceeds, which to most people would go: "Right, that is what we have now to build the hospital with." Part of the package. Sorry, John, do you want to pick up on ...

Deputy J.A.N. Le Fondré:

Well, it is a minor ... I have got some other questions coming but I have got an exception so I will add them on to the beginning of my section. But as a slightly detailed point, page 79 identifies the bond issue costs of £2.5 million not £1.5 million or is that the book runner fees as well? I know that you have just said £1.5 million to us. Your documentation said £2.5 million.

Director for Financial Planning and Performance:

That will be book runner and all fees.

Deputy J.A.N. Le Fondré:

Okay. So the total fees are £2.5 million?

Director for Financial Planning and Performance:

Up to, yes. Again, it is an estimate.

Deputy J.A.N. Le Fondré:

In your figures. But are you saying that some of that money is already included in the conservative £10 million?

Director for Financial Planning and Performance:

Yes.

Deputy J.A.N. Le Fondré:

Right.

Deputy S.M. Brée:

All right. Any other questions on the bond issue itself?

The Deputy of St. Ouen:

Yes. What authority is there to allow the Strategic Reserve to be used to pay these fees?

The Minister for Treasury and Resources:

Well, the authority is contained within the proposition, I think, is it not?

Director for Financial Planning and Performance:

So the principle is part of this proposition, we have a change to the Public Finances Law which we were hoping to lodge alongside this but it was slightly behind this which will allow those changes to be made so that those sums of money can be paid because, as you are aware, the Strategic Reserve currently cannot pay for anything directly so there are changes to the Public Finances Law being looked at, being lodged to do that.

Deputy S.M. Brée:

When will those be lodged?

Director for Financial Planning and Performance:

I thought they were already lodged. If they are not then it is as soon as possible. I thought they were already lodged.

Deputy S.M. Brée:

Have they? Can you confirm, Minister, that they have been lodged or ...

The Minister for Treasury and Resources:

I believe they have been lodged but we will confirm it back to you.

Director for Financial Planning and Performance:

We will confirm if it has not been lodged exactly when ...

Deputy S.M. Brée:

Sorry, these are propositions lodged by the Minister for Treasury and Resources?

The Minister for Treasury and Resources:

Yes. I am not sure whether it has come out the other end of the process so they have become visible yet.

Director for Financial Planning and Performance:

It is certainly with the Greffier.

Deputy S.M. Brée:

Okay.

The Deputy of St. Ouen:

Well, are the fees, whether they are £1.5 million or £2.5 million, are they going to be accounted for in the total costs of this project or is it going to be a separate accounting within the Strategic Reserve expenditure?

The Minister for Treasury and Resources:

It will be contained within the whole.

The Deputy of St. Ouen:

In the whole of what?

Director for Financial Planning and Performance:

It will be part of the construction of the hospital, the whole of the cost.

Deputy J.A.N. Le Fondré:

Over to me? Minister, I am just picking up on a couple of points you raised under this last section. Minister, you were saying that the difficulties of trying to get a unanimous view from the Council of Ministers but you said that often you have to go with a majority view. Can you remind me, how many members from the Council of Ministers?

The Minister for Treasury and Resources:

Eleven.

Deputy J.A.N. Le Fondré:

If it was one or 2 people that you were discussing that were disagreeing with the scheme?

The Minister for Treasury and Resources:

I think I was making the point of the importance with a capital project of this nature that you obtain as close to a unanimous view as possible. In many cases that is not going to be case with the other matters that are discussed. Not all Ministers are going to agree with absolutely every proposal that is brought forward. In this case I thought it was particularly important and specifically, where some alternatives were still to be suggested, we felt it appropriate to do that additional piece of work but it was not that alone. As I said a moment ago, it was also the fact that giving greater certainty to States Members, which we will now have for the debate in December with the development of the O.B.C. and obviously the improved work on the budget.

Deputy J.A.N. Le Fondré:

We will get to the greater certainty in a minute, Minister. I know you declined to identify the individual Ministers who were raising concerns but it is my very clear recollection from various hearings around that time that one of the principal people raising concerns over the funding was the Chief Minister. Can you confirm that was the case?

The Minister for Treasury and Resources:

I said a moment ago I was not going to discuss individuals.

Deputy J.A.N. Le Fondré:

That is on record in a hearing we had with the Chief Minister. I just wanted to raise that.

The Minister for Treasury and Resources:

If you have something on record that is a matter for you. I am not prepared to make any further comments outside of what I have already said.

Deputy J.A.N. Le Fondré:

Okay. So the question, I suppose, is that you made the point that one or 2 individuals, who you are not prepared to identify, raised the concerns. Does that mean anyone who comes along with a bright idea can halt a project?

The Minister for Treasury and Resources:

I think, Deputy, you would be well aware of the ability for individuals to influence government policy of the future by raising, in a constructive way, their views on particular matters. I think it is incumbent upon Ministers and it is incumbent on the Council of Ministers to give due and fair consideration where it is warranted to matters that are raised. As I have said all the way, there have been a

number of concerns raised about (a) the level of borrowing for this particular project, the amount of debt the Island was seeking to take on in order to fund it and indeed the method of raising that particular debt. Time has passed. The professional external advisers and the Treasury Advisory Panel have reviewed those particular options and we sit here today with a similar proposal to the one we were going to present in May, but I think the fact it has had additional scrutiny is a good thing from an Island perspective, particularly as it does not appear to have cost us any great additional money.

Deputy J.A.N. Le Fondré:

That leads me very nicely to my last question before I get on to the main area I shall be questioning you on. The difference in the change in rates was defined as being fairly marginal. I just wonder if you could put a number on that please. What was the rate in May and what did it drop down to in June or July?

Director for Financial Planning and Performance:

I do not have those numbers with me.

Deputy J.A.N. Le Fondré:

Could you send them through to us please?

Director for Financial Planning and Performance:

Absolutely. No problem.

Deputy J.A.N. Le Fondré:

Okay. Therefore, it will go to the public?

Director for Financial Planning and Performance:

Yes.

Deputy J.A.N. Le Fondré:

Okay, good. Right. Anybody else want to ask ...

Deputy S.M. Brée:

Carry on.

Deputy J.A.N. Le Fondré:

Okay. Minister, the proposition itself asked the States Assembly to give approval to the preferred scheme, i.e. a new build on part of the current site and a new build at Westaway Court. Are you able to describe clearly and concisely what facilities the new hospital will provide?

Director, States Department for Infrastructure:

They are outlined in the O.B.C. Do you want me to read out every aspect of the hospital?

Deputy J.A.N. Le Fondré:

Well, I think what I will do ...

Director, States Department for Infrastructure:

Or clarify the difference between what is in Westaway Court and what is within the existing hospital?

Deputy J.A.N. Le Fondré:

What I will do ... can you just ... I will come back to your comment in a second.

[10:30]

What existing facilities are not presently included in product cost? In other words, what the hospital does not provide and is not there in the new hospital at present in terms of what has gone to the planning and what is costed in here?

Director, States Department for Infrastructure:

I would need to refresh my memory on that but there will be elements, some will be in terms of size and nature and activity and there will be some specific individual aspects that are not planned currently into the new hospital.

Deputy J.A.N. Le Fondré:

Okay. The question one comes to, using this, because this, P.107, is what States Members have had access to. I do not believe States Members have got access to the O.B.C. as a whole.

Director, States Department for Infrastructure:

It is attached to the P.107.

Deputy J.A.N. Le Fondré:

Sorry, I meant all the appendices and ...

Director, States Department for Infrastructure:

The appendices are also there and the paperwork.

Deputy J.A.N. Le Fondré:

Could you just hold up the number of files that we have got in here? As I understood it was about that amount of documentation.

Director, States Department for Infrastructure:

I have not got the files with me.

Deputy J.A.N. Le Fondré:

So the O.B.C., all of it, is readily available to States Members online now? Okay. They are current. Right. Sorry, I had not appreciated that because I understood we were required to sign confidentiality agreements when we received them.

Director, States Department for Infrastructure:

There are links to all bar 2, which have got appendices which are commercially confidential.

Deputy J.A.N. Le Fondré:

Okay. So the States Members do not have access to the O.B.C.?

Director, States Department for Infrastructure:

They are able to have access to the O.B.C.

Deputy J.A.N. Le Fondré:

As of today if they were to go online they do not have access to the latest O.B.C.?

Director, States Department for Infrastructure:

There are 2 appendices which are marked as commercially confidential.

Deputy J.A.N. Le Fondré:

Okay, thank you. Right. Is there somewhere in the O.B.C., and I fully accept, or I may well have missed it, that it basically says: "This is what we have got and this is what you are getting"?

Senator S.C. Ferguson:

This is what we might include ... yes, sorry.

Deputy J.A.N. Le Fondré:

Well, let us do the "and this is what we are getting".

Director, States Department for Infrastructure:

In terms of a table side by side I suspect not in the form that you are suggesting but the details of what is included in the Future Hospital is set out in considerable detail within a number of those appendices.

Deputy J.A.N. Le Fondré:

Okay. Could you give me a direct reference from the O.B.C. as to where one should look, just for a public reference because the public here ...

Director, States Department for Infrastructure:

I cannot but you will appreciate, firstly, this is a Treasury hearing so I have come prepared for that. Second ...

Deputy J.A.N. Le Fondré:

Sorry, Mr. Foster, the reference to part (a) of the proposition is to conclude the preferred scheme contained in the Future Hospital Outline Business Case for £466 million.

Director, States Department for Infrastructure:

Indeed. I cannot today sit here and point to one item in one appendix of a set of documentation which is a considerable size. I can provide you with that information and will be happy and willing to do so.

Deputy J.A.N. Le Fondré:

I have a reference that says it is appendix 17 in the O.B.C. and that is what we should look at, and that will be fine or whatever the reference is. But the reason I ask is because, as Senator Ferguson had just referred to, is what I am trying to just get an idea on is what are we approving for £466 million? So, for example, is it possible to confirm, as of now, whether the chapel is presently included in the cost of the scheme?

Director, States Department for Infrastructure:

There will be facilities for multi-faith, i.e. a replacement for the chapel.

Deputy J.A.N. Le Fondré:

So that is included in the scheme?

Director, States Department for Infrastructure:

There is a replacement proposed. I cannot give you the details. I do not have them today.

Senator S.C. Ferguson:

It is not quite the same.

Deputy J.A.N. Le Fondré:

No. I just need to know the facility is there. The hydrotherapy pool, is that there?

Director, States Department for Infrastructure:

The hydrotherapy pool is not currently within the scheme because the service is being considered by the Health and Social Services Department in terms of how that service will be delivered and this is not uncommon.

Deputy J.A.N. Le Fondré:

No, I accept that.

Director, States Department for Infrastructure:

You will recall from our previous discussions that the processes of reviewing how services are delivered in and out of hospital is core to P.82 as well as the delivery of the Future Hospital Project.

Deputy J.A.N. Le Fondré:

What I was trying to get to, and I have used those 2 examples, because I think, as far as I am aware they are in the public domain, is that how does any one States Member identify, for example, that the hydrotherapy pool is not included whereas it previously was or that the chapel was there and is included, for example, because that is part of the story of telling people what they are signing up to?

Director, States Department for Infrastructure:

If I may, your question was "how may States Members", that was your specific question. I will answer that question by saying: you have an absolute opportunity on Friday, on the States Members' briefing, of bringing all of those questions and receiving the answers in full. Indeed, email invitations to States Members to attend on Friday have specifically and repeatedly asked for questions to be tabled that can be responded to. So there is a very ... there was a very clear opportunity for States Members for questions to receive responses to all of those questions at a high level, a general level, a detailed level.

Deputy J.A.N. Le Fondré:

Okay. Let us change that. How is a member of the public to know on the basis that this is, to the public, what you have made available; this information?

Director, States Department for Infrastructure:

Members of the public can ask questions and receive answers.

Deputy J.A.N. Le Fondré:

No. What I meant was, is how ... I am addressing this to the Minister. How does a member of the public, who obviously as a taxpayer, and assuming it is the taxpayers that are going to be funding this ultimately, or money that is going towards it, how do they identify the facilities being provided?

The Minister for Treasury and Resources:

Well, they would rely upon the fact that it has been properly scrutinised and that the information is available to those that have the ability to consider the overall package.

Deputy J.A.N. Le Fondré:

Right. I think I will take that as it is very difficult then for a member for a public to identify ... well, let us rephrase that. If one could have the reference that Mr. Foster has referred to so that can be sent through to us and perhaps we can assess that at that point I think. Okay. Minister, previously you accepted the Corporate Services Scrutiny Panel's amendment, this is in the main proposition, which split out the main works of £392 million and a contingency of £74 million in the proposition. Why have you not included this type of wording this time around?

The Minister for Treasury and Resources:

Through the process previously undertaken when the proposal was being scrutinised we acceded to a number of changes in order to try and improve the proposition, working together with members of the Scrutiny Panel. When it was withdrawn and we looked again we have crafted a proposition in a way that we believe is simple, straightforward and reflective of what is required.

Deputy J.A.N. Le Fondré:

In our previous conversation you said you took lots of views on ... particularly considering the funding of things because that was important. Our view obviously has been dropped and whereas previously it had been accepted in May?

The Minister for Treasury and Resources:

Well, as I have said, that was at a time when there were quite a number of changes being put in place and the proposition, through its various amendments, had become rather unwieldy and unclear. The proposition that is before you here and will go before Members, we believe is clearer and meets the objectives that are necessary.

Deputy J.A.N. Le Fondré:

Okay. In terms of clarity, the Corporate Services Panel previously identified that the budget for the hospital was £392 million before contingency. Can you just clarify how that figure has changed, Minister?

Director for Financial Planning and Performance:

So the contingency sums now total £70 million.

Deputy J.A.N. Le Fondré:

Whereas previously it was £74 million? Okay. So on that basis the main works to the hospital would be £396 million?

Director for Financial Planning and Performance:

Yes.

Deputy J.A.N. Le Fondré:

So one could bring an amendment to the proposition that suggested that the main works would be £396 million and the contingency would be £70 million, which would be consistent then with the original proposals that were mooted in May, correct, on the basis of what has just been said to me?

The Minister for Treasury and Resources:

Yes. I mean the fact that there is a change ...

Deputy J.A.N. Le Fondré:

Can I just refer that to the respondent? Then perhaps the Minister would want to follow up afterwards.

Director for Financial Planning and Performance:

If you wanted to present it in the same way that you did previously those would be the numbers that you would use.

Deputy J.A.N. Le Fondré:

Thank you. Minister, do you want to follow up?

The Minister for Treasury and Resources:

No. I am just going to make the point that that just demonstrates, and not surprisingly, and we said this at the outset, that was very early in the life of the project. Time has progressed and clearly, as the project develops, the numbers will change as more information is obtained and as the Outline Business Case is being developed and that is not really that surprising.

Deputy J.A.N. Le Fondré:

So the £4 million difference, where is that difference being spent?

Director, States Department for Infrastructure:

Once again the details are set out in appendices and within the O.B.C. As ...

Deputy J.A.N. Le Fondré:

Could you give me some direction roughly where to look?

Director, States Department for Infrastructure:

As design development continues with a project of this scale the project design will move forward, costs will change. We have moved through a period of time. Other elements of the contingency, such as the optimism bias, will become less of a contingency sum and more of a crystallised sum as that sum is realised into the design. That is the reason for the contingency being present.

Deputy J.A.N. Le Fondré:

The reason I am pausing is I am treading into the question areas that are coming forward. I am just worried that we are going to go into repetition.

Director, States Department for Infrastructure:

I cannot sit here and give you a like-for-like analysis as to how each pound of contingency is translated into a cost within the overall detail, as it were.

Deputy J.A.N. Le Fondré:

Okay. Well, we will see where that goes when we get to the next questioner. What happens if expenditure exceeds contingency? What are the plans?

The Minister for Treasury and Resources:

First and foremost, there is no intention that that should be an outcome but ultimately if the project costs were to exceed the budget that has been set then additional funding would have to be requested and that would come, depending on the scale of it, from either the capital vote or from the Strategic Reserve.

Deputy J.A.N. Le Fondré:

Okay. Quickly, on page 79 there is an analysis of revenue costs. Could you explain the total revenue cost of £15.6 billion please?

The Minister for Treasury and Resources:

What page are you on, sorry?

Deputy J.A.N. Le Fondré:

I was on page 79 in the Gleeds Report.

Director for Financial Planning and Performance:

So the table within there, within the O.B.C., explains that you have got life cycle costs including the capital costs as part of £466 million but also obviously we have the ongoing costs of running that facility once it has been built. It will include additional costs of running a larger facility, which will have to come through M.T.F.P.s (Medium Term Financial Plans) in the future. It also explains that there are other costs, such as lease costs, where we are currently having to move things around to allow the enabling works to happen. We have got bond costs. So that table is supposed to present to you the sort of full cost of the new build.

Deputy J.A.N. Le Fondré:

Okay. A couple of questions come out of this. So bond issue costs are included, correct?

Director for Financial Planning and Performance:

Yes.

Deputy J.A.N. Le Fondré:

Why?

Director for Financial Planning and Performance:

Because when drawing an O.B.C. that is what they do in the U.K. That is how they present it. They include the capital cost, the funding cost.

Deputy J.A.N. Le Fondré:

Right. That leads me nicely to my next question, why have the bond interest costs, which I call the funding costs, not been included?

Director for Financial Planning and Performance:

Because the way the proposal was put on the table does not ask for the project to pay those ongoing costs. So in the U.K. it is very different because the trusts have to have the affordability. They would have to have the interest cost within their budget.

Deputy J.A.N. Le Fondré:

I will just cut you down for a moment. Have you got page 79 in front of you?

Director for Financial Planning and Performance:

Yes.

Deputy J.A.N. Le Fondré:

Right. At the start of the paragraph on 4.121, can you just read that out to me please, the first line?

Director for Financial Planning and Performance:

“A summary of the revenue costs set out below.”

Deputy J.A.N. Le Fondré:

Right. So why are the funding interest costs not deemed to be part of revenue cost?

Director for Financial Planning and Performance:

Because it is not part of a revenue budget for any department. It is paid for outside of revenue budgets.

Deputy J.A.N. Le Fondré:

It says here: “The revenue cost” in the wider context, certainly for me, revenue cost is a cost in terms of ongoing and surely the interest cost would therefore ordinarily be treated as a revenue cost using that line as it says. It does not say anything about normally budgeted costs and where it is going to be funded from are not included here. That is what it says.

[10:45]

Director for Financial Planning and Performance:

We did have quite a long discussion about this as part of the project board including 40 years of interest rate for a funded solution that was outside of the project if you like. We decided that was not necessarily aligned with these sorts of end costs.

Deputy J.A.N. Le Fondré:

So my maths is not terribly quick at this stage but that is roughly £7 million in 40 years, which is, what, £280-odd million, something along those lines, was not considered necessary to include it in the revenue costs for the scheme?

Director for Financial Planning and Performance:

It was not deemed as a revenue cost for the hospital project, no.

Deputy J.A.N. Le Fondré:

Okay. Moving on just briefly then and this is only because ... and we looked at it. You refer to ongoing lease costs of £67.5 million, is that, for example, the cost of the catering site; would that have been included in that figure? So essentially the cost of going offsite is going to be £67 million over the life of the project?

Director for Financial Planning and Performance:

Ray might need to help me on this. I think some of these ... well, the lease costs are incurred in the short term as well as ongoing lease costs so there are elements of moving people off-site in order to do the work that we need to do to build the main hospital but those lease costs will then be dropped when we move them back over on to the main site but there are elements; so your reference to catering is one of those that we are not intending to bring back on site.

Deputy J.A.N. Le Fondré:

That is a consequential cost. Put it this way, is there, or if not, could you provide a breakdown of the kind of what I call the relocation cost element and the confirmed ...

Director for Financial Planning and Performance:

Ongoing?

Deputy J.A.N. Le Fondré:

Yes.

Director for Financial Planning and Performance:

Sure.

Deputy J.A.N. Le Fondré:

Could you give us a breakdown on that please?

Director for Financial Planning and Performance:

Sure. Yes, no problem with that.

Deputy J.A.N. Le Fondré:

Okay. In terms of the ... going back to the wording of the proposition and then I will be wrapping it up hopefully. The original proposals talked about essentially the protected capital balance. I am just trying to find exactly where it was. Yes, sorry. It was a proposition that was originally proposed by Chris Taylor, which I understood had been accepted and certainly was consistent with problems

you had about the process at the time. It said: "That provided the capital value of Strategic Reserve did not fall below the minimum level set out in ..." basically to protect a balance. That is not in the proposition now. Why not?

Director for Financial Planning and Performance:

I think there are 2 reasons. One was, when we had those discussions with Constable Taylor it was when £400 million was looked at being borrowed, so obviously there was a desire to protect the Strategic Reserve from being used for other purposes when we needed more money in the reserve fund to be able to afford the interest costs. Also, back to the comment that the Minister referred to earlier, is when you read the proposition again, the original proposition, it felt clunky and difficult to understand and we did not feel that it was something that necessarily needed to be in there as the borrowing costs were below it.

Deputy J.A.N. Le Fondré:

Okay. Just briefly and then I will get to my last question which is: how close to the protected capital funds do we get under the proposed modelling plan?

Director for Financial Planning and Performance:

It is £35 million.

Deputy J.A.N. Le Fondré:

Okay. So just for clarity, in a particular year one will be £35 million above the protected balance?

Director for Financial Planning and Performance:

Yes.

Deputy J.A.N. Le Fondré:

Okay. Final question, I think. The modelling that was done or the stress testing that was done of the impact on the particular service, has any new work been done since May of this year?

Director for Financial Planning and Performance:

No.

Deputy J.A.N. Le Fondré:

Okay. So from our purposes what we should be doing is relying on work done by Ernst & Young previously, which you previously supplied to us. There are no updates on that.

Director for Financial Planning and Performance:

We have no updates, no. On the basis that when we asked for that piece of work again, it was based on £400 million. With a much lower borrowing balance, we felt that there was no need to do the work again.

Deputy J.A.N. Le Fondré:

Okay.

Senator S.C. Ferguson:

Can I?

Deputy S.M. Brée:

Yes.

Senator S.C. Ferguson:

It is just a quick one. I notice obviously that this is the discounted amount. What is the undiscounted amount?

Deputy J.A.N. Le Fondré:

Is this page 79?

Senator S.C. Ferguson:

Yes.

Director for Financial Planning and Performance:

I am sorry I am not ... I do not understand the question.

Senator S.C. Ferguson:

Well, at the top of the column it says: "Pounds million discounted". So what is the value if it is not discounted? What is the discount rate?

Director for Financial Planning and Performance:

The discount rate is 3.5 per cent. Ray, is that right?

Director, States Department for Infrastructure:

I believe so, yes.

Senator S.C. Ferguson:

3.5?

Director for Financial Planning and Performance:

We can confirm back to you on what the undiscounted value would be.

Senator S.C. Ferguson:

The discount rate is 3.5?

Director for Financial Planning and Performance:

That is a cost of capital.

Senator S.C. Ferguson:

Right.

Deputy S.M. Brée:

Just one question from me. On page 79 of the Gleeds Report where we have this summary of revenue costs, just confirm that is over the projected lifetime of the new build hospital, correct? I am just trying to clarify that that is a total revenue cost, £15.6-odd billion over the lifetime of the new hospital.

Director for Financial Planning and Performance:

It starts when the hospital opens its doors effectively.

Deputy S.M. Brée:

Yes, from the date of effectively commissioning, if you want to call it that, to when? What is the timeframe? Just to confirm what timeframe are you working on there?

Director for Financial Planning and Performance:

So the Green Book uses 60 years as the life.

Deputy S.M. Brée:

So that is the total revenue costs for the next ...

The Minister for Treasury and Resources:

To 2084.

Deputy S.M. Brée:

... 60 years, you are using in that calculation?

Director for Financial Planning and Performance:

Yes.

Deputy S.M. Brée:

Okay. My other question was, just clarification. You have put in there as part of that cost the bond issue cost, i.e. the cost to issue the bond. You rightly say that because of the way in which the setup is, the interest coupon, annual coupon payments are not included because there is no income flow to service that debt, but you also have this issue of cost of carry of the bond. Why is the cost of carry of the bond in the early years, particularly, not included here because it is a direct cost attributable to that project outside of the funding costs? It is an additional cost and I think you were saying is it is £7 million, you think, is the additional cost of carry?

Director for Financial Planning and Performance:

Well, in terms of the cost of the coupon every year is about £7 million.

Deputy S.M. Brée:

Okay. But you have a cost of carry, do you not, of any bond?

Director of Treasury Operations and Investments:

Only if your investments do not return the same as your bond coupon.

Deputy S.M. Brée:

Yes, but what you were saying is, if you have got a coupon of 2.625 per cent in the early years, where you are investing that money prior to releasing it, you are only going to be earning say 1 per cent so you immediately have cost to carry on the total value of the bond of 1.625 per cent. That is what I am talking about, cost to carry in the early years.

Director of Treasury Operations and Investments:

I understand that.

Deputy S.M. Brée:

Right, and yet this is not included in this table whereas you have included £2.5 million for the issuance costs. It does not seem to be logical to have one and not the other, if you see what I mean. What was the rationale for excluding the cost to carry in the early years?

Director of Treasury Operations and Investments:

So as an example the last 3-year performance of the Strategic Service was 8.7 per cent per annum. The last 30 years' performance has been R.P.I. plus 4.4, all of which are above the bond coupon, therefore there would not be a cost of carry.

Deputy S.M. Brée:

I am talking about the fact that you were saying earlier on, the proceeds from the bond will be invested under a different strategy, which has a lot less risk, therefore has a lot less reward yield.

Director of Treasury Operations and Investments:

Yes.

Deputy S.M. Brée:

Right? So if you are bringing in £260 million and effectively putting it into its own profile within the Strategic Reserve, therefore there is no capital risk, or very little capital risk, your yield is going to be 1 per cent on that, if you are lucky.

The Minister for Treasury and Resources:

That is the assumption being used.

Deputy S.M. Brée:

Yes, that is the assumption. So what I am saying is, there is a differential therefore on the yield you are getting on the bond of money raised versus the coupon you are legally obligated to pay to investors. Now, you are saying that you are going to finance that difference out of the returns from the Strategic Reserve.

Director of Treasury Operations and Investments:

Which are modelled at R.P.I. plus 2.

Deputy S.M. Brée:

Fine. No, it is purely where does that cost go and yet you are charging the hospital the cost of issuing the bond. It does not seem to make sense that you would charge the project one value and not the other and we were just asking why you have applied that, I would say, seemingly illogical move.

Director for Financial Planning and Performance:

I guess we took advice from the financial advisers for the project, so there are financial advisers on the project as well as financial advisers on the funding, and they asked us to provide them with these numbers and that was what they asked to be included in these numbers for the O.B.C.

Deputy S.M. Brée:

So that table reflects what the advisers to the project want to see as opposed to what is normally seen in such circumstances? It is just trying to ascertain what we are looking at.

Director for Financial Planning and Performance:

Sure. I mean I think the ...

Deputy S.M. Brée:

Are all costs included? I would say; no, they are not. You would say; yes, they are. So it is just trying to understand it. Okay.

Deputy J.A.N. Le Fondré:

I have just one further question and it is on that table. So you have said that the discount rate is, you think, is 3.5 per cent but you have taken out £40 billion on 3 per cent inflation. So I was trying to get to the point and I was trying to work out the impact of that difference and I was kind of ... if it was ...

Deputy S.M. Brée:

Well, they have said they will get back to us. We will move on.

Director for Financial Planning and Performance:

I will have to talk to EY and find out what discount rate they have used.

Deputy J.A.N. Le Fondré:

I think so but broadly speaking the undiscounted figure is going to be, therefore, at least £55 billion, is it not?

Director for Financial Planning and Performance:

That sounds logical but I will have to ask EY to confirm that.

Deputy J.A.N. Le Fondré:

Yes, okay. That is fine.

Deputy S.M. Brée:

Right, okay, we are now going to move on to the question of contingency. Terry.

Deputy T.A. McDonald:

With contingency there comes a word “controlled”. The first question is: the scope of some parts of the budgets have changed since the last review. How have you controlled any scope creep?

The Minister for Treasury and Resources:

I do not think there has been any “scope creep”. I mean there is a set budget for the project. There have been changes to the project, some fairly fundamental changes in relation to, as an example, Westaway Court which is not going to be refurbished. It is going to be completely restructured. Some of the functions that would have been in the main hospital have therefore moved into that particular or new build area and there has been an adjustment of budget as such. That is not extending the scope of the budget. That is just reallocating from different areas. I think as far as the contingency is concerned the way in which they are going to be managed are laid out in the proposition. I cannot really add very much more than that.

Deputy T.A. McDonald:

I am quite happy that obviously people are doing exactly what you expect them to be doing.

The Minister for Treasury and Resources:

People are operating. There are teams in the appropriate areas that are carrying out functions that have been allocated to them and I have no reason to suggest that that has not been done appropriately.

Deputy T.A. McDonald:

The relocation costs have increased from £40 million to £80 million. How have you ensured proper control over these decisions?

The Minister for Treasury and Resources:

Well, again, it has gone through the same process but we have got ... you have got a Political Oversight Group. You have got a project board. There is a governance and oversight structure in place to ensure that decisions are taken appropriately.

Deputy S.M. Brée:

May I just ask a quick question at this point? When we are looking at the relocation costs which we have established a lot relates to Westaway Court and the rebuilding there and the movement of pathology there, would you, Minister, agree that what we are now looking at is a 2-site hospital?

The Minister for Treasury and Resources:

No. I think you have got a one-site hospital but there are some functions that are being undertaken elsewhere. There is one primary site for the main function of the hospital. I think the decisions ...

Deputy S.M. Brée:

So, as far as you are concerned, and this is just seeking clarity, the fact that we are now looking at 2 buildings, new buildings; outpatients is being moved out of the current General Hospital to Westaway Court, pathology is being moved out of the current General Hospital to Westaway Court. You still believe we are looking at a one-site option?

The Minister for Treasury and Resources:

Yes, principally. I mean you can argue around the edges on it.

[11:00]

I think the solution that is being presented now and the way in which Westaway Court has been ... its role, and as opposed to refurbishment, a rebuild, and some additional functions housed within it, I think makes perfect sense and I think that has evolved as the project has developed.

Deputy S.M. Brée:

We are not questioning the logic of doing it. I am just questioning whether you still believe that, hand on heart, this represents a one-site option.

The Minister for Treasury and Resources:

The principal functions of a hospital are still in one location.

Deputy S.M. Brée:

Even though current services provided as principal functions of the hospital are being moved out of the new location. Okay. It is just clarity. Sorry, carry on.

Deputy T.A. McDonald:

P.107/2017 reveals that the budget is obviously being managed in 2 parts, optimism bias and contingency. They are managed by the Treasury, and the remaining estimated project costs, including the reparation, managed by the delivery team. Under the proposition can you confirm exactly which elements of the budget will be under your control?

The Minister for Treasury and Resources:

Well, the Minister for ... in fact again it is laid out in appendix A, I think it is, which lists where the various functions are on page 19 but under appendix A, under 3.2, you can see that the roles of the Minister for Treasury and Resources, the responsibilities there are funding and investment. Under

3.3 you have got risk allocations in relation to the contingencies and the responsibility there for the Minister for Treasury and Resources.

Deputy J.A.N. Le Fondré:

May I ask a question?

Deputy S.M. Brée:

Yes.

Deputy J.A.N. Le Fondré:

Yes, Minister, you have just referred to 3.3, which talked about optimism bias and contingencies, can you just confirm what the elements are included in the ...

The Minister for Treasury and Resources:

Well, the total cost allocation ...

Deputy J.A.N. Le Fondré:

No, just the broad, what is contingency?

The Minister for Treasury and Resources:

Well, the risk allocation, you have got the optimism bias and contingencies.

Deputy S.M. Brée:

So what we are trying to understand, Minister, is confirmation from you under appendix A, 3.3, where you say "contingencies", exactly what is covered by that word within this proposition, the word "contingencies". We understand optimism bias. We are merely asking confirmation as to exactly what is included under the term "contingencies".

The Minister for Treasury and Resources:

You have got the works contingencies on the main scheme; that is ... you do not want the amounts, do you?

Deputy S.M. Brée:

No, we want the areas.

The Minister for Treasury and Resources:

Okay. The contingency risk; that is the client contingency. The optimism bias, the works contingency, the relocation schemes and the client contingency relocation schemes and there are allocated amounts to each of those.

Deputy J.A.N. Le Fondré:

Can I just clarify that ...

The Minister for Treasury and Resources:

Page 19, you will find under proposition 107.

Deputy J.A.N. Le Fondré:

Minister, can I just clarify, is inflation captured in that or not?

The Minister for Treasury and Resources:

No.

Deputy J.A.N. Le Fondré:

Right. In the original proposals that were lodged by Treasury on P.130, amendment 2, it says: "In accordance with best practice the project does therefore carry substantial contingencies at this stage for inflation risk and optimism bias." So contingency in May included inflation and therefore would have been under these words, under your report, lodged by the Minister for Treasury and Resources contingency for inflation. Why has that changed?

Director for Financial Planning and Performance:

The inflation was always a separate number to contingency and optimism bias.

Deputy J.A.N. Le Fondré:

No, it is a separate number. I am accepting that but it is a contingency.

Deputy S.M. Brée:

What we are trying to ascertain here is control of contingency allowances. Previously inflation, correctly, had been taken as contingency because one cannot determine what inflation rates moving forward are going to be therefore it is a contingency. A contingency is there to cover unseen circumstances. We now have a situation where the proposition that we are being asked to vote on has changed to remove inflation as a contingency so it is no longer under the control of the Minister for Treasury and Resources and effectively inflation is going to ... or the inflation risk and the contingency around that is to be managed by the delivery team. We are asking why the decision to change things was made about the inflation risk and the contingency attached to it.

Director for Financial Planning and Performance:

It is not a conscious change.

Deputy S.M. Brée:

Yet, you will agree there is one, but you cannot give, at this moment in time, an explanation of why, is that correct? At this moment in time, i.e. here, today you cannot explain to us why inflation previously was contained within contingencies and now has been moved to the delivery team as part of the project costs?

Director for Financial Planning and Performance:

So, my understanding when previous amendments were made it was the risk element of the cash flow excerpt in the report that was to be managed did not include inflation.

Deputy S.M. Brée:

It did, because it says here on your report: "The plan has always been for Treasury to retain control over the contingencies. The project is carrying substantial contingencies at this stage for inflation, risk and most notably optimism bias." So you identified there that inflation was a risk and therefore a contingency was attached to it, which is normal practice.

Director for Financial Planning and Performance:

Yes.

Deputy S.M. Brée:

What we are merely asking at this point in time, today, can you give us specific reasons why the decision was taken not to view inflation as a risk and therefore a contingency under control of Treasury, but instead actually put it as a project cost in control ... managed, sorry, by the delivery team. It is not the amount, it is not anything else, it is why has there been a change in thinking or policy?

Director for Financial Planning and Performance:

There has been no change.

Deputy S.M. Brée:

Well, there has.

Director for Financial Planning and Performance:

No.

Deputy S.M. Brée:

There has. We are saying previously we understood it, it made sense. Now we are questioning why is that that looks sensible and controlled and could understand the reasoning behind it, why has inflation now been put into estimated project costs managed by the delivery team? It is a very simple question. If you cannot, at the moment, answer that then could you please provide to this panel, as soon as possible, the reasons why it was done and who made the decision to do it?

The Minister for Treasury and Resources:

There is no conscious change but we will clarify the position because clearly the documentation is giving you the impression, from what you have said, that a certain action has been taken but we will confirm that position back to you.

Deputy J.A.N. Le Fondré:

So, to be clear, Minister, you have not made a conscious decision to ...

The Minister for Treasury and Resources:

No. That is the point, I think there is something misleading and it may be an error in ...

Deputy S.M. Brée:

Well, if you could clarify that point as to why inflation is no longer specifically a contingency.

Deputy J.A.N. Le Fondré:

One further point in respect of misunderstandings or not, it was a concern that the Corporate Service Scrutiny Panel had raised about future management of inflation because we were concerned that estimates of inflationary change can go up or down. I believe the example was used of Westaway Court in May and that the inflation estimate had gone down and then the inflation element was spent and that is why we raised it at that point. At that point in time Treasury accepted the principle, hence this amendment took place. So we were looking for why that conscious decision and that discussion appears to have been made.

Deputy T.A. McDonald:

The proposition states that optimism bias and contingency are managed by Treasury. Will this be a decision for your department alone?

The Minister for Treasury and Resources:

It will be. The recommendations obviously will flow through the set governance structures so from the project board through the team but ultimately it will be Treasury that make the decision.

Deputy T.A. McDonald:

Will the Political Oversight Group, for example, be involved?

The Minister for Treasury and Resources:

Well, the Political Oversight Group is part of the oversight arrangements for a particular project, but, as I have just stated, the ultimate decision will be a decision for Treasury, that is where the control is rightly placed.

Deputy T.A. McDonald:

When all is said and done, could you be outvoted by, again for example, the P.O.G. (Political Oversight Group) itself?

The Minister for Treasury and Resources:

No, absolutely not. It is a Treasury decision. The recommendations come through, as I have outlined, and I think the documentation makes clear, but ultimately the decision is a decision for Treasury. That is where the control and decision making in this regard lies.

Senator S.C. Ferguson:

Who sits on the Political Oversight Group?

Director, States Department for Infrastructure:

It is currently the Minister for Health and Social Services, the Minister for Infrastructure, Assistant Minister for Health and Social Services, that is Deputy McLinton, and the Assistant Minister for Treasury and Resources, that is Constable Refault, and Senator Routier from the Chief Minister's Department.

Senator S.C. Ferguson:

Does Connétable Refault find it a bit difficult being the Assistant Minister for both departments?

Director, States Department for Infrastructure:

I think that is a question you ought to direct to him, but it has not been an issue.

The Minister for Treasury and Resources:

It is a question that I will answer. The makeup of the board includes the Assistant Minister, there are 2 Assistant Ministers for Health, he sits on it not as an Assistant Minister for Health but as an Assistant Minister for Treasury and Resources and he does not find that a difficult position. He is wearing a different hat and that is perfectly reasonable.

Deputy S.M. Brée:

Sorry, Minister, can I just clarify that? You are entirely satisfied that there is no possibility of a conflict of interest between Connétable Refault sitting on the panel representing the interests of Treasury and Resources while at the same time being an Assistant Minister for the Health and Social Services Department as well? As far as you are concerned there is no possibility for a conflict of interest?

The Minister for Treasury and Resources:

I have discussed this with my Assistant Minister and I am very satisfied that his role and function on that particular group is as Assistant Minister for Treasury and Resources. As I have already stated, there is a separate, additional, Assistant Minister for Health who sits on that board representing health interests.

Senator S.C. Ferguson:

We have covered inflation as part of contingency, however the inflation has reduced from £68 million to £53 million since the previous proposals. As the budget has not reduced you must have allocated this difference to other expenditure lines, so what happens, as was mentioned, with regard to Westaway Court, for instance ... what is plan B if inflation increases as it appears to be doing?

The Minister for Treasury and Resources:

Are you asking what happens if the budget that has been set for this project is exceeded?

Senator S.C. Ferguson:

Well, we have had a reduction in inflation from £68 million to £53 million in the calculations and so, you know, this has been taken to have been a saving and has now been organised to be spent. But it is not a real saving because it is just a forecast. Inflation does seem to be going up a bit so what is plan B?

The Minister for Treasury and Resources:

There are many moving parts in a project of this size, not surprisingly. Inflation has risen slightly, it has fallen slightly and indeed the pressure is for it to increase in the future but there many other areas where cost pressures will fluctuate. That is the reason why at the early stage of a project of this size you have a contingency of the size that we do. Currently £70 million, it was £74 million, there has been a reduction since May for the reasons stated earlier on. So, again, it is still at the very early stages of this particular project. So it is not surprising there are some changes.

Senator S.C. Ferguson:

Well, the contingency has fallen to, I think, £38 million, has it not?

The Minister for Treasury and Resources:

The total contingencies are, or were back in May, £74 million, they are now £70 million.

Senator S.C. Ferguson:

I am sorry, I seem to recall that we have been looking at £38 million.

Director for Financial Planning and Performance:

Yes, that is optimism bias.

Senator S.C. Ferguson:

Okay.

Deputy J.A.N. Le Fondré:

Sorry to interrupt, the optimism bias is £38 million, that is fine, the contingency identified at page 78 is £19 million, what is the remaining balance to get up to £70 million? Where is it?

[11:15]

The Minister for Treasury and Resources:

Chairman, while my colleague is looking at that, could you just excuse me for one moment while nature calls?

Deputy S.M. Brée:

Of course.

Director, States Department for Infrastructure:

Perhaps I can also add something to fill the gap. The proposition with regard to the amendment to the Finances (Jersey) Law has been lodged, it is P.111/2017 and is on the States Assembly website. So that may help Members.

Director for Financial Planning and Performance:

Yes, it is quite difficult, the numbers are presented differently in different tables, so I have the table from ... the extract from the report which gives me my £70 million quite clearly in terms of stripping out contingencies. Some of the contingencies must be within the capital costs in the table, line 78.

Deputy J.A.N. Le Fondré:

So which page would you prefer us to look at?

Director for Financial Planning and Performance:

So page 19 of the report strips out what we classed as risk, which was the 9.71 works contingency, the 19.25 client contingency, 35.25 optimism bias, then a further 2.59 relocation works contingency and a 3.62 client contingency.

Deputy J.A.N. Le Fondré:

That rounds up to 70?

Director for Financial Planning and Performance:

About 70, yes.

Deputy S.M. Brée:

Once again any inflation risk is not ... you were saying does not fall into that £70 million?

Director for Financial Planning and Performance:

No.

Deputy S.M. Brée:

Okay, we will just clarify what we are looking at here. Right, okay.

Senator S.C. Ferguson:

We note also that inflation will be controlled by the Project team, not Treasury, why?

Director for Financial Planning and Performance:

I think what we were trying to demonstrate was to reflect an amendment that was brought to the previous proposition, which was around the risk element. That was the sum of money that we were being asked to demonstrate that Treasury was going to control in a way that has not been controlled in other capital schemes. Okay, so Treasury has always been responsible for inflation. What we were trying to do was to demonstrate how we were going to further control, so round the contingency sums, which you would ordinarily have seen as part of the money allocated in the capital programme. It is not our intention to not control, it is just that we have tried to demonstrate the risk elements to have further control.

Director, States Department for Infrastructure:

If I may add, inflation, in its purest sense, is an exogenous function, prices will change, they may rise, they may fall. If you want to do something that is costed at today's price base and you go out to the market in a year's time there may well be a different price associated with it. The budgets will

attempt to forecast that inflation as best as is possible for today's date. So in terms of a pure contingency, that inflation sum is a reflection of best estimate of the costs, all other things being equal, that you would need at that time. If inflation moves are greater or lesser, then there could be a return or an unused budget or there could be a call on contingency. In a traditional budget approach for a capital project, the allocation is an outturn cost allocation, which will include both the inflation sum as forecast to outturn, based upon the cash flow, and the contingency that reflects the need for that project to have flexibility because of movements in inflation and movements in other things. There are all sorts of other things that could happen. Those cost estimates get narrowed down to a point that, depending on the nature of the contract, on going out to tender you will have a price that will be namely fixed but will have some variability still within it. In this arrangement the contingency sums will be held within the Strategic Reserve, indeed the main principle funding and the inflation element is still within the Strategic Reserve. Those funds are released based upon a cash flow provided to the Treasury Department and authorised by the Treasurer and they will be based upon the estimates that become narrower in terms of their certainty and have less contingent element and more certainty. The funds will be raised at the point of the requirement for those funds to be expended. So the principle, in very simple terms - and it does not happen like this in practice - when a contract is ready to be signed the department will need the funds available to be able to meet the costs associated with that contract. At that point in time the funding, which will be the main funding with any inflation element that has been realised and any contingency sum that is needed which will have gone through a rigorous and extensive reporting process, will be released from the Strategic Reserve into the hospital fund for that to take place.

Deputy S.M. Brée:

Can I just ask a question here? What you have explained to us I understand and when we look at table 5, comparison of the capital costs and we are looking at that figure of £53.08 million inflation, and again please correct me if I get this wrong, that is an inflationary figure that you are saying: "If we take today's price, we have to account for the fact that the project has an 8-year life span, therefore there is an impact of projected inflation on today's costs and what it will be when we get to do it." So there is an inflationary figure already built in so that £53 million is saying that is the likely impact of inflation based upon the tables and figures that we currently have available and are used within the industry as a very good guideline as to what the inflationary impact may be.

Director, States Department for Infrastructure:

That is correct. That is the cost of doing it tomorrow ...

Deputy S.M. Brée:

Yes, it is the future value cost of something. What about the fact that ... where is the contingency on the inflation risk that inflation increases above the guidelines that you are using to give you that

£53.08 million, i.e. suddenly inflation goes through the ceiling for whatever reason, that is an inflationary risk above and beyond this calculated figure. So where is the contingency to cover that inflationary risk?

The Minister for Treasury and Resources:

I think it is safe to say in a project, any project, but a project of this size that there are going to be risks and the contingency, as we have said on numerous occasions, is much larger at this stage, the general contingency, than would otherwise have been the case. The assumptions on inflation are reasonable assumptions, that does not mean, as you painted, there could not be some extraordinary circumstance that will lead to that growing and if that were to have the net result of the overall budget being breached on the project, then we refer back to the answer that I gave you earlier on this morning.

Deputy S.M. Brée:

Right. I am just trying to clarify that inflation figure of £53 million: does it or does it not include a contingency figure for inflationary risk above and beyond that which you have factored in using industry guidelines.

Director, States Department for Infrastructure:

No, the inflation figure ...

Deputy S.M. Brée:

Well, that is all I am trying to understand ...

Director, States Department for Infrastructure:

... is our estimate of inflation ...

Deputy S.M. Brée:

Yes, based on?

Director, States Department for Infrastructure:

... it does not provide an estimate plus.

Deputy S.M. Brée:

A contingency for inflationary risk?

Director, States Department for Infrastructure:

If inflation were higher there would be other ... the other contingency pots would be a potential call, as would any value engineering, trench and design, all sorts of other aspects that one would ...

Deputy S.M. Brée:

I am purely talking about inflationary risk here. Do you not believe, Minister, that there should be a contingency to cover inflationary risk and that contingency should be under the control of the Treasury Department?

The Minister for Treasury and Resources:

I think as I have already stated, and have done previously, the contingency levels generally are appropriate and they are much larger than they would have been, therefore there is some scope within the general contingencies to deal with any minor changes, if that were to be the case.

Senator S.C. Ferguson:

Just one little one. Can you expand on the reasons for reducing the optimism bias from 13 per cent to 12 per cent?

Director, States Department for Infrastructure:

Simply put, optimism bias - and I am conscious of time so I will not give you the definition because I will probably get it wrong as well - relates to the fact that the experience of doing projects of this nature, this scale over a long period of time is that people are generally too optimistic in their delivery so a contingency labelled optimism bias underpins, in financial terms, that tendency to plan to do something and then have your plans moved by some degree that has a financial impact. As you move through the progress of a project you become more certain, so design and development becomes more certain and the project progresses, the likelihood of being over optimistic reduces. The review that was undertaken as part of the process for the delivery of this proposition and the Outlined Business Case recognised that significant progress has been made in a number of areas and that the optimism bias could be reduced. Now, you would expect the optimism bias to continue to reduce as you develop further within the project, to the point that the optimism bias effectively either disappears, is returned or is crystallised as a contingency sum. We are too far away to be able to have those decisions hardcoded, but that is the direction of travel. It is an interesting view but it is the view that H.M. (Her Majesty's) Treasurer takes and it is what we are following in accordance with the H.M. Treasury Green Book guidelines.

Senator S.C. Ferguson:

How does the value you are using compare with the value in the Green Book?

Director, States Department for Infrastructure:

It is within the normal band within the Green Book for a project of this nature. I do not have the Green Book with me but I can provide ... there are different optimism bias rates for different types of projects, for example an I.T. (information technology) project tend to be very overoptimistic and there is a history of them not achieving. I can provide you with some information on how the optimism bias is calculated and what sort of rates and the process for dealing with it. It is ...

Deputy S.M. Brée:

That would be useful. I am conscious of the time. We need to move on, if we may, to talk about the hospital construction fund.

The Deputy of St. Ouen:

Yes, Minister, so recognising concerns over contingency controls, the proposals for holding the bond monies were amended earlier this year so that the bond monies would be held in the Strategic Reserve, as we have discussed and only transferred to the hospital construction fund when required. Can you confirm that is the firm intention?

The Minister for Treasury and Resources:

Yes, that is the intention, exactly what will happen. In fact I think the detail is contained within appendix A of the proposition.

The Deputy of St. Ouen:

So is it fair to describe the hospital construction fund as simply a conduit through which money will pass and will not be used as a fund with any significant balances in it at any time?

The Minister for Treasury and Resources:

Yes, in general terms. Obviously the cash flow of it will need to be relevant to the project, make sure the project is not in any way hampered by the inability to progress without the funds being available to pay. But, yes, effectively the money is held in the Strategic Reserve and transfers through the hospital construction fund in the way described.

The Deputy of St. Ouen:

What will be the triggers that will release funds from the Strategic Reserve into the hospital construction fund?

The Minister for Treasury and Resources:

It will follow through the oversight governance structures that are in place and listed. Effectively the Project board and there is a Project delivery team, and those requests will therefore come through

to Treasury for release of funds into the hospital construction fund. There is an overall cash flow as well that will be developed to signpost.

[11:30]

The Deputy of St. Ouen:

Yes, can we just delve down a little more deeply. The contractor will presumably make applications at an agreed timetable for stage funding, will he?

The Minister for Treasury and Resources:

Yes, the project of course is being managed by D.f.I. (Department for Infrastructure) so the accounting officer is the chief executive or will be the chief executive for D.f.I. There is a cash flow for the project that will be part of this and that will be passed through the process that I have just identified to you in order to ensure the trigger of the transferring of funds.

The Deputy of St. Ouen:

Yes, I see. So your proposition explains that the accounting officer, who will be from D.f.I., is that right?

The Minister for Treasury and Resources:

Yes, correct.

The Deputy of St. Ouen:

Plus the Treasurer, will agree that the trigger points within the contract have been reached.

The Minister for Treasury and Resources:

That is right. The Treasurer effectively authorises the transfers or functions the transfers.

The Deputy of St. Ouen:

Yes, and is it likely that the contract will be written in such a way that there will be retentions at stages of the project?

The Minister for Treasury and Resources:

That is typical. Ray, do you want to just come in?

Director, States Department for Infrastructure:

Yes, there will be. We have not finalised the various forms of contract but there will be retentions within those contract forms. They do vary from contract form to contract form but normally 5 per cent is a retention sum and they are released at the end and may be released in whole or part.

The Deputy of St. Ouen:

Yes, so will those retention monies be retained within the Strategic Reserve?

Director, States Department for Infrastructure:

They will need to be available if they are due - if they are properly due. It is a level of fine detail we have not yet discussed with the Treasury and it really depends upon the investment strategy, I think, as much as anything. We need to understand ... as the man paying the bills in effect, I need to understand that I have access to funds to pay the costs of the property that have been incurred and for which budgets have been applied through the process of releasing budgets. Whether the cash is held within the fund or the cash is held within the Strategic Reserve would be a matter for discussion as we get nearer honing down the fine detail of the funds operation.

The Deputy of St. Ouen:

I understand. Okay, when would the preferred scheme be deemed to be complete and the last of the retentions released?

Director, States Department for Infrastructure:

The simple answer to that is when all bills due to be paid have been paid. The likelihood is that it is going to be a minimum of one year from the completion of all works. In practice it is often beyond one year if there are any disputes or any funds that are retained because of issues that need to be resolved. It is impossible at this stage to say precisely when. I think what we can do is identify the amounts of funds that need to be retained quite precisely when we get towards that end of contract point so that the funds that could be required to be retained within the Strategic Reserve can be very clearly identified for specific items. If we are in the good position of having funds that are not required the proposition retains those funds within the strategic reserve - so they do not move out of the Strategic Reserve - and the investment strategy will take account of what is required to meet those outstanding payments.

The Deputy of St. Ouen:

Will you be looking to the contractor to provide a warranty period for any defects that might arise?

Director, States Department for Infrastructure:

The way that warranties and defects will be addressed will be within the contract form. So the short answer is yes, but the details of which would be in contract form. There is a process of what is

called soft landings, which is a more considered way of the contractor exiting from the contractor with a longer period of handover. This is clearly a building that needs to operate and operate absolutely, completely effectively. So the contractor has quite a long period post normal contract completion in which the contractor's involvement is maintained. That is a soft landing process. We can send you details of what soft landing comprises if that would be useful.

The Deputy of St. Ouen:

Yes, I think it would be.

Deputy S.M. Brée:

Just going back to the way in which the actual hospital construction fund works, Minister, you mentioned the question of the accounting officer for the hospital construction fund is intended to be ...?

The Minister for Treasury and Resources:

The chief officer of the Department for Infrastructure.

Deputy S.M. Brée:

Who is the current accounting officer for the Department for Infrastructure?

The Minister for Treasury and Resources:

The chief executive of the department.

Deputy S.M. Brée:

Okay, so the Department for Infrastructure are responsible for delivering the scheme; you, Minister, are responsible for raising the funds and ensuring direct Treasury control happens and yet you are intending to have the same accounting officer for the department who is going to deliver the project being the accounting officer for the hospital construction fund, who are meant to be controlling movements of money and funds, being the same person. How are you intending to keep control?

The Minister for Treasury and Resources:

Well, an accounting officer has responsibilities under the law, first and foremost. Secondly, the way in which this has been structured, whereby the majority of the money sits in the Strategic Reserve and is only then passed down through the process that we have just outlined to the hospital construction fund, I think it is a not unreasonable way of operating. You have to bear in mind that the project delivery is going to be through that department so it is quite appropriate that the chief officer is, in this case, the accounting officer.

Deputy S.M. Brée:

So you see no possibility for any conflict of interest between his role as the accounting officer for the Department for Infrastructure under the control of the Minister for Infrastructure effectively, who is trying to deliver the project, and his role as the same man being - or Minister as the case may be - the accounting officer for the hospital construction fund whose responsibility it is to ensure that everything is controlled properly when it comes to the release of funds from the hospital construction fund to the contractor? You do not feel (1) there is any conflict of interest or (2) an area which the Minister for Treasury and Resources - whoever it will be - will lose sight possibly of what is going on?

The Minister for Treasury and Resources:

No, I do not see why that should be the case at all.

Deputy S.M. Brée:

Any other questions?

The Deputy of St. Ouen:

Can I just ask: part of the budget for the project includes the building of a temporary block in front of the granite building, when the use of temporary block comes to an end does that temporary building have any value?

Director, States Department for Infrastructure:

If I can take this. The answer is absolutely it does. Temporary buildings are fully complied with by laws and all sorts of other energy efficiency measures and what have you and are very good buildings. We are procuring that block, which is a 4-storey block in such a way that you can disassemble it into its individual storeys and it can be used elsewhere. It could be used for delivering health services or for more general use on that site or off that site. The exact purpose we have not yet determined.

The Deputy of St. Ouen:

Would we expect to receive a financial return to come back into the costs here?

Director, States Department for Infrastructure:

Well, the useful life of the building is likely to be significantly beyond the years that it is required for its immediate purpose. You say its useful life is 20 years and it is needed for, say, 10 years as a maximum, it has to be removed from that site once it is not required. It can be used for other States purposes, it could be disposed of, it could be used for non-health States purposes, so it could provide facilities for other purposes. At the moment we simply do not have a specific use but we are trying

to ensure that what we do have is something that does have a future use and can be used helpfully and successfully for 10 years beyond its immediate requirement.

Deputy S.M. Brée:

Okay, I am obviously very mindful of the time. We have gone over time a little bit, however, there were a large number of areas that we needed to cover. I feel we need to draw this public hearing to a close now. Thank you, Minister and members of your department, for your time and for your patience in explaining things to us. If we have any specific questions that arise out of this we will be contacting you. If we could ask you to undertake carrying out the tasks that you have committed to as soon as possible in providing us with information, we would be most appreciative. So, thank you very much.

[11:40]