IX
2009

# BILLET D'ÉTAT

## WEDNESDAY, 27th MAY, 2009

TREASURY AND RESOURCES DEPARTMENT –
CAPITAL PRIORITISATION

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# *B I L L E T  D' É T A T*

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**TO THE MEMBERS OF THE STATES OF**

**THE ISLAND OF GUERNSEY**

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I have the honour to inform you that a Meeting of the States of Deliberation will be held at **THE ROYAL COURT HOUSE, on WEDNESDAY,** the **27th MAY, 2009,** at 9.30am, to consider the item contained in this Billet d'État which has been submitted for debate.

G. R. ROWLAND
Bailiff and Presiding Officer

The Royal Court House
Guernsey
6 March 2009

# TREASURY AND RESOURCES DEPARTMENT

## CAPITAL PRIORITISATION

The Chief Minister
Policy Council
Sir Charles Frossard House
La Charroterie
St Peter Port

24th February 2009

Dear Sir

In December 2008, the States noted a Report **(Appendix A)** that *"set out the process that the Treasury and Resources Department intends to put in place between December and March 2009 when the States will debate and establish its capital priorities for this term"* and *"outlines the structure of the report that the Department will submit to the States in March on capital prioritisation. The March report will put forward recommendations on which projects the States should consider as the highest priority based on the results of the strategic review process to which each capital project will have been subjected. It will also address the possibility of strategic partnerships with the private sector to deliver States capital projects and include fully researched proposals on various borrowing options. Finally, the March States Report will include information on the economic climate and other important considerations that have been taken into account by the Department in developing the capital programme (including timings) which will be recommended to the States."*

This Report includes a recommendation that a borrowing arrangement is entered into to fund the proposed capital programme. This would be a significant departure from recent States practice but the Treasury and Resources Department is confident that this is the most appropriate way forward.

Nevertheless, the Policy Council is concerned that there is no over-arching States policy to guide Members and believes that such a framework should be in place prior to consideration of the Capital Prioritisation Report. Therefore, it has requested its Fiscal and Economic Policy Group to compile a formal fiscal policy framework to be proposed by the Policy Council for consideration by the States at its April 2009 meeting. This framework is intended to maintain a conservative fiscal policy and encompass issues such as long-term budgetary balance and prudent financing, including borrowing to fund States expenditure.

Therefore, whilst this Report is published at the same time as the March 2009 Billet, it is not for debate until May 2009. This will allow ample time for States Members to review and reflect on the complex, wide-ranging and strategically important issues detailed in this Report.

The Treasury and Resources Department is confident that the proposals contained within this Report will be compliant with any likely parameters specified within the fiscal policy framework. However, amendment(s) to the recommendations in this Report would be placed in the event that they conflict with the approved fiscal policy framework.

## 1. Executive Summary

The purpose of this Report is to recommend a programme of capital projects that the Treasury and Resources Department considers should be the highest priority for the four year period up to 2013 based on the results of the Strategic Review process to which each capital proposal has been subjected.

The Treasury and Resources Department is recommending that the capital programme should include all projects that have been assessed as Priority 1 under the strategic review process. This programme is estimated to cost £301million and will be funded from the Capital Reserve (anticipated to have £140-£150million available over the period of this States Assembly) and borrowing of £175million.

The recommended capital programme includes projects relating to the Ports (Airport and Harbours) as the Ports Holding Account is not able to fund the major capital expenditure that is proposed. It is therefore being recommended that the Ports Holding Account is closed and that, from 2010 onwards, major capital projects for the Airport and Harbours are subjected to the same processes as all other capital projects funded from the Capital Reserve.

It is also recommended that the States of Guernsey issues government bonds of £175million, with a fixed coupon (interest rate), repayable in twenty years with the States establishing a Sinking Fund to accumulate the redemption amount (see Section 8).

In the Department's view, the recommended capital programme is sustainable in meeting the needs of the present without compromising the ability of future generations to meet their own needs.

This Report also sets out the estimated structural revenue deficit arising from the implementation of the Economic and Taxation Strategy (Zero-Ten) and global economic circumstances and outlines some measures (both income raising and expenditure reductions) that could be introduced to address this funding gap. There will be some difficult decisions to be made in the near future.

## 2. Introduction

As outlined in Billet d'Etat XX of December 2008, this Report addresses the following main areas: -

- An explanation of the Strategic Review process (see Section 4).

- A standard summary of each project, detailing the proposal, cost (capital and revenue implications) and timing, together with the priority ranking it has been allocated (see Appendix C).

- A recommended capital programme (see Section 6) which requires funding from the Capital Reserve and through borrowing which would be repaid from the annual appropriation from General Revenue over the project's anticipated lifetime.

- An analysis of economic conditions including the possible impact on the local economy in delivering the capital programme, in particular the use of on and off island resources. It also addresses the benefit of supporting the local economy by undertaking capital expenditure during any period of recession and securing best value for money in what may be difficult market conditions.

- A consideration of the possibility of strategic partnerships with the private sector to deliver States capital projects.

- A recommendation of the level and source of borrowing that is necessary to finance the States capital programme and how it would be repaid and the consequential impact on States finances.

In addition, this Report reviews the States revenue budget position following the introduction in 2008 of the Economic and Taxation Strategy (Zero-Ten) and the direction of the Government Business Plan. The first stage of the Economic and Taxation Strategy includes:

- Measures to promote economic growth.

- A shift from corporate tax to income tax from individuals (mainly ETI receipts).

- Public Sector expenditure restraint.

- Increases in indirect taxes.

- Increased collections from social security contributions.

- If required, use of up to half of the Contingency Reserve Fund.

It was intended that Stage Two would come into effect between 2011 and 2013 with the actual measures necessary dependent on the level of success achieved by the measures introduced in Stage One.

The Strategic Economic Plan includes the objectives of *"using the total value of income to individuals from remuneration and other sources as the prime reflection of economic* *performance"* and *"pursuing policies to achieve 3% growth per annum in the total value of income to individuals from remuneration and other sources."*

The Government Business Plan includes the objectives of containing increases in revenue expenditure to RPI or less and to invest £20million per year in capital expenditure.

**3. <u>Background</u>**

In the November 2007 Budget Report, it was stated that *"During the latter part of 2008, a further capital prioritisation process will be undertaken which will identify those projects which should be progressed during the period up to 2012 (i.e. during the life of the next House)".*

Due to the complexity of this task, the Treasury and Resources Department has had to delay the presentation of its Report on capital prioritisation. It was also considered to be essential that every States Department had sufficient time to determine their capital (and other) priorities and to subject those capital proposals to the strategic review process. In December 2008, the States noted a Report that outlined the structure of this Report and set out the process that the Department intended to facilitate for ensuring that all States Members were fully informed and engaged in the process leading up to the debate on this Report.

**The 2006 capital prioritisation process**

The October 2006 capital prioritisation process was a simple allocation of Capital Reserve Funds to General Revenue projects for the period up to 2009.

The following major projects were prioritised in October 2006 and votes totalling £54.5million have been approved:

| | |
|---|---|
| Clinical Block | £36.1m |
| Medical Patient Records and CT Scanner | £3.9m |
| Sewer Network Extension to Creux Mahie (final tranches of funding) | £4.0m |
| Alderney Commercial Quay | £6.0m |
| Belle Greve Wastewater Disposal Facility (first phases) | £4.5m |

**Capital Expenditure since 2000**

Since 2000, States capital expenditure on major projects has totalled in the region of £350million including approximately:

- £90million by the Education Department,
- £60million by the Health and Social Services Department (with a further £15million in open capital votes),
- £58million transferred to the Corporate Housing Programme Fund (of which

£31million has been granted to Housing Associations and approximately £12million expended on capital works to States Housing),

- £23million on the Sewer Network Extension Plan,
- £20million on the Courts extension, refurbishment and essential maintenance.
- £47million by the Ports including £26million on the Airport Terminal Redevelopment and £14million on the St Peter Port Harbour New Jetty structural refurbishment.

## 4. The Strategic Review Process

Departments are given, as part of their Cash Limit, an allocation to prioritise and fund 'routine' capital expenditure (i.e. replacement of essential equipment, maintenance and repairs/upgrades to buildings and IT projects) and, with few exceptions, capital votes funded from routine capital allocations can be approved by individual Departments or the Treasury and Resources Department. Any other capital expenditure requires approval by the States and is funded by transfer from the Capital Reserve. Therefore, as part of the capital prioritisation process, Departments have submitted for strategic review, capital proposals costing in excess of £250,000 which cannot be funded from their routine capital allocations.

All capital proposal submissions have been subjected to the recently introduced rigorous and objective strategic review process to assist the Treasury and Resources Department in giving direction to the States on the relative merits of each proposal. Individual proposals are reviewed and scored, on behalf of the Treasury and Resources Department, by a cross-Departmental panel of three senior civil servants. **Appendix B** is the code of practice for Strategic Review of Capital Expenditure Proposals.

Approximately 30 proposals costing in the region of £370million have been submitted for strategic review (including some that are intended to be self-funding through fees and charges). The reasons for these capital proposals are varied including increases in public expectation, legislative requirements, technological advances, demographic changes and the life-expiry of existing facilities.

The strategic review process is designed to be a consistent and transparent method of assessing the relative merits of a large number of diverse capital proposals including construction, Information and Communication Technology and major equipment purchases. The eight criteria headings under which proposals are reviewed are:

- Mandate/Policy Delivery including
    - o Interaction with Government Business Plan.
- Economic Sensitivity including
    - o Effect on local economy – employment, income stream, etc.

    - Potential for rationalisation of States property portfolio.

- Community Sensitivity including
    - Effect on community if the proposal is/isn't carried out.
    - Potential for this proposal to be delivered by or in partnership with the private sector.
- Financial Sensitivity including
    - Capital cost and the ongoing revenue funding requirement for the lifespan of the project.
    - Cost per service recipient.
    - Costs of not proceeding with the proposal.
- Resource Sensitivity including
    - Capacity of the local business community to supply labour, plant and materials.
- Heritage and Cultural Impact.
- Programme Sensitivity including
    - Effect of any delay to the proposal.
    - Inter-relationship with any other projects – public or private sector.
- Other Risks which will be project-specific.

All of the capital proposals have been allocated a priority ranking as follows:

- Priority 1 – Recommended for inclusion in the capital programme for the current prioritisation period.
- Priority 2 – Recommended for inclusion in the capital programme but not necessarily in this prioritisation period.
- Priority 3 – Not recommended for inclusion in the capital programme.

Proposals which are assessed as Priority 1 display some or all of the following attributes:

- Benefit substantial parts of the community in a significant way.
- Represent value for money (including whole life costing).

- Appropriate time to undertake project (i.e. economic and commercial considerations as well as need).

- Add to or significantly enhance the Island's Infrastructure for the long term.

- Add to the Bailiwick's heritage (i.e. quality of project, sustainability, environmental impact, etc.).

**Appendix C** summarises each proposal including details of the proposal, cost (capital and revenue implications) and timing together with the priority ranking it has been allocated.

Reports containing extensive details of three of the proposals for major capital expenditure which would require full funding from the Capital Reserve have been submitted to the States for noting.

The three proposals are: -

- December 2008 Billet d'Etat XVIII – the Public Services Department's Report on Guernsey Airport's Pavements Rehabilitation project,

- January 2009 Billet d'Etat II – the Health and Social Services Department's Report on Adult Mental Health Facilities and

- February 2009 Billet d'Etat VII - the Education Department's Report on the Rebuilding of Les Beaucamps School.

These Departments have also arranged presentations for all States Members.

In respect of all other capital proposals that have been submitted for prioritisation, the Treasury and Resources Department has facilitated a series of five presentations for the respective Departments to present their plans to States Members.

The Treasury and Resources Department has also arranged a separate presentation for States Members in March to explain: -

- Details of the strategic review process through which each project has been put.

- The issues associated with entering into strategic partnerships with the private sector to deliver States capital projects.

- The recommended capital programme.

- The available routes for any necessary borrowing.

The Treasury and Resources Department intends to review and improve the strategic review process to be used for assessing all future proposals for inclusion in the capital programme. Furthermore, all Departmental routine capital allocations will be reviewed to ensure that they are set at an appropriate level to fund routine capital expenditure with all strategic developments and large-scale replacement programmes being assessed for funding through the strategic review process.

## 5. Capital Reserve

The Government Business Plan (Priority 3) includes a requirement to *"Invest £20m per year in capital expenditure'*. It is assumed that this amount, maintained in real terms at 2009 values (ie increasing annually in line with RPI), will be transferred to the Capital Reserve for the four years 2009 – 2012. In addition, as it is recommended that Ports projects are funded from the Capital Reserve, it is also recommended that the operating surpluses of the Ports which are anticipated to be £3million per annum (see Section 13) are, with effect from 2010, transferred to the Capital Reserve.

Therefore, the anticipated total amount available from the Capital Reserve for the period up to 31 December 2012 is a minimum of £160million*:

| | £m | £m |
|---|---|---|
| Balance at 31 December 2008 | | 42 |
| 2009 Appropriation | 20 | |
| 2010 Appropriation | 24 | |
| 2011 Appropriation | 25 | |
| 2012 Appropriation | 26 | |
| | | 95 |
| Other Income (including receipts from property sales and interest) | | 23 |
| Total funding available up to 31 December 2012 | | 160 |

* It is currently anticipated that the 2008 operating surplus will be some £30million better than estimated, mainly arising from one-off income tax receipts relating to banks and companies for years of charge prior to 2008. However, this is subject to finalisation and external audit of the 2008 Accounts. The Treasury and Resources Department will include a recommendation for appropriation of any surplus funds to either the Capital Reserve or Contingency Reserve Fund in the 2010 Budget Report.

Up to £20million will be retained in the Capital Reserve to fund any unanticipated projects (emergency or strategic opportunities), lower-value minor projects which cannot be funded from Departments' routine capital allocations but where the details and costings are not yet sufficiently developed to be subjected to strategic review and any variations in budgeted cost that occur prior to the project being approved by the States. All proposals should be subject to the strategic review process before an approach to the States for funding is made.

**Therefore, it is anticipated that the Capital Reserve will have funding of £140 - £150million to part-fund the capital programme although this would rise to as much as £180million should the entirety of any additional 2008 operating surplus be appropriated to the Capital Reserve.**

## 6. Capital Programmes

The Treasury and Resources Department has modelled a number of permutations of capital proposals and three programmes are detailed below.

The only project assessed as priority one or priority two which is intended to be self-funded through an existing or new income stream (fees and charges) is the Solid Waste Solution. This project will have a borrowing requirement to finance the initial capital cost which would be repaid over the project lifetime. All three programmes include the Solid Waste Solution (at a cost of up to £80million) as it is assumed that charges are increased from the current £3.6million per annum to the level necessary to service the borrowing (approximately £5.0million per annum maintained in real terms).

The Wastewater Treatment Plant is not included in these programmes as, although the investigatory and preliminary works will be undertaken during the term of this States Assembly (and funded through the anticipated surcharge to the Wastewater Charge), the Plant would be a project for the next States Assembly to consider.

**Programme A**

This programme funds all of the proposals that have been assessed as Priority 1 or Priority 2 and is estimated to cost £373million.

| Proposal | Best Estimate £'000 | Cumulative Cost £'000 |
|---|---|---|
| **PRIORITY 1** | | |
| Education – College of Further Education Phase 2b | 2,700 | 2,700 |
| Education – Les Beaucamps School | 38,150 | 40,850 |
| Environment – Cobo Bay Bunker/Sea Wall Repair | 350 | 41,200 |
| HSSD – Adult Acute Mental Health Facilities | 25,400 | 66,600 |
| HSSD – Homes for Adults with a Learning Disability | 5,300 | 71,900 |
| Home – eBorders IT system | 1,000 | 72,900 |
| Home – Police core IT system | 1,200 | 74,100 |
| Home – Tetra Radio | 1,800 | 75,900 |
| PSD – Belle Greve Wastewater Disposal Facility | 15,500 | 91,400 |
| PSD – Solid Waste Solution | 80,000 | 171,400 |
| Ports – Airport Pavements | 84,500 | 255,900 |
| Ports – Airport Radar | 2,400 | 258,300 |
| Ports – St Peter Port Harbour Crane Strategy | 10,000 | 268,300 |
| Ports – St Peter Port Harbour Pontoons | 1,000 | 269,300 |
| Ports – Sarnia Work Boat | 1,000 | 270,300 |
| Social Security/Income Tax IT System | 5,500 | 275,800 |

| | | |
|---|---:|---:|
| T&R - Cabernet Limited Recapitalisation | 6,000 | 281,800 |
| T&R – Corporate Asset Management IT System | 600 | 282,400 |
| T&R – IT Wide Area Network | 3,600 | 286,000 |
| Inflation Allowance | 15,000 | 301,000 |
| **SUB-TOTAL (PRIORITY 1 PROPOSALS)** | | **£301,000** |
| **PRIORITY 2** | | |
| Culture & Leisure – Museums Store | 5,000 | 5,000 |
| Environment – Val des Terres Rockface | 200 | 5,200 |
| HSSD – Giffard Ward (Princess Elizabeth Hospital) | 500 | 5,700 |
| Home – Redevelopment of Maison Celine | 15,000 | 20,700 |
| PSD – Cobo Foul Water Pumping Station | 1,000 | 21,700 |
| PSD – Permanent Civic Amenity Site | 1,200 | 22,900 |
| PSD – Sewer Network Extension Plan | 20,000 | 42,900 |
| Ports – St Peter Port Harbour Careening Hard | 23,000 | 65,900 |
| Treasury & Resources – Corporate SAP Initiatives | 2,100 | 68,000 |
| Inflation Allowance | 4,000 | 72,000 |
| **SUB TOTAL (PRIORITY 2 PROPOSALS)** | | **72,000** |
| **TOTAL** | | **373,000** |

The Treasury and Resources Department is **not** recommending that this programme is approved because it would necessitate borrowing of approximately £250million; the servicing of which would require approximately £19million of the £23million annual appropriation to the Capital Reserve for the next twenty years. This would severely limit the flexibility of future States Assemblies to determine their own capital priorities as projects could only be funded by increasing the annual appropriation to the Capital Reserve or issuing further debt.

A portion of the annual transfers to the Capital Reserve during the period 2009 – 2012 would be required to service the borrowing, thus reducing the £160million of funding available from the Capital Reserve (Section 5) to part-fund this capital programme.

**Programme B**

This programme would use only the funding available within the Capital Reserve - £140 - £150million plus the Solid Waste Solution (£80million).

| Proposal (all Priority 1) | Best Estimate £'000 | Cumulative Cost £'000 |
|---|---:|---:|
| Education – Les Beaucamps School | 38,150 | 38,150 |
| PSD – Belle Greve Wastewater Disposal Facility | 15,500 | 53,650 |
| PSD – Solid Waste Solution | 80,000 | 133,650 |
| Ports – Airport Pavements | 84,500 | 218,150 |
| Inflation Allowance | 10,000 | 228,150 |
| **TOTAL** | | **228,150** |

This programme would mean that the following priority one proposals (totalling £72,850,000) including the Ports – St Peter Port Harbour Crane Strategy project which was approved by the States in 2008 could not be progressed during this prioritisation period:

| | **Best Estimate £'000** |
|---|---:|
| Education – College of Further Education Phase 2b | 2,700 |
| Environment - Cobo Bay Bunker/Sea Wall Repair | 350 |
| HSSD – Adult Acute Mental Health Facilities | 25,400 |
| HSSD – Homes for Adults with a Learning Disability | 5,300 |
| Home – eBorders IT system | 1,000 |
| Home – Police core IT system | 1,200 |
| Home – Tetra Radio | 1,800 |
| Ports – Airport Radar | 2,400 |
| Ports – St Peter Port Harbour Crane Strategy | 10,000 |
| Ports – St Peter Port Harbour Pontoons | 1,000 |
| Ports – Sarnia Work Boat | 1,000 |
| Social Security/Income Tax IT System | 5,500 |
| T&R - Cabernet Limited Recapitalisation | 6,000 |
| T&R – Corporate Asset Management IT System | 600 |
| T&R – IT Wide Area Network | 3,600 |
| Inflation Allowance | 5,000 |

Variations on this programme could be to exclude just the Airport Pavements Project giving a programme cost of approximately £210million or to just prioritise the three highest value projects - Airport Pavements, Les Beaucamps School and Adult Acute Mental Health Facilities giving a programme cost of approximately £240million.

If the anticipated 2008 additional operating surplus of approximately £30million is appropriated to the Capital Reserve, it will be possible to do more, but not all, of the priority one proposals.

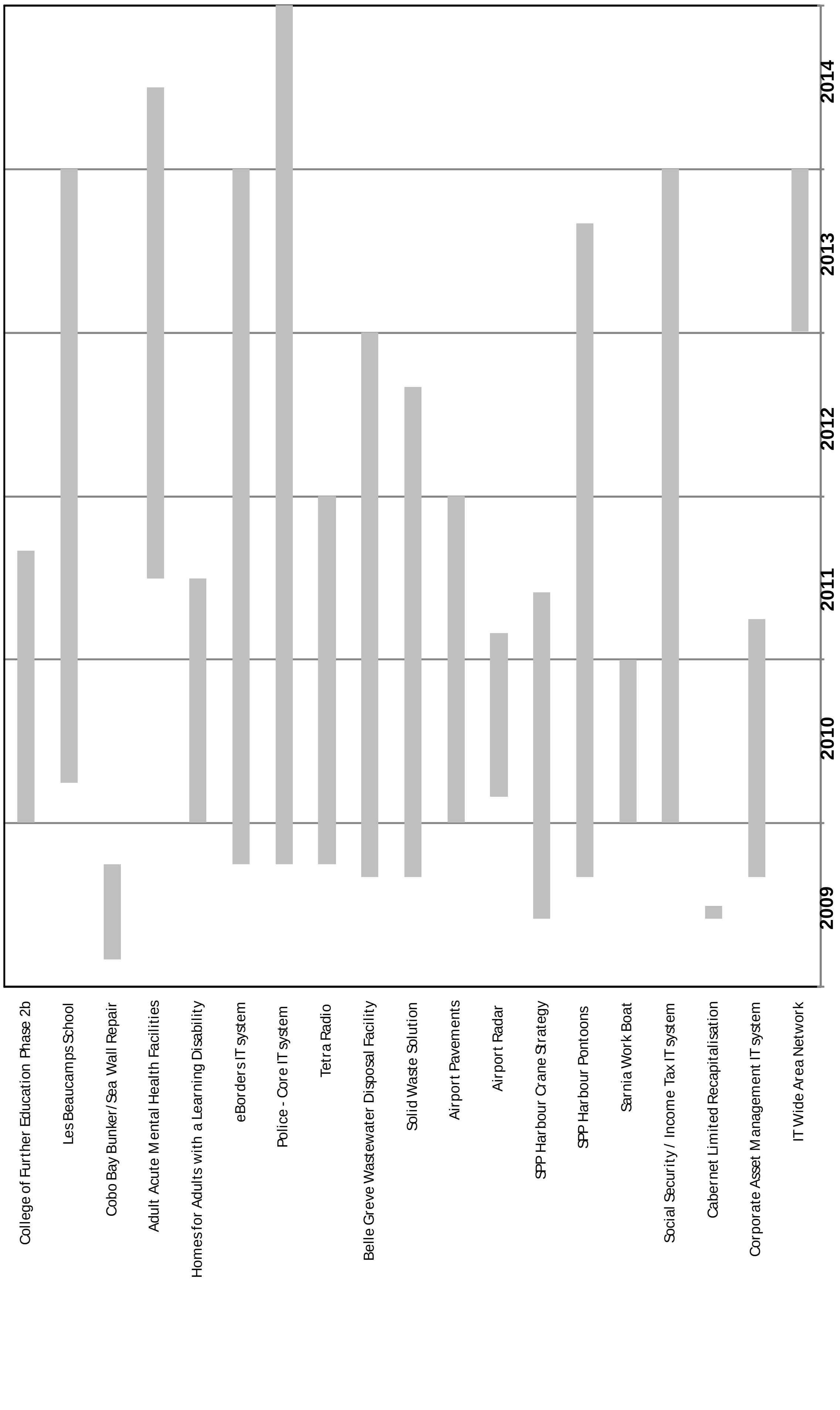
The Treasury and Resources Department is **not** recommending a capital programme using only funding available from the Capital Reserve (plus a self-funding Solid Waste Solution) as it is firmly of the opinion that all Projects that have been assessed as Priority 1 should be progressed without delay.

**Programme C (Recommended Capital Programme)**

The Treasury and Resources Department is recommending that funding for the following capital programme, which includes all of the proposals that have been categorised as Priority 1, is allocated during the term of this Assembly:

| Proposal | Best Estimate £'000 | Cumulative Cost £'000 |
|---|---|---|
| **PRIORITY 1** | | |
| Education – College of Further Education Phase 2b | 2,700 | 2,700 |
| Education – Les Beaucamps School | 38,150 | 40,850 |
| Environment - Cobo Bay Bunker/Sea Wall Repair | 350 | 41,200 |
| HSSD – Adult Acute Mental Health Facilities | 25,400 | 66,600 |
| HSSD – Homes for Adults with a Learning Disability | 5,300 | 71,900 |
| Home – eBorders IT system | 1,000 | 72,900 |
| Home – Police core IT system | 1,200 | 74,100 |
| Home – Tetra Radio | 1,800 | 75,900 |
| PSD – Belle Greve Wastewater Disposal Facility | 15,500 | 91,400 |
| PSD – Solid Waste Solution | 80,000 | 171,400 |
| Ports – Airport Pavements | 84,500 | 255,900 |
| Ports – Airport Radar | 2,400 | 258,300 |
| Ports – St Peter Port Harbour Crane Strategy | 10,000 | 268,300 |
| Ports – St Peter Port Harbour Pontoons | 1,000 | 269,300 |
| Ports – Sarnia Work Boat | 1,000 | 270,300 |
| Social Security/Income Tax IT System | 5,500 | 275,800 |
| T&R - Cabernet Limited Recapitalisation | 6,000 | 281,800 |
| T&R – Corporate Asset Management IT System | 600 | 282,400 |
| T&R – IT Wide Area Network | 3,600 | 286,000 |
| **SUB-TOTAL (before Inflation Allowance)** | | **286,000** |
| Inflation Allowance | 15,000 | 301,000 |
| **TOTAL** | | **301,000** |

Following is the timeline for the recommended programme:



College of Further Education Phase 2b
Les Beaucamps School
Cobo Bay Bunker/Sea Wall Repair
Adult Acute Mental Health Facilities
Homes for Adults with a Learning Disability
eBorders IT system
Police - Core IT system
Tetra Radio
Belle Greve Wastewater Disposal Facility
Solid Waste Solution
Airport Pavements
Airport Radar
SPP Harbour Crane Strategy
SPP Harbour Pontoons
Sarnia Work Boat
Social Security / Income Tax IT system
Cabernet Limited Recapitalisation
Corporate Asset Management IT system
IT Wide Area Network
2009
2010
2011
2012
2013
2014

## 7. Funding the Recommended Programme

In order to fund the recommended capital programme, two sources have been identified. Firstly, a transfer from the Contingency Reserve Fund could be made. However, assuming that the Solid Waste solution is self-funding, there would need to be a withdrawal of approximately £80million which would virtually exhaust the available balance of the Fund.

The Contingency Reserve Fund was established in 1986 with the purpose of providing protection against major emergencies including significant economic downturns having a severe adverse effect on the Island. The original target was a balance equivalent to 50% of annual revenue expenditure but this was revised to 100% in the 1997 Budget (with a high of 78% attained in 2007). The Treasury and Resources Department is of the view that it is of strategic importance that a significant balance continues to be maintained in this Fund.

Therefore, it is recommended that the capital programme is financed through a combination of the balance of the Capital Reserve and from borrowing of £175million (approximately 8.8% of 2007 GDP). It should be noted that any significant variations to these projects (eg an extension to the Airport Runway) would necessitate an increase in the borrowing requirement.

In the knowledge that bids for capital investment were likely to be substantial in this States term, in Autumn 2008 the Treasury and Resources Department decided to seek external and independent advice on exploring funding options for the States' medium term capital investment requirements in order to give Members comprehensive information on the options available. Following a selective tendering process, NM Rothschild & Son Ltd (Rothschild) was appointed as independent advisor. The brief was not only to advise on the funding options available, but also to assess what any borrowing requirement might be and the likely timings of drawdown. The Rothschild team has worked closely with the Treasury and Resources Department in order to develop a detailed model including:

- Income and expenditure projections for the next ten years based on historical performance and economic forecasts.

- Detailed cash flows for the capital proposals submitted including allowances for inflation.

- The establishment of a Sinking Fund to repay the principal on any borrowing.

- Forecasts for the significant reserves (Contingency Reserve Fund and Capital Reserve).

- Debt issue indicative pricing received from selected banks on a confidential basis.

- The requirement for future revenue raising to cover the structural deficit.

Scenarios were developed in order to model the impact of undertaking all priority 1 and 2 proposals and the recommended programme. In addition to the 'base case' which is the scenario deriving from the baseline modelling assumptions, two further scenarios have been modelled using positive and negative variations in the forecast assumptions (upside and downside) to demonstrate the sensitivity of the model.

**Appendix D is the Rothschild's report.**

As modelled in the base case, to fund the recommended capital programme, there is an expected borrowing requirement of £175million (including £80million in respect of the 'self-funding' Solid Waste Solution). In order to repay this borrowing over a period of twenty years through the recommended sinking fund mechanism, the annual commitment would be £15million (including the assumed £5million of income from the Solid Waste Solution). Therefore, the £23million (at 2009 values) annual transfer to the Capital Reserve would reduce to approximately £13million per annum.

It is likely that all Priority 2 proposals will seek funding during the next States term, together with future phases of the Education Development Plan (La Mare de Carteret School, etc), Wastewater Treatment Plant and other proposals currently in the initial development phase. If borrowing is progressed, funding for these proposals would either:

(i) be limited to £13million per annum,

(ii) require an increase in the annual transfer to the Capital Reserve,

(iii) necessitate additional borrowing, and/or use of the proposed Sinking Fund.

Therefore, if several major capital projects are to be progressed during subsequent States Assemblies there will be a requirement to provide additional funding to the Capital Reserve – either by transfer from annual operating surpluses (met by increasing revenue income or reducing public sector expenditure) or by extending/increasing the debt raised.

## 8. <u>Borrowing Options</u>

The States of Guernsey have borrowed on a number of occasions over the last century, for both general purposes (eg. £550,040 - 2.75% General Purposes Loan issued in 1947) and for specific projects including by the Water Board (eg. £25,000 – 3.25% Loan issued in 1935) and the Ports. In recent years, States practice has been to only borrow where there is an associated income stream – eg to fund Housing loans and nursing staff accommodation.

The Treasury and Resources Department has taken advice on, and considered a number of, options for raising funds to finance the recommended capital programme, before deciding to recommend a bond issue. The Department was keen to examine all possible and practical solutions with a view to finding the most appropriate solution for the island.

The key requirements of any debt solution were that it minimised overall cost, and remained simple and flexible. Some of the forms of debt examined were:

- Bank Finance

  Banks make loans to governments in the same way as they lend to businesses, providing there is a strong business case for projects financed by the loan and the government has a good credit rating. This can be extremely flexible since funds can be drawn as needed but, in the current market, duration is unlikely to exceed five years and interest rates and charges are expected to be higher than other forms of financing.

- Public Bond Issue

  A bond issue attracts loans of different amounts from institutional and substantial private investors. It pays investors a fixed rate of interest and is repayable (redeemable) at a fixed date after issue (usually between 10 and 40 years). That repayment can be made by the lender (in this case the States of Guernsey) building up a reserve (called a Sinking Fund) to cover the cost of repayment when it is due. A public sterling bond issue could be offered at a low rate of interest and attract limited set-up costs given the government's AAA credit rating. Once issued, bonds may be bought and sold by investors in the financial markets. A government bond issue of in excess of £100million is generally more attractive because of increased market liquidity and some institutional investors' internal policies which may stipulate a minimum holding value and limit their percentage exposure to an individual issue.

- Private Placement Bonds

  These operate in a similar way to a public bond issue except that the bonds are not generally offered to the public or traded in the secondary market and some investors may not require a government to have a particular credit rating. Whilst there may be a premium to be paid in interest rates and charges, the costs associated with private placements are broadly comparable with public bond issue if the government has a favourable credit rating.

- Project Finance

  Limited borrowing can be secured for individual projects with each loan being offered and set up separately with clear evidence that the costs and revenues (if any) of each project are ring-fenced. This involves significant administrative costs and loans of this kind in the current market attract relatively high interest rates and charges.

The Department has also considered internal borrowing as part of the process. The States operates a General Revenue Cash Pool (includes General Revenue reserves and working balances and deposits from States Trading Undertakings, associated entities and a small number of charities and other organisations with a historic association with the States) which has in the region of £250million and has been used in the past to finance internal borrowings and overdrafts. The main advantage of funding from this source is that the rates charged are low relative to the market. However, the rate of interest paid will fluctuate with the market and therefore offers no certainty. It is estimated that the cash pool could be used to fund projects of up to £100million as there is a need to retain sufficient liquidity within the Cash Pool for the States and associated entities. This option would not remove the requirement to utilise external borrowing to fund the recommended capital programme.

A number of sources of funding have therefore been examined and modelled by the Department and it seems likely that the most efficient form of borrowing will be to issue a Guernsey government bond to raise the full amount required to fund the recommended capital programme over and above any Reserves used for that purpose.

However, it should be recognised that an issue of £175million is at the low end of benchmark bond issues, and it may be more effective to consider a private placement. Therefore, it is the Department's recommendation that borrowing of up to £175million be approved with the timing and method of borrowing to be finalised by the Treasury and Resources Department.

It became apparent early in the process that, in order to access the lowest cost debt, a formal rating would be beneficial. The Department decided to seek a rating from Standard & Poor's (S&P), who are one of the leading agencies for sovereign ratings. **In January 2009, S&P confirmed that Guernsey had been awarded a AAA long-term and A-1+ short-term, the highest ratings available which place Guernsey in the top 25 rated jurisdictions in the world. The recently published S&P release is included as Appendix E and a more detailed research update will be published by them in the coming weeks.**

Another key consideration in any debt issuance will be timing. Borrowing is possible at any time but it may be beneficial to borrow ahead of the actual funding requirements whilst interest rates and gilt yields are low (pre-funding). This carries some risk in that for a period of time there may be a difference between the interest to be paid on that funding and the interest received on deposits (negative carry). However, long-term savings on the costs of capital should outweigh these short-term costs. When the Rothschild's Report was compiled, a debt interest rate of 5.25% was assumed – a 0.1% variation equates to £3.5million over the twenty year period.

The markets are extremely volatile at present and although gilt yields (investment return on UK Government Bonds) are currently comparatively low, these are expected to rise as the UK Government issues debt to cover its policies of fiscal stimuli and bank rescue packages. Should the States agree to a bond issue, the Treasury and Resources Department will need to work very closely with its advisors, Rothschild, in order to determine the most appropriate and cost effective timing.

The Treasury and Resources Department is also recommending that a Sinking Fund be established in order to accumulate the principal for repayment over the term of any borrowings. This will mean that an amount will be transferred to the Sinking Fund each year, which will grow in real terms, to enable the bond or loan to be repaid at the end of the period without the States encountering any refinancing risk. **This is a prudent way of saving for repayment and the fund will also accumulate interest over the period.**

Although the various Superannuation Fund investment managers will consider holding bonds issued by the States of Guernsey within their portfolios, their guidelines and strategy will preclude the entire issue being held by the Fund.

## 9. Ongoing States Financial Position

The 2009 Budget Report stated that there is anticipated to be an ongoing shortfall (structural deficit) of £35-40million in States Finances after taking into account the annual appropriation to the Capital Reserve. However, the funding model devised by Rothschild (and using the assumptions contained therein) projects that this shortfall could increase to approximately £60-65million in the event that downside economic forecasts for the coming years are realised (eg for 2009 there is, based on UK economic trends and forecasts, expected to be negative growth in the economy of 2.7%, compared to the long-term positive growth target of 3%). This shortfall is not a result of borrowing to fund the capital programme (which is reducing the amount of capital available for investment in future years).

In June 2006, the States resolved that up to half of the Contingency Reserve Fund (interest and capital) may be used to fund the shortfall in public sector expenditure during a transitional phase (up to 2011/2013) of the implementation of the Economic and Taxation Strategy. As at 31 December 2008, there was approximately £118million available to be used in the transitional phase which will only fully fund two years of anticipated deficits (2009 and 2010).

Therefore, Stage Two of the Economic and Taxation Strategy will require measures that will either increase States income and/or reduce expenditure. The Strategy seeks to sustain Guernsey's competitive economic position, whilst generating sufficient income to ensure that Guernsey maintains an acceptable level of essential public services and infrastructure. The Rothschild's model projects that additional income/reduced expenditure of £52million per annum from 2011 coupled with use of half of the Contingency Reserve Fund could be necessary to achieve a balanced budget by 2017.

It is the intention of the Treasury and Resources Department, in conjunction with the Policy Council's Fiscal and Economic Policy Group, to investigate, model and cost a number of options for consideration by the States. There are, of course, a number of permutations of measures (some of which may be considered politically unacceptable) that could be implemented including (but not limited to) the following:

- An ongoing real terms reduction in States expenditure - a 2% cut would equate to approximately £6million.

- Reducing or eliminating the States Grant to the Social Security Funds (£17million in 2009).

- Reducing or phasing out Income Tax relief for mortgage interest which currently costs £12-15million per annum.

- An increase in Excise Duties - an 'across the board' increase of 20% would raise £5-6million per annum or targeted increases – a 20p increase in motor spirit duty would raise approximately £7million per annum.

- Increasing Tax on Rateable Values tariffs – a straightforward doubling of the existing tariffs would raise £12million per annum.

- Increasing the Document Duty rate – based on the 2007 values, an increase from 3% to 4% would raise approximately £5million per annum.

- Transferring the annual interest on the Contingency Reserve Fund (approximately £6million) to General Revenue.

- Increasing the basic rate of Income Tax – a 1% increase to 21% would raise approximately £10million per annum.

- Revisions to the corporate Income Tax system.

- Introducing a higher-rate Income Tax band.

- Introducing a Goods and Services Tax - it has previously been estimated that a similar tax to that introduced in Jersey would raise in the region of £40million per annum.

It is recognised that it is unlikely that such a significant deficit could be eliminated in one year without having a serious effect on the local economy. Therefore, it is anticipated that any necessary measures would be implemented over a number of years with the shortfall being funded from the Contingency Reserve Fund.

However, as set out in the Rothschild's report, it will be necessary for measures intended to reduce the structural deficit to be introduced as soon as possible as any delay will impact on the ability of the Contingency Reserve Fund to fund the resulting shortfall.

## 10. Economic Conditions

### Value for Money

The use of public sector spending to stimulate aggregate demand in an economy (the so called 'Keynesian boost') is an established tool used to shift economies out of slumps by using public investment and employment to provide a stimulus to demand. The benefits are that employment and income would not just be provided to the workers engaged directly on public programmes but their spending on other goods and services would then multiply through the economy many times.

Guernsey's economy has, in the past, proven to be more resilient and less volatile than the UK's economy, which is currently in recession. The outlook however is for somewhat subdued local conditions for the foreseeable future. Therefore, an increased level of capital spending commencing in the next 12 months or so could provide a timely 'assist' to the local economy.

Furthermore, the States should obtain keener prices and secure better value for money for its capital expenditure, as it will not be competing with private sector investment for limited capacity within the construction industry. However, the timing of any public sector investment has to be carefully planned and scheduled as too large and too immediate an increase would hit capacity constraints in the local construction industry feeding immediately through to higher prices and costs.

The Treasury and Resources Department believes that the recommended programme would have a positive impact on the local construction industry and economy with an appropriate mix of construction, civil engineering, equipment and ICT projects. The timing of any projects will be key and the Treasury and Resources Department will work closely with other States Departments and industry representatives to deliver an optimally beneficial programme.

**Impact on the Local Construction Industry**

Only a subset of the proposals in the recommended capital programme will draw on the resources available within the local construction industry as illustrated in the following table:

| Category | Number of Proposals | Proposed total investment £'000 | On island value £'000 | On island value % | Off island value £'000 |
|---|---|---|---|---|---|
| Building | 4 | £71,550 | £48,005 | 67.09% | £23,545 |
| Engineering | 5 | £190,350 | £66,515 | 34.94% | £123,835 |
| Equipment | 3 | £4,400 | £390 | 8.86% | £4,010 |
| Finance | 1 | £6,000 | £6,000 | 100.00% | - |
| IT | 6 | £13,700 | £865 | 6.31% | £12,835 |
| Inflation Allownce | - | £15,000 | £6,000 | 40.00% | £9,000 |
| Total | 19 | £301,000 | £127,775 | 42.45% | £173,225 |

Building → Traditional public, commercial and residential construction
Engineering → Works involving either marine, civil or major infrastructure engineering
Equipment → Proposals where the majority of the cost is related directely to equipment procurement
Finance → Proposals relating solely to financial management
IT → IT or telecommunications systems procurement

**Appendix F** analyses the individual proposals within the recommended capital programme between on-island and off-island value and categories of expenditure – building, engineering, equipment, finance and IT.

In order to assess the financial benefit of a proposal to the local construction industry the Treasury and Resources Department has consulted with industry representatives of the Construction Sector Group to establish a general assessment of the financial benefit likely to impact on the local industry as a percentage of the proposal value. To avoid undue bias, generic proposal types were considered and an additional weighting for local labour included at the request of the industry representatives.

As a principle, a greater local weighting is allocated to routine domestic residential construction, with lower weightings as the projects become larger in value and more complex, particularly when process plant and equipment form a large part of the proposal value.

It has not been possible to quantify the maximum value of work which the local construction industry can sustain notwithstanding that public projects only contribute in part to the well being of this industry sector. Instead, the timing of the programme of works will seek to avoid the 'boom & bust' scenarios for which the States have been criticised in the past and smooth out the peaks and reduce the troughs by managing project awards. This is a vital tool if the construction sector is to remain viable through times of uncertain workload.

The Commerce and Employment Department has advised that, in time for the debate on this Report, it will have a local construction industry endorsed view of the state of the local construction industry in these difficult economic times. Furthermore, in future, the Construction Sector Group intends to develop a more quantitative analysis tool.

**Impact on the Local Economy**

The proposals considered for capital prioritisation do not only impact on the construction industry. Invariably local hauliers and sea freight business will benefit from the works which will result from this process. For those proposals where there is a lower benefit to the local construction industry there will still be benefits in the local accommodation sector, with associated catering and entertainment spend benefiting the local economy. Once complete the proposals will have varying degrees of impact on the local economy dependent upon the intended function.

Not all the impacts are positive. Heavy road transport will cause the islands road network to deteriorate at an accelerated rate which will impact on future revenue expenditure. There is also a risk that the more specialist construction resources (labour and equipment) may be in short supply which will impact on the timing or cost of other projects. On a temporary basis works compounds will be required for the larger projects with an impact on local traffic flows and amenity.

## 11. <u>Strategic Partnerships with the Private Sector</u>

Strategic partnerships have become extremely popular in the public sector in the United Kingdom with government policy dictating that all significant projects are carried out under the private finance initiative. Traditionally, the public sector has attempted to "do everything" from setting policy frameworks to procurement and on to delivery of service. Strategic partnerships allow government to facilitate opportunities and then allow operations to be carried out by those better placed to deliver and obtain best value for money. An example of a successful local strategic partnership is that with the Guernsey Housing Association.

There are many forms of strategic partnership from working closely in public-private partnerships with local ‘not for profit’ organisations to full scale, design build finance and operate projects which see significant control transferred to the chosen private sector operator. The current proposals have been examined in order to assess whether the States might gain anything through pursuing a strategic partnership. The Wastewater treatment plant might, in the future, afford an opportunity to develop such a partnership.

**However, project finance is more expensive than conventional government borrowing and the credit crunch has meant that availability is limited and spreads have risen significantly meaning that this would not offer value for money in the current environment. Furthermore, the key requirements of any debt solution were that it minimised overall cost, and remained simple and flexible.**

One of the major benefits to be gained from strategic partnerships derives largely from the rigorous due diligence process which the private sector can bring to bear. The Treasury and Resources Department will now be facilitating this process on all future projects at the gateway review stage. Another key benefit is the allocation of risk to the party best suited to deal with it, which is something that the States is already doing quite effectively through its contract terms.

The assessment criteria within the strategic review process will be developed by the Treasury and Resources Department so that the possibility of strategic partnerships for future proposals can be assessed at an early stage.

## 12. <u>Next Steps</u>

The inclusion by the States of a proposal in the capital programme does not mean that the project is able to commence. Once it has been agreed by the States that a Department’s proposal is to be included within the programme for capital funding it should be treated as a project and managed following the Code of Practice guidance on “Gateway Review, Project Management and Post Implementation Review” issued by the Treasury and Resources Department.

The first step would be to establish a Project Board appropriately constituted for the project - for small straightforward projects this may comprise entirely of Officers. However, for larger and more complex projects, it should include political representatives from the sponsoring and Treasury and Resources Departments.

The Project Board would then compile a budget to cover design fees, investigations, surveys, enabling works, etc and the costs of conducting a tender exercise. The sponsoring Department would submit a request to the Treasury and Resources Department for approval of a budget to fund such preliminary expenditure. The release of funds to progress the project to tender stage will be subject to the project progressing satisfactorily through the three Gateway Reviews (business justification, strategic fit and achievability and award decision). These high-level Gateway Reviews are carried out before the key decisions are made in the procurement of a project and will provide assurance that the project continues to have merit and that it can be justified on a business need basis with an assessment of the likely costs, risks and potential for success compared to the original brief.

Therefore, it is recommended that the Treasury and Resources Department is given authority to approve capital votes for expenditure to be incurred on progressing to tender stage those projects that have been included in the capital programme, with such expenditure being funded by transfers from the Capital Reserve.

The outcome of the Gateway Review process will be used to inform the Treasury and Resources Department's Letter of Comment which will be appended to the Report produced by the sponsoring Department when seeking approval of a capital vote (which will include all of the preliminary costs) for a project. At this stage, States Members will be able to propose amendments to any aspect of a particular project.

There are a small number of projects where the Treasury and Resources Department has delegated authority to establish capital votes including those projects which have already been approved by the States (eg. Belle Greve Wastewater Disposal Facility) or for low value straightforward replacements/repairs (eg. Cobo Bay Bunker/Sea Wall Repairs).

## 13. Ports Accounting Arrangements

It is clear that the Ports Holding Account is unable to fund the cost of the Airport Pavements Project (£84.5million) and, even if a loan from General Revenue was advanced, the annual surpluses of the Ports would be insufficient to service it.

In addition to the Airport Pavements Project, there are four Ports proposals costing £14.4million which the Treasury and Resources Department is recommending are included in this term's capital programme and funded from the Capital Reserve.

Over the six year period 2002 to 2007, the annual operating surpluses of the Ports (before depreciation but including 'routine' capital expenditure) have totalled £20million and ranged between £3million and £3.5million. Therefore, for the purposes of this Report, the Rothschild's funding model has prudently assumed an annual transfer from the Ports of £3million which would be directly credited to the Capital Reserve.

The Public Services Department has commissioned the Office of Utility Regulation to conduct a cost/benefit and feasibility study to assess the merits of commercialising a number of the business activities including Guernsey Airport and Harbours. Discussions have also been held at both political and officer level with the Commerce and Employment Department and it has been established that, if commercialisation is found to be appropriate and politically acceptable, it would take a reasonable period of time to implement but not more than three years. In the meantime, it is recommended that the Ports Holding Account should be collapsed.

Further discussions will take place with the Public Services Department to determine the most appropriate short-term accounting arrangements for the Ports including a General Revenue 'Cash Limit' or the maintenance of a trading account making an annual contribution ('dividend') of £3million to the General Revenue Capital Reserve.

The 2010 Budget Report will include appropriate recommendations, pending the outcome of the commercialisation investigations.

## 14. Recommendations

The Treasury and Resources Department recommends the States to:

1. Approve the recommended programme for capital projects totalling £301million as set out in Programme C of Section 6 of this Report.

2. Note that each project that is included within the capital programme will be the subject of a separate Report before the project can commence unless the Treasury and Resources Department has delegated authority to approve a capital vote.

3. Authorise the Treasury and Resources Department to approve capital votes for expenditure on progressing to tender stage those projects that have been included in the capital programme, funded by transfers from the Capital Reserve.

4. Authorise the Treasury and Resources Department to transfer from the Capital Reserve such sums that are necessary to fund approved capital votes.

5. Authorise the Treasury and Resources Department to enter into a borrowing arrangement at the best available terms for a sum not to exceed £175million, repayable over a maximum period of 20 years.

6. Establish a Sinking Fund to accumulate annual transfers from the Capital Reserve such that, by the end of 20 years, the principal borrowed can be repaid in full.

7. Confirm that the Ports Holding Account should be collapsed and direct the Treasury and Resources Department, following consultation with the Public Services Department, to recommend in the annual Budget Report appropriate short and long term accounting arrangements.

Yours faithfully

C N K Parkinson
Minister

**[NB Deputy Domaille has significant reservations about the principle of borrowing where there is no associated income stream]**

**Appendix A**

# TREASURY AND RESOURCES DEPARTMENT

CAPITAL PRIORITISATION

The Chief Minister
Policy Council
Sir Charles Frossard House
La Charroterie
St Peter Port

14th November 2008

Dear Sir

## 1. Executive Summary

The purpose of this States Report is to set out the process that the Treasury and Resources Department intends to put in place between December and March 2009 when the States will debate and establish its capital priorities for this term. Importantly, the Department intends to ensure that all States Members are fully informed and engaged in the process leading up to the March debate.

This report also outlines the structure of the report that the Department will submit to the States in March on capital prioritisation. The March report will put forward recommendations on which projects the States should consider as the highest priority based on the results of the strategic review process to which each capital project will have been subjected. It will also address the possibility of strategic partnerships with the private sector to deliver States capital projects and include fully researched proposals on various borrowing options.

Finally, the March States Report will include information on the economic climate and other important considerations that have been taken into account by the Department in developing the capital programme (including timings) which will be recommended to the States.

## 2. Background

In the November 2007 Budget Report, it was stated that *"During the latter part of 2008, a further capital prioritisation process will be undertaken which will identify those projects which should be progressed during the period up to 2012 (i.e. during the life of the next House)"*.

Due to the complexity of this task, which will be evident from the remainder of this Report, the Treasury and Resources Department has had to delay the presentation of its

States Report on capital prioritisation which it now intends to submit for consideration at the March 2009 States Meeting.

The capital prioritisation process will not be a simple allocation of Capital Reserve Funds to General Revenue projects as was the case in 2006. Instead, it will also address: -

- The capital funding requirements of trading entities.
- The possibility of entering into strategic partnerships with the private sector.
- The issue of borrowing to enable more projects to be undertaken.
- The available routes for any borrowings.
- An analysis of the impact on the general economy, construction industry and States finances of progressing the top priorities.

All capital project submissions will have been subjected to the recently introduced rigorous and objective strategic review process (see below) to assist the Treasury and Resources Department in giving some direction to the States on the relative merits of each project.

In excess of 30 projects costing in the region of £400million have been submitted for strategic review although a significant proportion could be self-funding. The reasons for these capital projects are varied including increases in public expectation, legislative requirements, technological advances, demographic changes and the life-expiry of existing facilities.

## 3. <u>The process</u>

Prior to the States debate in March 2009 on capital prioritisation, the Treasury and Resources Department intends to put in place a process to assist States Members in being fully informed beforehand on the capital projects that have been submitted by Departments.

It is particularly important that States Members are provided with this necessary information in advance of the March debate particularly in relation to three of the major projects that have been submitted. The process that the Department intends to implement should also ensure that the debate in March on capital prioritisation is more focused.

It is therefore intended that the following **five-part** programme will be delivered: -

**Part 1**

Between December and February three major projects will be debated under Rule 12(4) of the States Rules of Procedure such that they are considered by the States without amendment. Members will however be able to debate the proposals and ask detailed and searching questions.

The three projects are: -

- December 2008 Billet d'Etat – the Public Services Department's report on Guernsey Airport's Pavements Rehabilitation project.

- January 2009 Billet d'Etat – the Health and Social Services Department's report on Mental Health Facilities,

- February 2009 Billet d'Etat - the Education Department's report on the Redevelopment of Les Beaucamps School.

**Part 2**

In respect of all other capital projects that have been submitted for prioritisation, the Treasury and Resources Department will facilitate a series of presentations during February where the respective Departments will be invited to present their proposals to States Members.

**Part 3**

The Treasury and Resources Department will also arrange separate presentations for States Members in February/March to explain: -

- Details of the strategic review process through which each project has been put.

- The issues associated with entering into strategic partnerships with the private sector to deliver States capital projects.

- The available routes for any necessary borrowing.

**Part 4 (States Report)**

Detailed summaries of all of the capital projects that have been submitted by Departments, including the three major ones mentioned above, will appear in the States Report on capital prioritisation. That report will be submitted by the Treasury and Resources Department for debate by the States in March 2009 and will enable the States to determine its capital priorities and its capital programme for the next four years.

At the same time, the States will also be asked to agree on the funding route(s) for the recommended capital programme. Of course, should the States decide not to enter into any borrowing arrangements then fewer projects (and especially those without income streams) will be capable of being progressed.

**Part 5**

Following the States debate in March on capital prioritisation, those projects that have been prioritised for funding by the States, **including** any/all of the three major projects mentioned above that the States decides to prioritise, will then each need to be the subject of a further report to the States. Those reports will include an appropriate level of detail together with the final costings and will seek States approval for a capital vote to be established (i.e. agreement for the funds to be released). At that stage, States Members will be able to propose amendments to any aspect of a particular project.

## 4. Structure of the March States Report

The Treasury and Resources Department's Report to the States on Capital Prioritisation will address seven main areas. It will: -

- Include an explanation of the Strategic Review process (see section 6 below).

- Include a standard summary of each project, detailing the proposal, cost (capital and revenue implications) and timing together with the priority ranking it has been allocated.

- Recommend a capital programme (see Section 5 below) which requires funding from General Revenue – either in whole or in part. These projects would be funded from the Capital Reserve, by a withdrawal from the Contingency Reserve Fund, by increased taxation or through borrowing which would be repaid from General Revenue over the project's anticipated lifetime.

- Recommend a schedule of capital projects which are self-funded through an existing or new income stream (fees and charges). These projects may have a borrowing requirement to finance the initial capital cost which would be repaid over the project lifetime.

- Consider the economic conditions – this will include analysing the possible impact on the local economy in delivering the capital programme, in particular the use of on and off island resources. Consideration will also be given to the benefit of supporting the local economy by undertaking capital expenditure during any period of recession and securing best value for money in what may be difficult market conditions.

- Address the possibility of strategic partnerships with the private sector to deliver States capital projects including private finance initiatives, public private partnerships and joint ventures.

- Address the issue of any borrowing that is necessary to finance the States capital programme including an analysis of how such borrowing could be sourced (conventional bank loan, bond issue, private placement, etc) and how it would be repaid and the consequential impact on States finances.

## 5. The Capital Programme

The Treasury and Resources Department will consider the outcome of all the strategic reviews and devise a capital programme for the period up to 30 April 2012 to be recommended in its March States Report on Capital Prioritisation. The recommended programme can, of course, be accepted, rejected or amended by the States.

**As alluded to above, the inclusion by the States of a project in the capital programme does not mean that the project is able to commence; a States Report requesting approval of a capital vote will then be required.**

Additionally, the categorisation of a Project as a Priority 1 through the Strategic Review process does not mean that it will automatically be included within the capital programme. It may be the case that the capital programme does not include some high value Priority 1 Projects as sufficient funding is not available, but there is funding available to undertake several minor Priority 2 projects.

The recommended capital programme will, of course, take account of the priority rankings that each project achieved through the Strategic Review process but will also have regard to other important considerations such as the likely capacity within the construction industry, the impact of timing of projects, the funding and the availability of States resources to manage the projects. A recommended timeline for the various projects will also be included.

It will also be beneficial to include within the capital programme a stream of lower value projects to be undertaken by small/medium sized local firms, such that the on-island skill base is supported.

## 6. The Strategic Review Process

The strategic review process is designed to be a consistent and transparent method of assessing the relative merits of a large number of diverse capital projects including construction, Information and Communication Technology and major equipment purchases. Individual projects are reviewed and scored by a panel of three senior civil servants under eight criteria headings:

- Mandate/Policy Delivery
- Economic Sensitivity
- Community Sensitivity
- Financial Sensitivity
- Resource Sensitivity

- Heritage and Cultural Impact

- Programme Sensitivity

- Other Risks which will be project-specific.

All of the capital projects will be allocated a priority ranking as follows:

- Priority 1 – Recommended for inclusion in the capital programme for the current prioritisation period.

- Priority 2 – Recommended for inclusion in the capital programme but not necessarily in this prioritisation period.

- Priority 3 – Not recommended for inclusion in the capital programme.

Projects which are assessed as Priority 1 will display some or all of the following attributes:

- Benefit substantial parts of the community in a significant way.

- Represent value for money (including whole life costing).

- Appropriate time to undertake project (i.e. economic and commercial considerations as well as need).

- Add to or significantly enhance the Island's Infrastructure for the long term.

- Add to the Bailiwick's heritage (i.e. quality of project, sustainability, environmental impact, etc.).

As stated earlier in this report, a presentation for States Members will be held in February/March where a detailed explanation of the Strategic Review process will be given. More information will also be included in the Department's March States Report.

**7. <u>Recommendation</u>**

The Treasury and Resources Department requests that the following proposition is debated under Rule 12(4) of the Rules of Procedure such that it is considered by the States without amendment.

Accordingly the Department recommends the States:

> To note the Capital Prioritisation process that the Treasury and Resources Department intends to facilitate prior to the March States Meeting together with

the proposed structure of the States Report on Capital Prioritisation that the Department intends to submit for consideration in March 2009.

Yours faithfully

C N K Parkinson
Minister

**NB The Policy Council endorses the proposed capital prioritisation process and supports the proposal.)**

The States are asked to decide:

Whether, after consideration of the Report dated 14th November, 2008, of the Treasury and Resources Department they are of the opinion:-

To note the Capital Prioritisation process that the Treasury and Resources Department intends to facilitate prior to the March States Meeting together with the proposed structure of the States Report on Capital Prioritisation that the Department intends to submit for consideration in March 2009.

**(NB The Treasury and Resources Department has requested that this matter be debated in accordance with Rule 12 (4) of the Rules of Procedure of the States of Deliberation which provides**

*"Where a Department or Committee originating a matter for debate before the States is of the opinion that the proposals it is submitting to the States are ones of general policy, and where it is desirable that the general principles of that policy should be considered, the Department or Committee may request that its propositions be considered by the States without amendment, on the understanding that if the propositions are accepted, the Department or Committee would return with detailed proposals which could be accepted or rejected, together with any amendments…"***)**

**Appendix B**

**CODE OF PRACTICE**

**FOR**

**STRATEGIC REVIEW OF CAPITAL EXPENDITURE PROPOSALS**

## 1.0 Introduction

Departments will always be considering how best to deliver existing services and how to improve service delivery in the future. As part of this function the Departments will have to be mindful of the assets utilised in service delivery, not least of which will be the built environment that they occupy. From time to time Departments will cease to require some of the buildings they occupy and at others they will need to refurbish, repair existing buildings or acquire new facilities.

Any investment proposal that requires funding from the Capital Reserve, irrespective of value, must be subject to the Strategic Review process.

The proposal is to be submitted to the Chief Officer, Treasury and Resources Department for strategic review, the strategic review will determine the priority of the proposal against a set of criteria developed to test the worth of the proposed scheme to the States and community of Guernsey.

Sponsoring Departments will be required to give six calendar weeks notice of its intent to submit a proposal for strategic review, this notice period is necessary to assemble the review panel which is comprised of senior officers across several Departments.

The review will be completed within twenty working days of receipt of the proposal unless further information is required by the review panel in which case the review will re-commence and be completed in a further twenty working days.

The proposing Department will be informed of the Panel's decision at the end of the review process (which might be prior to the end of the twenty working days).

If the proposing Department wishes to query the outcome, they can do so using the appeals procedure. (Appendix 1)

**Members or officers of the proposing Department must not approach individual members of the review panel directly. Review panel members will be instructed not to respond to such requests for further information.**

The process outlined above may be subject to change as and when any changes occur to the Administrative and Accounting Guidelines or as a result of a States' Resolution.

## 2.0 Strategic Proposal Review

The purpose of this review is to determine into which priority of project the proposal will be placed (**NB at this stage we are dealing with a proposal for a scheme <u>not</u> a project. At this stage, therefore, the term proposal is used)**.

This in turn will determine the timing of delivery of the resultant project, whether it will be considered for funding by the States and whether the value, programme proposed, quality and risks associated with the project satisfies the States' requirements.

There are three priorities of proposal:

**Priority 1** projects will be recommended for immediate inclusion in the States capital programme to be delivered to end users in the short term, subject to availability of funds.

**Priority 2** projects will be recommended for inclusion in the capital programme but are of secondary importance to be delivered in the medium term (or sooner if their scores improve following resubmission e.g. demographics may change compared to forecast which might mean a proposal becomes more urgent compared to other proposals considered at that time).

**Priority 3** projects are ill conceived and will not be recommended to progress to the project stage and will not be recommended for inclusion in the Strategic Review process.

This first stage strategic review to determine prioritisation of capital schemes will be undertaken by a panel of appropriate senior officers under the direction of the relevant service director within the Treasury and Resources Department.

**This process is designed to take an objective view of all types of proposals, however when scoring is complete batches of proposals will be presented to the Treasury and Resources Board (T&R) for moderation and approval to be considered in the annual prioritisation process and ensure compliance with strategic, political and fiscal objectives of the States of Guernsey as set out in the Government Business Plan.**

The proposal will be scored and ranked into a priority against the stated criteria, the Treasury and Resources Board will then be in a position to understand the merits of the individual proposal and make a considered decision as to its inclusion into the capital programme based upon transparent, consistent and auditable criteria.

The next section of this guidance will concentrate upon each of the criteria to be covered within the strategic review and will detail the information to be investigated within each criterion.

## 3.0 Scoring Methodology

There are eight criteria to be scored under this review process. Each require answers to a standard set of questions with responses tailored to each individual proposal but which follow similar themes of enquiry.

The scoring panel will comprise of senior staff to be appointed from Departments not sponsoring the proposal.

All scorers will be provided with copies of the written proposal information sheets from the Department sponsoring the proposal, together with any other relevant information in support of the proposal e.g. plans and current usage of land/property.

If considerable discrepancies exist between scorers, moderation of the scores shall take place under scrutiny of the relevant service director, to establish a consolidated score for the project.

If there are proposal information sheets missing, incomplete or containing conflicting information, the relevant service director shall identify these shortcomings to the sponsoring department and the proposal scoring will not proceed until the outstanding information has been provided.

**Sponsoring departments must understand that this process will be time consuming and are encouraged, therefore, to undertake an internal review of their proposals prior to submission of the project into the process.**

## 4.0 Criteria to be scored

The following eight criteria to be scored have been developed as representing the criteria which reflects a balance of the issues which should be considered for any States capital project and will be applied to each proposal entering this prioritisation review process.

Whilst it is not the intention to place obstacles in the way of any proposal, the process is designed to be a transparent, open and fair process, there may be occasions when a particular circumstance may, on its own, prevent a proposal from progressing to the next stage.

**Given the nature of the proposal the Panel reserves the right to seek further information which might require supplementary information from the sponsoring Department, which may cause a delay to the review process.**

The following criteria will be considered:

### i) Mandate/Policy Delivery

This section deals with how the proposal will help deliver States policies. The States has several high level strategic policy initiatives that have been agreed by the States of Deliberation, focussing on Education, Health and infrastructure.

Within each policy initiative there are high, medium and low priority deliverables e.g. waste management has several strands – high level consideration might be the energy from waste plant, medium might be recycling initiatives, low might be encouraging better habits regarding littering. Questions relating to this are:

- Which policy does this proposal relate to? (if more than one please state), and identify the relevant States Resolution.
- What is the Departmental policy priority (high, medium or low?)
- What is the timescale for delivery of policy outcomes affected by this proposal?
- Is the policy framework to be reviewed within the lifetime of the proposal to tender stage?
- What would be the effect on policy outcomes if the proposal did not progress? What contingency plans exist?
- How does the proposal interact with other policy initiatives and timescales? Where does the proposal fit in the Government Business Plan?
- Where does this proposal fit in the Department's operational Business Plan?

**Economic Sensitivity**

These criteria must be populated to show the likely commercial impact of the proposal.

- Will this proposal provide permanent employment post completion? Give details and justification for projections.
- How might the provision of this proposal have an impact on other businesses or Departments within the Bailiwick?
- Will the proposal generate any income? If the proposal will generate income, where will the income be spent or invested? What are the basic assumptions and calculations of the income predicted?
- How much income might be generated for local businesses as a result of delivering the proposal?
- What assets will the Department be able to release back to the centre for re-use/disposal if this proposal is delivered? When would those assets become available?

**ii) Community Sensitivity**

This section deals with the benefits to the community if the proposal is delivered.

- ❖ Which sectors of the community will benefit from this proposal and how is this justified?
- ❖ What currently exists for the provision of this service proposal? How will it be affected by the proposal?
- ❖ What are the alternatives to the proposal that have to be considered? What benefits will the proposal bring to the community?
- ❖ What would be the impact on the targeted community if the proposal does not progress? How has this been assessed?
- ❖ Could this proposal be provided by another organisation? If no, why not?
- ❖ Could the proposal be delivered as a collaborative scheme with another (other) Department? Has this been discussed? What are the critical issues to make this option possible?

**iii) Financial Sensitivity**

This section looks at the financial provision for the proposal. Not just initial capital outlay but the continuing requirement for the future lifespan of the proposal. That is not to say that at this stage there must be a fully costed whole life plan for the proposal but rather that the sponsoring department has given due consideration to how the proposal will be funded and maintained for the duration of its useful life.

- ❖ How will the proposal be funded? What contributions are planned from existing funds?
- ❖ Will the sponsoring department be making a contribution to costs (by selling some existing equipment, property or land, for example?)
- ❖ What financial impact will the proposal make to the sponsoring Department?
- ❖ What is the cost/benefit for this expenditure?
- ❖ What is the cost per capita of the proposal for its entire lifespan?
- ❖ What is the cost per service recipient (e.g. pupil, patient, elderly resident etc.) for the proposal's entire lifespan? Capital plus revenue costs, provide details and basis for all calculations.

**iv) Resource Sensitivity**

This criteria is concerned with the impact on local resources to be utilised by the proposal during its construction or development phase. It is important to consider the effect the proposal will have locally in terms of capacity to deliver the proposal's required inputs to enable a successful outcome.

- ❖ Who will be the Senior Responsible Officer (SRO) (Project Director) for this proposal?
- ❖ What experience do they have in regard to managing such a proposal?
- ❖ What support will be required by the SRO, both in-house and externally?
- ❖ Can the Bailiwick support the proposal with labour, plant and materials supply?
- ❖ Will this proposal require the use of innovative techniques or the use of scarce/unique materials?
- ❖ Will this proposal be similar to other projects already undertaken elsewhere (not necessarily in the Bailiwick)?

**v) Heritage and Cultural Impact**

The proposed location and composition of the proposal may impact on local heritage, it is important, therefore, that the proposal addresses this aspect.

- ❖ How will the proposal address the latest Building Regulations, particularly those dealing with CO emissions and access for all provisions?
- ❖ What are the relevant heritage issues, and how is it proposed to deal with these?
- ❖ Will the proposal be a landmark building or adjoin an existing listed building or in any way affect such heritage structures or monuments?
- ❖ Does the proposal fit with current area plan requirements and use class requirements?
- ❖ Have issues such as health and safety, future needs of users, use of pre-fabricated components and sustainability been addressed and how?

- ❖ How will the proposal contribute to the future heritage, arts or sporting facilities in the Island?
- ❖ How will the proposal complement existing facilities?

**vi) Programme Sensitivity**

This section deals with the timing of the proposal and its effect on other departmental projects or proposals. (A particular proposal may form part of a much larger and longer programme of work or be an individual proposal.)

Issues around programming affect funding opportunities, resource implications and policy delivery. Whilst a proposal may be sound in other areas, its timing will be a critical factor in so far as it may affect other activities of the States, the construction industry, commerce generally and the general community.

- ❖ Does this proposal form part of a bigger programme of work, if so where does it sit in the programme and how important is this proposal and why?
- ❖ How sensitive is the timing of the proposal, must it be completed within a specific timescale and why?
- ❖ What would be the effect of delay to the proposal by 5, 6, 10, 15 years?
- ❖ Are there any associated enabling works which must be completed before this proposal could be commenced?
- ❖ What other similar projects/programmes or proposals are being undertaken or being brought forward for approval?
- ❖ What interdepartmental consultation has been undertaken to check for similar projects/programmes or proposals?

**vii) Other Risks**

This section deals with other proposal specific risks such as planning, environmental impact, external influences (e.g. pressure groups) etc.

As these risks will be identified for each specific proposal it is not proposed to be prescriptive regarding the questions to be asked. However the review panel will reserve the right to challenge the notified risks as to whether these are a complete set of risks for the proposal and may offer advice as to other risks they feel should be addressed at the review.

## 5.0 Timing and submission of a proposal for strategic review

Strategic reviews will be undertaken when required; they will not be triggered by a time of year such as the annual budget review.

Sponsoring Departments have to allow time to undertake the review within the overall timescale envisaged for the delivery of the proposal. Departments should allow up to twenty working days for a decision from the review panel subject to the complexity of the proposal and the information provided. Should further information be requested from the panel, the time to reach a decision may be extended. Departments are urged, therefore, to address each category as fully as possible when submitting their proposal.

Proposals should be delivered to the Chief Officer (T&R), who will request the relevant service director to acknowledge receipt of the proposal and give an indication of when a panel will be convened for the strategic review and whether it is likely that attendance from officers and/or Deputies of the sponsoring Department will be required during part of the review.

For the avoidance of doubt and to reduce queries from the review panel, submissions should comprise the following:

- Executive summary of proposal
- Details of the proposal – information to be provided against the eight criteria
- Outline business case
- Sketch plans and elevations – outline
- Programme – outline
- Information as to how the proposal has been produced
- Any early feedback from Environment Department

The Executive Summary need only be as long as required to convey the essence of the proposal e.g. why now? What it is for, general impact and what would happen if not approved, etc.

Some proposals may not require information to be provided against each of the eight criteria but sufficient information must be provided to enable the review panel to understand the proposal and as a minimum, it is suggested, answers to the questions listed above.

## 6.0 Associated Costs

For this review process costs should be kept to a minimum as most of the information should be available internally (sponsoring Departments are advised to contact the relevant service director in the first instance to determine whether help could be provided by the Treasury and Resources Department). If, however it is thought that some external help from a consultant is required, that help must be obtained in accordance with the Accounting and Administration Guidelines and in particular the rules contained in the Appointment of Consultants Guidance.

The sponsoring Department will have to fund the costs of such consultancy, which may be recovered within the project vote should the proposal move forward to become a project.

**Scoring System**

i) The weighting is in the scores, and so is not done separately.

| | |
|---|---|
| **Score 0-10** | **Mandate Policy Delivery –** How will this project help deliver current and/or future departmental mandates and support States policies. |
| **Score 0-10** | **Economic Sensitivity** – Will this project contribute to or be detrimental to the commercial wellbeing of the community of Guernsey?<br><br>What will the effect be of not proceeding with this project? |
| **Score 0-20** | **Community Sensitivity** – What percentage of the community will benefit from this project?<br><br>Can services generated by and from project be provided in any other way? |
| **Score 0-20** | **Financial Sensitivity –** How will this project be funded? All from States, revenue demands £p.a. (gross) and HR, other income streams *etc*.<br><br>What else may not happen if this project goes ahead – impact on other work streams? |
| **Score 0-10** | **Resource Sensitivity** – How will project be resourced, (not just staff to be included in the project team), and is there capacity to uphold scheme – how much (or little) can be sourced locally. Does it re-use existing staff, training, wage bill issues?<br><br>HR, Natural Resources Energy Efficiency *etc* Assets. |
| **Score 0-10** | **Heritage and Cultural Impact** – Location and size of project, materials to be used, existing building, listed status, Guernsey history and general history. |
| **Score 0-10** | **Programme Sensitivity** – Does project have to be provided within a total time frame, why now/then, effect of bringing forward/delay? Is value significant in the market sector to which it applies?<br><br>Does this affect, or could it help detract from departmental projects? |

**Score 0-10** **Other Risks**

- Planning;
- Environmental impact;
- External influences (*eg* pressure groups);
- Internal influence.

**TOTAL 100**

Thus, proposals are scored against each criterion to determine ranked order and priority number, *i.e.* Priority 1, 2 and 3, Priority 1 being of greatest strategic importance.

**Priority  Definition**

**<u>Priority 1</u>**

**Score 70 Marks +**

- Will benefit the whole community;
- Cost commensurate with outcome, (*ie* represents value for money/best value including whole life costing);
- Has significant impact commercially;
- Adds to Bailiwick's heritage - heritage is taken to be in its widest context *i.e.* quality of project, sustainability, environmental impact;
- The time is right for project; and
- Does not impact significantly on other programmes/projects.

**<u>Priority 2</u>**

**Score 30-69 Marks**

- Benefits significant sections of community;
- Cost reasonable for projected outcome, (represents value for money);
- Has some commercial impact;
- Has some impact on heritage; heritage is taken to be in its widest context *i.e.* sustainable, environmental impact *etc*;
- Could be put off for limited period with little effect; and
- Could impact significantly on other projects/programmes of work.

**<u>Priority 3</u>**

**Score 1-29 Marks**

- Only benefits very limited community or purely cosmetic;
- Costs unreasonable – not value for money;
- No commercial impact;
- Does not contribute to heritage; heritage is taken to be in its widest context *ie* sustainable, environmental impact *etc*;
- Could be put off indefinitely with no material effect; and
- Is likely to impact significantly on other projects/programmes.

**APPENDIX 1**

## APPEALS PROCEDURE

1 Upon notification of the outcome of a Code of Practice 1 Review (COP 1 Review), the Sponsoring Department, through its Chief Officer, may accept or reject the outcome.

2 The relevant Chief Officer notifies the Chief Officer (T&R) that they wish to appeal the COP 1 Review findings. The Chief Officer (T&R) will then require relevant service director to provide a copy of all papers produced under the COP 1 Review.

3 Upon receipt of the COP 1 Review papers, the Chief Officer (T&R) will notify the Appeals Panel that an examination of the original review findings is required. The Appeals Panel is chaired by the Deputy Chief Executive and will comprise three further senior officers, other than those that undertook the COP 1 Review. The Appeals Panel will examine, in detail, the original review outcome and may call any officers involved in the original COP 1 Review to the Appeal Review. The Appeals Panel have the right to endorse the original review findings or change scores upwards or downwards to derive a new outcome.

4 Upon completion of the Appeals Panel Review, the Sponsoring Department will be notified of its findings. If the Appeals Panel Review endorses the original findings or indicates a change to the original COP 1 Review score, either upwards or downwards, the Sponsoring Department can either accept the result or reject it.

5 If the Sponsoring Department rejects the Appeals Panel findings they can make further appeal via their Board, by Ministerial letter, to Policy Council. Policy Council will then examine the Appeals Panel Review findings and come to a binding conclusion, if not unanimously, by simple majority.

**There is no further right of Appeal, the Policy Council decision is final.**

**Appendix C**

## Summary of Proposals Submitted by Departments

| Department | Proposals | Priority |
|---|---|---|
| **Culture and Leisure** | Museums Store | Two |
| **Education** | College of Further Education Phase 2b | One |
| | Les Beaucamps School | One |
| **Environment** | Cobo Bay Bunker / Sea Wall Repair | One |
| | Val des Terres Rockface | Two |
| **Health and Social Services** | Adult Acute Mental Health Facilities | One |
| | Homes for Adults with a Learning Disability | One |
| | Giffard Ward (Princess Elizabeth Hospital) | Two |
| **Home** | eBorders IT system | One |
| | Police core IT system | One |
| | Tetra Radio | One |
| | Redevelopment of Maison Celine | Two |
| **Public Services** | Belle Greve Wastewater Disposal Facility | One |
| | Solid Waste Solution (approved by the States) | One |
| | Cobo Foul Water Pumping Station | Two |
| | Permanent Civic Amenity Site | Two |
| | Sewer Network Extension Plan | Two |
| **Public Services (Ports)** | Airport Pavements | One |
| | Airport Radar | One |
| | St Peter Port Harbour Crane Strategy (approved by the States) | One |
| | St Peter Port Harbour Pontoons | One |
| | Sarnia Work Boat | One |
| | St Peter Port Harbour Careening Hard | Two |
| | St Sampson’s Harbour Marina Wave Screen | Three |
| **Social Security/ Treasury and Resources** | Social Security/Income Tax IT System | One |
| **Treasury and Resources** | Cabernet Limited Recapitalisation | One |
| | Corporate Asset Management IT System | One |
| | IT Wide Area Network | One |
| | Corporate SAP Initiatives | Two |

# Museums Store

| | | | |
|---|---|---|---|
| Submitting Department | | **Culture and Leisure Department** | |
| Estimated Capital Cost | **£5,000,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **April 2009 (detailed planning)** | | |
| Completion Date | **April 2011** | | |
| Duration | **2 years** | | |

## Summary of Proposal

The Museum Collection Centre (MCC) will be constructed on part of the site of the former Longfield School. It will comprise:

- A purpose-built storage facility for the Museum's reserve collection
- Offices, research space and workshops for the Museums Service

The store will be a windowless industrial-type building on two floors, plus a basement. The building will be sub-divided to provide different storage regimes in terms of humidity, light and temperature appropriate to the objects we have in care. It will inter-connect with two-storey accommodation for the Museums Service curatorial staff including offices, layout space and object preparation areas. A workshop and a drawing office will be included for the design & technical staff.

The proposal arises from two main drivers.

### 1. Collections Care

The Museums Service has in its care a large number of irreplaceable objects representing Guernsey's material culture. Currently museum objects are stored at a number of locations, none of which are considered to be fit for purpose. There is insufficient space, little environmental control and in some cases inadequate security. The facts have been confirmed in a number of reports dating back to the 1990's, the latest of which is the National Audit Office report "Safeguarding Guernsey's Heritage Assets" published September 2007. Cramped conditions mean that the collection cannot be used effectively. Inadequate storage facilities mean that some museum objects will be damaged beyond repair. In addition there will be a growing risk of the Service losing its Accredited Museum status, which as well as proving to be a huge embarrassment for the States of Guernsey, could have far reaching implications for the whole operation of the Service.

### 2. Staff Welfare

There is a pressing need to provide staff with decent working conditions. Museum staff have been housed for almost two decades in sub-optimal office accommodation which has raised health and safety concerns. The lack of working space also impairs efficient working. A partial temporary fix has been achieved by moving into two floors of Grange House, but a long-term solution is essential. Delays in progressing this proposal will inevitably result in an increased risk of staff injury and low morale.

**Savings**

Construction of the MCC will allow the following buildings to be released back for States use or sale:

* St John's Street Store
* St John's Street Police Garage
* St John's Street Back Quarters (ground floor)
* Grange House (first and second floors)
* Hermes House (The Telephone Museum)
* Baubigny Arsenal
* Gibauderie Yard

It will also allow reduction and rationalisation of space taken up at L'Islet Arsenal. Rented space at Bulwer Avenue and at 'The Archivist' has already been released. We believe that working practices will also be improved.

**Curatorial Work Areas**

The Curatorial staff care for the Museum objects, conduct research, prepare exhibitions and answer enquiries from the public. The Archaeologists in addition investigate sites and rescue objects from excavations. All this work requires an amount of layout space with good light, which is currently lacking. Members of the public assist the museum on a voluntary basis, providing both community involvement and a valuable extension to the workforce at minimal cost to the States. We have to date lacked the space to fully utilise these volunteers.

**Technical Work Areas**

The technical department works to conserve objects in care of the Museum and to prepare these for display. For this, a conservation laboratory is required. The technicians also build and maintain the museum displays, requiring a safe workshop equipped to modern standards. Exhibitions, publications and publicity material are designed in-house, requiring a drawing studio.

**Public Access**

Members of the public will be able to visit the MCC on an appointment basis to conduct individual research into the collections. We do not currently have the space to permit this beyond a very limited basis.

**Requirements for Object Care**

All museum objects need to be kept secure from theft, physical damage or attack by pests. Objects of flint, stone or pottery are relatively robust and can survive for thousands of years with minimal care. Most other objects require controlled storage conditions if they are not to deteriorate. Metals need to be kept relatively dry, whilst many objects can be damaged by fluctuating temperature or humidity. In addition, textiles, paintings and photographs are damaged by light. Storage in unsuitable boxes or cabinets can also result in chemical attack. We cannot currently provide the required level of care.

**Government Business Plan**

The Museum is the principal repository of the Island's material culture, which underpins Guernsey's Cultural Identity. In order that the Museums Service can fulfil its mandate to the States and to the people of Guernsey, it is vital that a suitable new store is sought as soon as possible.

## College of Further Education Phase 2b

| | | | |
|---|---|---|---|
| Submitting Department | | **Education Department** | |
| Estimated Capital Cost | **£2,700,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **August 2009** | | |
| Completion Date | **September 2010** | | |
| Duration | **13/14 months** | | |

**Summary of Proposal**

### Background

The facilities at Route des Coutanchez and Brock Road used by the College of Further Education, Youth Service and Youth Theatre are not fit for purpose and incur high levels of maintenance expenditure. In addition to this, there has been a significant rise in demand for Post-16 (including Special Needs) provision within the Further Education sector in recent years, which has necessitated the College of Further Education providing an increased number and type of courses for greater numbers of students. Despite falling rolls in schools, further increases in Post-16 participation rates are expected to result in continued growth in this sector. The construction of new facilities will require significant funding, therefore the consolidation of the College of Further Education and other Services onto a single location on the St. Peter Port school site was planned to be undertaken as a phased project:

**Phase A: College Hall** (Completed November 2006)

The construction of a multi-purpose hall that could be used for examinations, meetings, conferences, rehearsal, tuition and performance. Dance and drama studios were also to be provided, along with changing, storage and administrative facilities.

**Phase B: Re-use of the St. Peter Port Secondary School building**

An interim measure pending completion of the remaining construction phases, to enable the release of other buildings (Longfield, Grange House and Brock Road). Evaluation of space requirements identified that a further site (St. Sampson’s Secondary School) would also be needed in order to provide sufficient accommodation until new facilities were built. Phase B was therefore divided into two parts:

- Phase B1: The re-use of St. Sampson’s Secondary School at Delancey, enabling the release of Longfield and Grange House (funding available from previous budget allocation).

- Phase B2: The re-use of St. Peter Port Secondary School, enabling the release of the Old Boys’ Grammar School buildings in Brock Road.

Phase B was initially planned on the basis of minimal expenditure as it was expected that the St. Peter Port school building would need to be re-used only for two or three years. In view of the recent change in States' financial circumstances, the Education Department anticipates that Phase B may now need to be in operation for longer than originally anticipated. This increases the cost of Phase B as additional works will be needed due to more elements of the building requiring repair or replacement to support the building's extended use. This proposal requests funding for Phase B2 to enable this longer-term re-use.

**Phases C/D: Construction of new facilities**

The remaining construction elements, to be built on the St. Peter Port Secondary School site. Demolition of the St. Peter Port Secondary School and the release of the College of Further Education sites at Route des Coutanchez and Delancey.

**Cost Summary**

Preliminary estimated costs for the required works are outlined in the following table.

| **Cost area** | **Estimate** |
|---|---|
| Repair/replacement of roofing, windows, doors and external panels | £473,000 |
| Replacement/upgrading of mechanical and electrical infrastructure | £529,000 |
| Flooring, ceilings, decoration, asbestos removal, layout modifications | £951,000 |
| Disposals, Furniture, Fixtures and Equipment | £172,000 |
| Clerk of Works | £30,000 |
| Professional fees | £250,000 |
| Contingency (14%) | £334,000 |
| **Total (**at 2008 prices) | **£2,739,000** |

Should the relocation to the St. Peter Port school not take place, the Brock Road site will need to be retained, significant maintenance funding will be required and costs will continue to be incurred for rented accommodation for the Schools' Music Service. Based on the most recent condition survey information available, these costs are estimated in the table below.

| **Site** **Usage Period** | **5 years** | **10 years** | **15 years** |
|---|---|---|---|
| Brock Road (maintenance, at 2007 prices) | £1,995,851 | £2,636,677 | £3,519,620 |
| Music Service (rent, at 2008 prices) | £106,500 | £213,000 | £319,500 |
| **Total** (excl. inflation & contingencies) | **£2,102,351** | **£2,849,677** | **£3,839,120** |

**Release of the Old Boys' Grammar School in Brock Road**

If funding for this proposal is approved early in 2009, the Old Boys' Grammar School building at Brock Road will be released in 2010 or 2011. The Education Department has been requested by the Strategic Land Planning Group to release the Brock Road site as early as possible so that it may be redeveloped by the Housing Department.

## Les Beaucamps School

| | | | |
|---|---|---|---|
| Submitting Department | | **Education Department** | |
| Estimated Capital Cost | **£38,150,000 *** | Estimated Additional Revenue Cost | **£395,000 per annum** |
| Start Date | **Construction start August 2010** | | |
| Completion Date | **May 2014** | | |
| Duration | **3 years 10 months** | | |

∗ Includes £2.9million of project costs (including post-16 and special needs)

Project Brief

Les Beaucamps is the oldest of the three secondary schools which were built after the Second World War. It was officially opened in 1959 and currently provides secondary education for the children of the Castel, St. Andrew's and St. Martin's parishes.

The Les Beaucamps High School brief is to provide a new-build secondary school to replace and improve the facilities currently provided by the existing school on the same site. It will provide places for up to 660 pupils aged from 11 to 16.

The project will provide new buildings to a maximum gross internal area of 8570m$^2$ on the school site. It will comprise a school building, a separate sports facilities block, and external sporting, hard play and parking areas. A compact plan form has been achieved, with general teaching accommodation arranged around a central courtyard cloister. The sports building is also based on a very efficient plan to reduce circulation space, maximise teaching area and reduce volume.

The school will be able to operate throughout the construction period because the new school buildings will be constructed on the school site and on land purchased by the States in 2004 for the purposes of the new school to the west of the existing school building. After demolition of the existing school buildings, the sports building will be built on that part of the site.

The new school buildings are expected to have an expected minimum 50-year life and a 15-year minimum period prior to first major maintenance. The buildings will adhere to Guernsey regulations, but also strive to achieve the principles of the latest UK standards. In particular, the school building design will use natural light and ventilation, as well as comply with the standards laid out in the Disability Discrimination Act 1995 and Part M of the UK Building Regulations. The intention is to achieve a highly sustainable solution reinforcing the Island's commitment to reducing carbon emissions and global warming.

It is intended that the new sports building and its facilities are made available to the local community outside the normal school working hours. Facilities include a 4-lane pool, gymnasium and sports hall, with associated indoor and outdoor changing. Some external sports facilities, including the synthetic pitch and tennis courts, will also be available for use by the local community outside of the normal school hours. The sports field will be retained as the main external sports facility on the site. The landscape masterplan has endeavoured to retain as many mature trees on the boundaries and within the school field as possible, with the boundaries positively enhanced with native shrub, perennial and tree planting. The Education Department intends to retain the Drill hall and Scout hut for further and continued use by the community. The Caretaker's house and Militia hut store will also be retained by the school to serve the new building. The World War 2 bunker will remain unaltered.

Project Rationale

The project is of the highest priority to the Education Department because the existing buildings do not satisfy current standards for condition, capacity and fitness for purpose. The project was first approved by the States in 2001 and subsequent States Reports have been submitted to progress the project. A full project history is contained in the February 2009 Billet d'État.

Condition, Capacity and Fitness for Purpose

The buildings are **in very poor condition** and are failing to meet current standards for health, safety and disability compliance. Significant costs for maintenance will be needed to keep Les Beaucamps running for a further 10 years. In total around £5.5 million will be needed. The building requires a new roof, and the replacement of its glazing and hard surface external play areas. The elevations are in poor condition. The building services in the main are the original installations and in need of replacement. Les Beaucamps is not Discrimination Disability Act compliant. Modern fire safety requirements for compartmentation or sprinklers cannot be met. It is not energy efficient and there is insufficient separation of play areas from the areas used for school buses and parents' dropping-off and collection points.

The buildings are **no longer fit for purpose** to provide for the curriculum of the school and the required social, recreational and community sporting facilities. Many of the classrooms are too small to accommodate the technology used in today's lessons and the school hall is too small to accommodate the increased numbers. The raising of the school leaving age to 16 also requires new, more personalised learning facilities to be available. The facilities for school lunches are not adequate – the school was built at a time when most children did not stay during the lunch-hour. In the present buildings, none of the rooms below is fit for purpose:

| | | |
|---|---|---|
| Library | School Hall | Gym/Changing rooms |
| Science laboratories/Prep room | Music rooms | Art rooms |
| Dining room/canteen | Staff room | Staff toilets/offices |
| Reception | Workshops block | |

The buildings **do not provide the capacity** required for the increased number of pupils attending the school because of the reorganisation of secondary education and the raising of the school leaving age to 16. Les Beaucamps High School should presently accommodate no more than 490 pupils.

Procurement

Following consultation with States Property Services, the project will be procured using a two-stage design and build contract as a single project with three phases:

- new-build school building
- demolition of existing school buildings
- new-build sports hall, gym and swimming pool.

Planning in Principle and Design Development

The formal Planning in Principle submission was made at the end of October 2008 and a decision expected from the Environment Department by the end of January 2009. To date, the building design has been developed to Detailed Design stage (RIBA Stage D). The internal and external design layout has been progressed in response to the specific functional requirements, adjacencies and circulation flows and in response to the need to reconcile the environmental, educational and cost considerations to achieve the best value scheme.

## Cobo Bay Bunker/Sea Wall Repair

| | | | |
|---|---|---|---|
| Submitting Department | | **Environment Department** | |
| Estimated Capital Cost | **£350,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **Spring 2009** | | |
| Completion Date | **Summer 2009** | | |
| Duration | **6-8 weeks (subject to weather/tidal conditions)** | | |

**Summary of Proposal**

The section of wall in question is approximately 20m long running north-east to south-west and is located to the south of the tar macadam public car park off Cobo Coast Road. The entire length of wall is currently used as a sea defence structure and, for most of its length, is in front of a partially buried German Casemate bunker.

Monitoring (undertaken by engineers from States Property Services since 2004) indicates that the wall is moving away from the bunker and also gradually rotating towards the sea at a rate of approximately 3 to 4mm per year.

It has been observed that the rate of movement has increased and whilst analysis suggests that there is no immediate risk of the wall collapsing there is a risk that, as the movement continues, it could accelerate leading to a sudden toppling failure of the wall away from the bunker. It is therefore proposed that works are needed as soon as possible to ensure both the safety of beach users and the integrity of the coastal defences at Cobo bay.

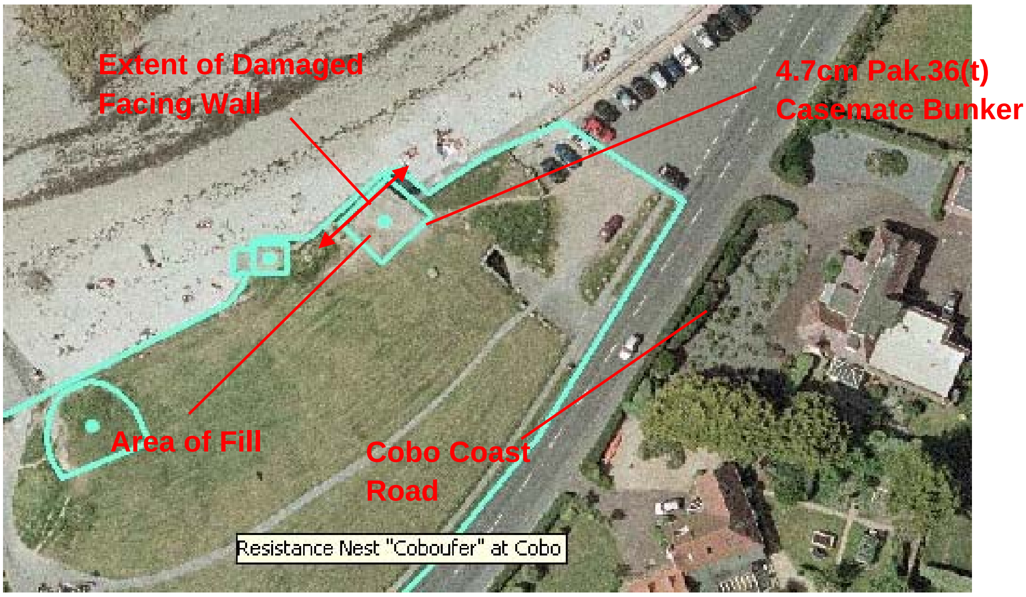
Two preferred remedial works options were set out to provide both a long term and medium term coastal defence solution.

The medium term option (approx 20 years) consisted of a new concrete apron along the entire length of the retaining wall together with tying the retaining wall back to the casemate behind with steel dowels (not supported by the Historic Sites Curator, Guernsey Museum). This option was costed at £75,000. However, this did not address the stability of blocks that form the wall which would potentially have cost a further £50,000.

The long term option (50+ years) consisted of the removal of the damaged facing wall to expose the casement bunker behind to act as the new coastal defence. A new, smaller, retaining wall would be built to retain the soil at the southern end of the partially buried casement (in line with the Historic Sites Curator’s considerations).

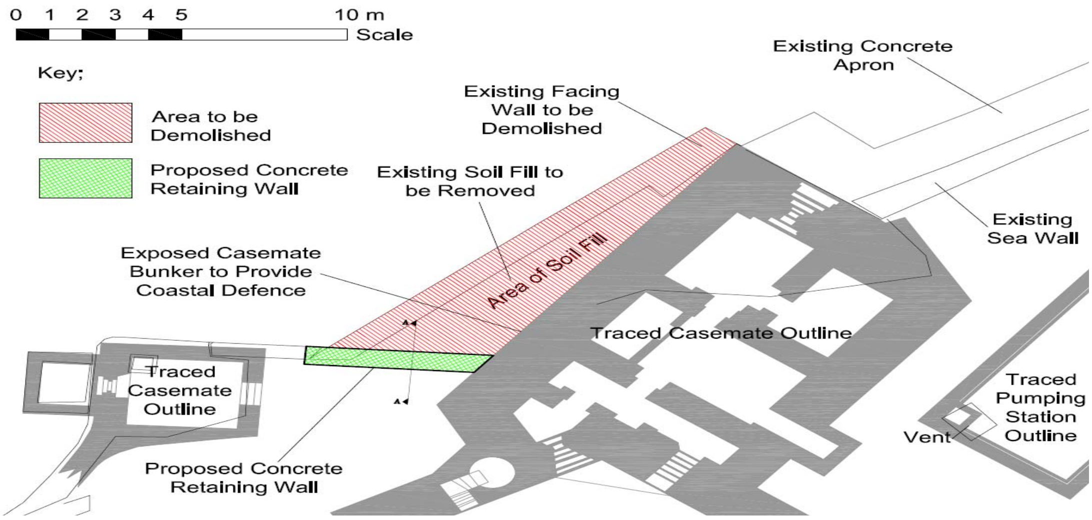
Following extensive and detailed consultations with the Historic sites curator from Guernsey Museum and Engineers from States Property Services, the Environment Department has agreed to put forward plans to remove the facing wall and construct a new coastal defence structure spanning between a casemate to the south and the newly exposed casemate.

The view of the Environment Department is that in view of the urgency of the works and in order to avoid working on the beach during the busy summer months, it is essential that these works are tendered as soon as possible and works commenced in spring 2009.




Aerial Photo Showing Site Layout and Fortification

Photo Showing Gap between Bunker and External Facing Wall




<u>Drawing Showing Proposed Concrete Retaining Wall</u>

# Val des Terres Rockface

| Submitting Department | | **Environment Department** | |
|---|---|---|---|
| Estimated Capital Cost | **£200,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **Summer 2009** | | |
| Completion Date | **Autumn 2009** | | |
| Duration | **Approx 12 weeks (subject to contractors working schedule)** | | |

## Summary of Proposal

The east side of Le Val de Terres has been cut into a sloping valley side, resulting in a very steep cutting that varies in height from about 3-8m. A geotechnical inspection of the rock cuttings was undertaken by Frederick Sherrell Ltd. in January 2008 following a rock fall precipitated by a vehicle impact in September 2007. Since then a temporary scaffold barrier has intercepted further falls of rock in this area.

Four areas of exposed rock cutting were examined by Frederick Sherrill over a 285m long section of the road and the areas are hereafter identified as Cutting No. 1 - No. 4. The report states that the exposures in the road cuttings indicate that the bedrock is moderately to highly weathered and closely fractured in the upper levels. Vegetation, trees and water penetration are also factors where fractures are open and have been further penetrated, particularly by tree roots. The geometry and geological conditions and the stability of each of the four cuttings were considered and recommendations for remedial works made.

In summary, the recommendations are that each of the four cuttings requires remedial works. Whilst it is not considered that a major collapse or failure of the rock face is likely it is considered that there is potential for small-scale rock falls at each cutting. In Frederick Sherrell's opinion whilst the blocks of rock which might fall in the area of Cutting No. 1 would probably be small (up to 0.2m across) they would impact the road and are therefore considered a hazard to road users. At Cutting No. 4 it is noted that several narrow wedges could easily detach from the exposed face with little or no warning.

It should be noted that in each area works would be required to remove, or reduce, trees and vegetation in addition to the works outlined below:

**Cutting No. 1** (at the lower end of the road, the site of previous vehicle impact) The rock face scaled to remove loose rock and a small section of cracked masonry wall.

The construction of a free-standing wall approximately 20m in length to replace the temporary barrier, the wall to be tied back to the rock face with 2m long galvanised dowels and weep holes installed to dissipate hydrostatic pressure at the back of the wall.

A rock interceptor fence to be installed on the slope in front of the face to deal with potential rock fall hazards from the upper rock face.

**Cutting No. 2**
The upper levels of the rock face should be scaled and netted. The netting to be secured to the face with galvanised cables and galvanised dowels by a specialist contractor.

**Cutting No. 3**
The upper part of the rock face should be scaled and then netted using galvanised cables and galvanised dowels to mitigate the risk of rockfalls impacting the road. The lower rock faces to be checked and lightly scaled to remove any loose flakes.

**Cutting No. 4**
A masonry facing wall should be constructed approximately 26m long and about 3m high for the full length of the cutting. It would be necessary for the rock face to be trimmed back by about 0.5m to maintain the road width.

The option of installing rock netting and bolting in two areas was proposed by Frederick Sherrell Ltd. This would be a less costly solution for these areas. It was considered by the Director of Transport Services that rock bolting at a level at which a vehicle could collide with in the event of an accident would be hazardous and should be avoided. In order to reduce this risk it was considered that rock netting and bolting should be restricted to areas of 3m and above the road level.

Subject to the projects approval, detailed plans would be prepared by States Property Services and submitted for planning consent.

## Adult Acute Mental Health Facilities
## (Phase 6B)

| | | | |
|---|---|---|---|
| Submitting Department | | **Health and Social Services Department** | |
| Estimated Capital Cost | **£25,400,000** | Estimated Additional Revenue Cost | **£475,000 per annum** |
| Start Date | **2011** | | |
| Completion Date | **2013** | | |
| Duration | **18 months** | | |

**Summary of Proposal**

The inpatient accommodation at the Castel Hospital does not meet current standards for the care of people with mental health problems. The adult psychiatry ward (Albecq Ward) does not provide for separation between the different types of patient in terms of their condition or gender. Although this ward has recently been refurbished, this was an interim measure to make the situation bearable until the ward can be relocated to the Princess Elizabeth Hospital site at La Corbinerie.

As well as inpatient facilities, modern mental health care relies on a number of other arrangements, including a community focus. In line with this, the HSSD has developed three Community Mental Health Teams (CMHTs) which are based at the Castel Hospital. These teams consist of Community Psychiatric Nurses, Occupational Therapists, Social Workers and Psychologists and are each led by a Consultant Psychiatrist. The CMHTs are operating out of a former ward at the Castel Hospital where the facilities are too small, the layout is unsatisfactory, it is extremely difficult to see patients with any form of privacy and access for disabled people is very difficult.

The Castel Hospital also provides day services for mental health patients. The Day Centre building offers a range of services including psychotherapy, drama therapy, reflexology, art therapy, woodwork therapy and many more. There are approximately 60 attendees per day, Monday to Friday. The building is just capable of taking this number of people but cannot accommodate any more and demand is rising. Other outpatient services on the Castel Hospital site include the lithium (depot) clinic and consulting rooms for the psychologists and other professional staff. Again, these facilities are not fit for purpose.

Divette Ward, an assessment and respite ward for people with mental health problems, was relocated from the Castel Hospital site to temporary facilities in the Princess Elizabeth Hospital as an interim measure until permanent facilities could be provided at La Corbinerie. It had to be moved because access to it was dangerous for frail and confused older people. The facilities at the Princess Elizabeth Hospital are, however, not ideal as the ward was not designed for people with dementia, so Divette Ward is to be moved into Phase 6B.

It is planned that Phase 6B will comprise a twenty-four bedded adult acute mental health ward, a twelve bed assessment and respite ward for older people with mental health problems, a psychiatric day hospital and a social and therapeutic day centre, plus clinic and consulting room space and a base for the CMHTs, Community Drug and Alcohol Team, Cognitive Behaviour Therapists, psychologists and all the associated support services necessary to provide mental health care.

The main benefits of the proposed new facilities, compared to the existing premises at the Castel Hospital, can be summarised as follows:

- segregation of sleeping and day areas to allow for separation of male and female patients and people with different types of mental health problems;

- facilities built to modern standards, thus providing a safe environment for the patients;

- bedrooms with en-suite facilities, thus improving privacy and dignity for the patients;

- improved ‘extra care’ facilities, including well located control and observation bases, which may help to reduce the number or length of off-island placements;

- provision of domestic skills and complementary therapies areas, which will help to facilitate an early and successful return to independent living;

- improved clinic and outpatient facilities to allow for the ever increasing numbers of people needing these services;

- ability to enhance the CMHTs’ services, which will help to maintain patients in the community;

- improved range of mental health services, e.g. Cognitive Behaviour Therapy, as provision of suitable accommodation allows enhanced services to be provided;

- improved access for disabled people;

- reduced stigma of mental illness;

- improved working conditions, which will help the HSSD to recruit and retain staff;

- improved staff and patient security;

- improved use of mental health service staff: due to the division of the mental health services over split service delivery sites, it is not possible to cross cover staff absences when necessary, which leads to increased overtime and use of locum or agency staff (mainly nurses);

- four more beds will be available for assessment and respite care of people with dementia, which will meet the increasing need for those services;

- the valuable Castel Hospital site will be vacated and available for other services or for sale.

## Homes for Adults with a Learning Disability

| Submitting Department | | **Health and Social Services Department** | |
|---|---|---|---|
| Estimated Capital Cost | **£5,300,000** | Estimated Additional Revenue Cost | **£560,000 per annum (to be partially offset by savings on off-island placements)** |
| Start Date | **2010** | | |
| Completion Date | **2011** | | |
| Duration | **1 year** | | |

**Summary of Proposal**

Vacating Oberlands House is a necessary step towards clearing the area of the Princess Elizabeth Hospital campus required for Phase 6B of the Site Development Plan to proceed and allow transfer of acute mental health services from the Castel Hospital. For this to happen, two new homes to accommodate a total of twelve adults with a learning disability, who currently live at Oberlands House, need to be built.

Notwithstanding the importance of replacing the mental health facilities, Oberlands House itself is no longer fit for purpose. The general population is living longer and this includes people with learning disabilities. The residents of Oberlands House are becoming older and more frail, which in turn leads to mobility problems, difficulty in moving around the building and increasingly impossible conditions for the staff to work in safely. These facilities will benefit not only the current residents of Oberlands House but also those who will need to be accommodated by the Adult Disability Service in the future.

Over the past twenty years, it has been HSSD policy to accommodate people with disabilities in smaller homes (for around 6 people) that are as much like ‘normal’ life, as far as possible. The Department owns and runs several homes of a domestic nature, whereas Oberlands House is institutionalised.

The design of Oberlands House does not lend itself to the care of the people who live there. The rooms are cramped, the interconnecting corridors are narrow and do not allow the easy movement of people in wheelchairs, there are slopes in the corridors which cause difficulties for people using walking frames (particularly when going downhill, as they can fall over the walking frame) and the building is becoming increasingly difficult and expensive to maintain. It does not meet the standards that the States decided should apply to private residential and nursing homes.

In addition, the HSSD spends a considerable amount of money on ‘off-island’ placements for people with learning disabilities. In 2007, the HSSD spent £2,020,897 on off-island placements for this client group alone. The issue of off-island placements was raised when the Public Accounts Committee (PAC) presented the National Audit Office (NAO) report entitled ‘Controlling Expenditure on Off-Island Placements’ to the

States in 2005 (Billet d'État II, 2005). The summary of the main findings and recommendations in the NAO report concluded that "more should be done to reduce the number and cost of off-island placements", and "developing facilities on island where justified on grounds of cost and better care".

The HSSD is proposing the development of three units of accommodation for adults with disabilities, two of which are to replace Oberlands House and one to provide accommodation for people either currently in an off island placement or who will need such a placement if no local provision is made.

The proposal to build a further unit of accommodation, at the same time as building units of accommodation to replace Oberlands House, would allow for some of the clients who are either currently accommodated in the UK or coming through the system now and are likely to require off-island care to be catered for locally at less expense and in facilities appropriate to their needs and therefore achieving the objectives cited in the Government Business Plan and in the PAC report in relation to off-island placements, as agreed by the States.

Two properties have been purchased to provide accommodation for the replacement of Oberlands House, The Oaks at Baubigny, St Sampson's, and Valderie at Rue Maze, St Martin's. These properties were purchased with the intention that the HSSD develop them to accommodate the residents of Oberlands House. It was, therefore, proposed to develop, on The Oaks site, one unit to accommodate six of the residents from Oberlands House and a second unit either to accommodate seven people who are currently in residential accommodation in the UK or who would otherwise need to be sent to the UK at considerable expense.

The original proposal has, however, been changed following consultation with the Environment Department on what development would be allowed on The Oaks site. The HSSD still wishes to build 3 homes for adults with disabilities but instead of building 2 homes at The Oaks, due to difficulties with site density etc, the Department is now exploring proposals to build the third home either on other land owned by the HSSD or to purchase a further property to develop.

It is still proposed to develop Valderie to accommodate the other six residents of Oberlands House.

## Giffard Ward (Princess Elizabeth Hospital)

| | | | |
|---|---|---|---|
| Submitting Department | | **Health and Social Services Department** | |
| Estimated Capital Cost | **£500,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **2nd Quarter 2010** | | |
| Completion Date | **3rd / 4th Quarter 2010** | | |
| Duration | **4 months** | | |

**Summary of Proposal**

Giffard Ward at the Princess Elizabeth Hospital is one of two wards that are used to care for patients following surgical procedures carried out in the hospital. These two wards (and the hospital theatres, sterile supplies and associated facilities) were built in the 1970’s using the most up to date design and construction techniques available at the time. This included encapsulating the steel frame of the building in asbestos.

As the HSSD’s site development has progressed, other areas in the Princess Elizabeth Hospital, which have been refurbished or upgraded, have been treated and the asbestos removed. Giffard Ward is the final area of the hospital that requires removal of asbestos and it also requires upgrading as the facilities on the ward do not meet current standards for the care and treatment of surgical patients.

Proposals were first put forward in 1995 (Billet d’État IV) and again in 1999 (Billet d’État XV) to upgrade the surgical wards. Ozanne Ward was upgraded in 2006 and the asbestos removed and the intention is to upgrade Giffard Ward once the Phase 5 clinical block is complete.

This proposal is for Giffard Ward to be upgraded to meet current Health Building Notes (HBN) and Health Technical Memoranda (HTM) standards and for the removal of the remaining asbestos. The HBN are a series of publications that set the UK Department of Health's best practice standards in the planning and design of healthcare facilities. They inform project teams about accommodating specific department or service requirements.

The HTM series of publications sets healthcare specific standards for building components - such as windows and sanitary ware - and the design and operation of engineering services, such as medical gas installations and fire safety requirements.

Both HBN and HTM guidance is used as best practice within the HSSD.

The work required to be undertaken on Giffard Ward includes:

- complete electrical rewire, including appropriate containment;
- replacing medical gas pipelines and control systems;
- enlarging bedhead spaces to meet current HTM guidelines;
- replacing flooring;
- replacing the fire detection system;
- improving segregation between male and female patients;
- replacing suspended ceiling;
- replacing the nurse call, TV and radio systems;
- upgrading bathrooms, toilets and shower rooms;
- upgrading nurse base and other ancillary areas (e.g. treatment rooms, disposal hold etc);
- removal of asbestos;
- redecoration.

It is necessary to complete Phase 5, the clinical block, first, as the HSSD must transfer patients on Giffard Ward to a different ward area in order to carry out the work. Currently, de Sausmarez Ward is being used to accommodate patients from the former Brock Ward, who were displaced when work commenced on Phase 5, and they will move into Phase 5 on completion. De Sausmarez Ward will then be available for ‘decant’ of the patients from Giffard Ward whilst the work is undertaken. It is estimated that the upgrading work and the removal of the asbestos will take approximately 4 months.

**eBorders IT system**

| | | | |
|---|---|---|---|
| Submitting Department | | **Home Department** | |
| Estimated Capital Cost | **£1,000,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **2009** | | |
| Completion Date | **2013** | | |
| Duration | **5 years** | | |

**Summary of Proposal**

This proposal is a series of projects which are closely inter-related insofar as they contribute significantly to the security of the Bailiwick's borders. This is identified as priority 7, Level 3 E in the current States of Guernsey Government Business Plan and to which the Customs and Immigration Service is committed to delivering.

The proposals identified will facilitate the most significant modernisation of the Bailiwick's border protection and immigration system for many years and will help to guard this Bailiwick and its economic interests, whilst welcoming the legitimate travellers and trade. The proposals are essential to protect identities and, by acting early, will assist the Law Enforcement agencies in targeting their resources and deterring those who would seek to cause us harm. It is not an option to do nothing and not to adopt these proposals will adversely impact on the social and economic wellbeing of both this Bailiwick and the wider Common Travel Area. Indeed, not to undertake these initiatives would leave the Bailiwick’s position within the Common Travel Area and the Customs territory of the EU in a vulnerable position as well as removing the ability to continue to issue British Passports to local residents.

## Police core IT system

| Submitting Department | | **Home Department** | |
|---|---|---|---|
| Estimated Capital Cost | **£1,200,000** | Estimated Additional Revenue Cost | **£60,000 per annum** |
| Start Date | **May 2009** | | |
| Completion Date | **2014** | | |
| Duration | **5 years** | | |

### Summary of Proposal

The recent States Report *"The Future of Law Enforcement"* sets out clear objectives on how Law Enforcement should be shaped and operated. This, together with the GBP (Government Business Plan) Priorities, demand that Law Enforcement operations become smarter and more efficient. In order to achieve this it is essential that existing systems are rationalised and that one Law Enforcement System for the Bailiwick of Guernsey is procured to deliver the necessary platform which all Law Enforcement personnel can operate from. Having multiple disparate Law Enforcement systems and duplication of data and effort is no longer acceptable. Furthermore, Law Enforcement is often the first point of entry into the Criminal Justice System and as such, for data accuracy and efficiency purposes, it will be necessary for Criminal Justice Systems to securely exchange data and eliminate duplication of effort. This is seen as crucial if we realistically wish to achieve a cohesive and joined up criminal justice system.

With the above in mind, it is necessary to replace the now outdated legacy LinkWorks System and migrate functionality into a single Law Enforcement System. This single Law Enforcement System can be achieved by further development of the new THEMIS Customs & FIS (Financial Intelligence Service – Jointly resourced by Police & Customs) System.

Obtaining security and information assurance accreditations is also necessary not only for extending PNN (Police National Network) access to all Law Enforcement locations but will also be necessary to access and process the proposed e-border initiatives. Currently PNN is only accessible from the Police network which is separate from the main States of Guernsey Network.

Without investment in infrastructure and providing evidence that we have the appropriate security accreditations, other Law Enforcement sites will be unable to utilise the PNN Network. This will severely hamper Law Enforcement's ability to carry out their existing duties and those proposed by the new e-borders directives. With this in mind, it is crucial that this proposal is considered in conjunction of the wider issues such as that of major national initiatives.

## Tetra Radio

| | | | |
|---|---|---|---|
| Submitting Department | | **Home Department** | |
| Estimated Capital Cost | **£1,800,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **June 2009** | | |
| Completion Date | **Dec 2011** | | |
| Duration | **2 ½ years** | | |

### Summary of Proposal

A Private Mobile Radio (PMR) that is fit for purpose is essential to maintaining and providing public safety. The emergency services such as Guernsey Police and Fire & Rescue are totally reliant on a communications system which enables them to respond to emergencies and control and communicate effectively. Whether it's a fire fighter wearing breathing apparatus in the centre of a major fire or a police officer at the centre of a public conflict a reliable and robust radio communications system is the lifeline to those presented to these types of situations. An "always on, always available" radio system is not an option. it is mandatory. It is similarly operationally critical for the safety and security of staff and prisoners at Guernsey Prison. Also, in the unfortunate situation of a major incident or disaster such as a large scale flood, fire or plane crash having a system which is resilient, robust, secure with guaranteed simultaneous talk time for all connected parties can result in saving lives.

Today the global system of choice is TETRA (**TE**rrestrial **T**runked **RA**dio) and the States of Guernsey Home Department have been operating a SELEX Communications system since 2001.

Under the Ofcom radio licence for public safety TETRA is now used in Guernsey by the following:-

- Guernsey Police
- Fire & Rescue Services
- Guernsey Prison Service
- Community Service
- Sea Fisheries Protection
- Customs Immigration and Nationality Service

There are plans underway to bring Ambulance & Rescue and many other States Departments online. Even non States entities are being considered such as Channel Island Air Search, Sark Ambulance and the Lifeboat Service.

Other jurisdictions such as the Isle of Man have extended their radio use to include transport services such as buses and trams and Jersey even include their beach life guards.

TETRA is the States of Guernsey standard for a PMR and is under continued and controlled expansion of its user base in order to maximise the cost benefit of owning such a system.

It is clear from the above and the business case that ensuring such a system is in place and fit for purpose is crucial. Jersey also face the need in 2010 for a major TETRA re-fresh and the Home Department has worked hard to reach an agreement in principle to take the opportunity to work with Jersey and procure a joint Channel Islands system, which will provide many benefits over having individual systems. Working together with Jersey to provide a resilient Channel Island based solution not only technically provides many benefits but would also demonstrate a new fresh approach to tackling what was once looked at as individual and isolated needs. A collaborative approach will not only improve services but increase procurement power, reducing costs and risks. This proposal represents a unique opportunity to work together with Jersey for the mutual benefit of the Channel Islands.

## Redevelopment of Maison Celine

| Submitting Department | | **Home Department** | |
|---|---|---|---|
| Estimated Capital Cost | **£15,000,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **2012** | | |
| Completion Date | **2014** | | |
| Duration | **2 years** | | |

### Summary of Proposal

A single site headquarters for the Home Department is urgently required, particularly to improve the delivery of joined up and cost effective Law Enforcement services. Currently, Police, Probation and Central Support Services operate from different locations. The Customs and Immigration Department has two main offices, again, both at different locations.

There is a pressing need to bring together, at one physical location, as many as possible of the services for which the Department has responsibility.

The main reasons for this are:

- to reduce high rental costs for non States owned property;
- to facilitate the provision of more cohesive Law Enforcement services in accordance with the recent "Future of Law Enforcement" States Report; and
- to rationalise and reduce the resources utilised in the provision of support services for the operational effort. This is exacerbated and resource intensive due to the multi-site location.

The proposed site forms part of the Police Station and is currently used by the Housing Department as flats, which are accessed from the courtyard of the Police Headquarters. The site footprint is actually twice the size of the flats when the waste ground to the East is taken into account.

Since the formation of the Home Department in 2004, a variety of options have been investigated in consultation with States Property Services, in order to provide the required solution. This proposal has been identified as the only really viable option.

The proposal would provide office accommodation for Customs and Immigration, Probation Service and Central Support Services, including Civil Contingencies and potentially a joint Emergency Services control room. The facility would adjoin the existing Police Station and as part of the project, the existing inadequate Custody suite would be relocated to the new wing allowing the Police to utilise the space for essential office space.

Since 2004, the Department has been working towards improving the overall Law Enforcement service provided to the public of Guernsey. However, subsequent increase on task demand, much of which is dictated by statutory legislation, has seen the Home Department and its component services outgrow current facilities and accommodation. The continued occupation of multi-site private sector accommodation is not seen as a cost effective solution. Some operational rationalisation has taken place and many support functions are now delivered more efficiently. However, in order to achieve a fully joined up Law Enforcement effort and to achieve staff savings in support functions it has been identified that a single office base is required.

This proposal will also significantly reduce the annual expenditure for rental of non States owned accommodation and free up some States owned property for use by other Departments, such as the Oberlands in regard to phase two HSSD accommodation plans.

**Belle Greve Wastewater Disposal Facility**

| | | | |
|---|---|---|---|
| Submitting Department | | **Public Services Department** | |
| Estimated Capital Cost | **Phase IV (b)- Outfall Refurbishment - £4m**<br>**Phase V - Replacement of Preliminary Treatment - £8.5m [including £4m for storm water retention option]** | Estimated Additional Revenue Cost | **None** |
| Start Date | **Phase IV (b) – summer 2010**<br>**Phase V – 2011/12** | | |
| Completion Date | **Phase IV (b) – Dec 2010**<br>**Phase V – Dec 2012** | | |
| Duration | **2 years** | | |

**Summary of Proposal**

Guernsey is totally reliant upon the existing Belle Greve Wastewater Disposal Facility to provide preliminary treatment and wastewater disposal for almost all foul wastewater arising throughout the Island. The existing facility now comprises preliminary treatment, two pumping stations, a long sea outfall and an auxiliary outfall.

The proposed project comprises:

- outfall refurbishment and upgrading [Phase IV(b)]
- replacement and upgrading preliminary treatment plant [Phase V]
- a potential option to include storm water retention capacity.

It should be noted that further investigations are required to establish the viability of refurbishing the long sea outfall pipe where it is submerged within an undersea tunnel; there is a potential future requirement to replace the long sea outfall at a budget cost of £10 million. Refurbishment and upgrading of the Red Lion Auxiliary Outfall are vital to ensure that a suitable alternative outfall remains available in the event that the long sea outfall has to be taken out of service.

Refurbishment of Belle Greve Wastewater Disposal Facility was one of the major projects prioritised by the States in October 2006, to be funded from the Capital Reserve. A five phase refurbishment commenced in 2006 and this project is Government Business Plan Priority 6 for Liquid Waste, Level 3, Item A.

In October 2007 [Billet XXI] the States resolved to '*allocate priority within the limited financial resources available for wastewater services to those measures necessary to sustain and develop the existing sewerage network, including measures* *to reduce ingress of saline and surface water'.* The first two phases of the refurbishment project were approved by the States in October 2007, and are now substantially complete. In February 2009, in accordance with the States decision in November 2008, the Treasury and Resources Department approved a capital vote of £2.5million for the refurbishment of the main pumping station [Phase III]. There is also approved a £500,000 budget for planning outfall refurbishment [Phase IVa].

The Belle Greve Wastewater Disposal Facility has operated continuously since it was commissioned in May 1971, without major refurbishment or upgrading. Refurbishment and upgrading of this 37 year old facility is urgently required to sustain existing wastewater disposal services. After 37 years in continuous operation, the Island's strategically vital wastewater disposal facility is no longer fit for purpose.

This project would complete comprehensive refurbishment of the existing Belle Greve Wastewater Disposal Facility as an interim measure until further wastewater treatment plant can be provided and thereafter as essential infrastructure required for full wastewater treatment.

It is intended that provision of wastewater treatment would follow on after refurbishment of the existing Belle Greve Wastewater Disposal Facility. A new treatment plant would receive flows from the refurbished Belle Greve Wastewater Disposal Facility. The planned refurbishment is therefore being designed so that it can be integrated with future wastewater treatment facilities. The proposed new preliminary treatment facilities, storm water retention capacity and refurbished outfalls would reduce the future cost of providing further treatment facilities. **In effect the planned refurbishment would provide the first stage of full wastewater treatment.**

## Cobo Foul Water Pumping Station

| Submitting Department | | **Public Services Department** | |
|---|---|---|---|
| Estimated Capital Cost | **£1,000,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **September, 2009** | | |
| Completion Date | **March, 2010** | | |
| Duration | **6 months** | | |

### Summary of proposal

The Cobo Pumping Station was built in 1998 to replace the existing pumping station. It pumps foul water from Cobo to the Haye du Puits from where it gravitates to Bellegreve. The catchment area for the station extends as far as La Passee and it is estimated that it serves about 3,000 properties.

In the event of a major station fault or a power cut, the station will surcharge the incoming sewers until they back up to an overflow facility which discharges into the surface water system draining to the Mare de Carteret pumping station and to sea through its short sea outfall. This occurs in 50 minutes in dry weather and even quicker in wet weather. This does not allow sufficient time for States Works to respond and the outcome is pollution of Cobo beach. The associated bad publicity of such an event adversely affects the tourist industry and local hotels and businesses. In addition pollution incidents affect the bathing water quality which is regularly monitored for compliance with European Union Bathing Water Standards. The results are displayed at beaches and on the Environment Department’s website.

The problem can be solved by the construction of storage tanks or installing large diameter tank sewers to increase the time period before overflow occurs. A standby generator could be used as a possible solution to cover failure of the power supply to the station. However this will require appropriate housing in this scenic coastal situation.

The advantages of proceeding with the proposed scheme are:-

1. The reduction of risk of pollution incidents at Cobo.

2. An improved tourist image of this beach and the Island generally.

3. The reduced risk of pollution benefits local hotels and businesses.

Should the scheme not proceed, the present risk of pollution of Cobo bay will remain.

The scheme is estimated to cost £1million but this will be subject to detailed design and costing. If approval is given, construction could proceed in September 2009 and be completed in March 2010.

**Permanent Civic Amenity Site**

| Submitting Department | | **Public Services Department** | |
|---|---|---|---|
| Estimated Capital Cost | **£1,200,000** | Estimated Additional Revenue Cost | **£200,000 per annum** |
| Start Date | **September, 2011** | | |
| Completion Date | **March, 2012** | | |
| Duration | **6 months** | | |

**Summary of Proposal**

The Environment Department presented the States Report on Waste Disposal to the States of Guernsey on 31 January 2007 (Billet D'Etat I, 2007). This report detailed the future requirements for waste disposal for the Island, as required by various previous resolutions of the States.

In the above report the Environment Department presented a draft Waste Disposal Plan which was approved by the States and this included the provision of a Civic Amenity Site as one of the facilities needed to deliver Guernsey's long-term waste strategy.

As a result of the enactment of the Environmental Pollution (Guernsey) Law, 2004, the Public Services Department has taken on the role of Waste Disposal Authority, with responsibility for the delivery of the Waste Disposal Plan.

This capital project is included in the Government Business Plan, Priority 6, level 4, item C (a) for Solid Waste.

The development of a full Civic Amenity Site forms part of the long-term waste strategy for waste disposal and is an essential component required to achieve a high recycling rate. However until the size and form of residual waste treatment facility is known, the extent of any dedicated Civic Amenity facility required to complement this cannot be specified.

The Civic Amenity Site (CA Site) would enable the public to deposit waste items which would not be acceptable in their normal household waste collection service. Various types of waste may be accepted at these facilities, with reuse and recycling options available for some, keeping these items out of the waste disposal stream.

A temporary waste recycling facility was introduced at Longue Hougue in 2008, and has proved very successful, although this cannot be described as a true CA Site as not all waste materials can be delivered there, in particular putrescible waste. The Outline Planning Brief for the residual waste treatment facility at Longue Hougue makes provision for a fully specified CA Site in the south west corner of the site.

Although there is provision for a CA Site at Longue Hougue through the OPB, this is subject to the footprint of the final residual waste treatment facility that will occupy the majority of this site. Concerns have also been raised about the implications of the Buncefield Fuel Storage Depot explosion, with recommendations restricting future developments within a certain distance from fuel storage facilities and therefore an alternative location may be required. The Environment Department is therefore currently looking at alternative locations for the permanent CA Site.

The design of such a facility will require consideration for a large hard standing area, drainage for run-off, provision of all utilities, easy access for the public, construction of an office, workshop and storage areas. The facility will also require a waste management licence to operate, administered by the Office of Environmental Health and Pollution Regulation.

The cost of a fully specified, licensed CA Site as described above is estimated to be £1.2 million. This estimate does not include the cost of purchasing land if the chosen site is not in States ownership.

Construction of the Waste Treatment Facility at Longue Hougue will require all of the site including the area occupied by the temporary CA Site. This will have to be removed to an alternative site until the permanent CA site has been constructed.

Approval of the permanent Civic Amenity site will enable the Public Services Department to complete this vital part of the Waste Disposal Plan and is an essential component required to achieve high recycling.

## Sewer Network Extension Plan

| | | | |
|---|---|---|---|
| Submitting Department | | **Public Services Department** | |
| Estimated Capital Cost | **£4,000,000 per annum*** | Estimated Additional Revenue Cost | **None** |
| Start Date | **2009** | | |
| Completion Date | **2014** | | |
| Duration | **5 years** | | |

∗ Including £1,000,000 per annum currently allocated to Public Services Department.

**Summary of Proposal**

The provision of public wastewater drainage and water supply networks commenced in the late 19th Century in response to epidemics of cholera and other waterborne diseases. To this day, an effective drainage system remains fundamental to protect public health.

In its 1998 Business Plan the former Public Thoroughfares Committee indicated its intention to extend the foul water sewer network to enable 95% of the population to connect to the network within 20 years.

In July 2000 the Committee produced the Network Extension Plan detailing how its target could realistically be achieved. The Plan retained the flexibility necessary to adapt to changing circumstances, particularly through knowledge gained from detailed topographical survey and site investigation of each individual project.

The extended sewerage network eliminates most of the pollution caused by leaking cesspit drainage systems, which become redundant as the property owners connect to main drain. Damage to sewerage infrastructure, pollution of the aquifer from leaking cesspits and offensive odour from septic sewage would also be minimised.

The States of Deliberation in October 2007 (Billet XXI) resolved to 'allocate priority within the limited financial resources available for wastewater services to those measures necessary to sustain and develop the existing sewerage network'.

This project is included in the Government Business Plan Priority for Liquid Waste (Level 3, Item B).

The previous level of funding of £3m per year allowed two major foul sewer network extension projects to be constructed simultaneously with minor projects programmed within budgetary constraints.

The major projects have evolved into two distinct areas of working. Firstly there was the extension of previously sewered areas in the north of the Island and secondly the construction of a new foul sewer to serve properties to the south and west of Vazon. This new system of spine sewers and pumping station in the south and west of the

Island will allow flows from Creux Mahie to be diverted to Belle Greve pumping station by mid 2009 and discharges to sea through the short sea outfall at Creux Mahie to cease.

Interrogation of the sewage tanker operational database has provided details of areas with cesspits that require a high frequency of emptying during the winter period which shows these cesspits are leaking inwards with groundwater. This also shows that cesspits leak outwards causing pollution of the groundwater. As most of the Island lies within the water catchment area this pollution could affect the Island's water supply.

The wastewater collection fleet, which currently stands at 36 tankers operated by 33 staff, will progressively decrease as the foul sewer network expands reducing labour, vehicle and maintenance costs. An additional benefit will be a significant reduction in the problems associated with hydrogen sulphide, particularly odour and damage to the fabric of the sewerage infrastructure.

The Network Extension Plan, in conjunction with the Term Contract for sewer installation, is providing the opportunity for a greatly increased number of properties to connect to the foul sewer network at a lower cost per property than previously achieved by tendering individual projects.

In 2008 the funding for the Network Extension Plan was reduced from £3m per year to £1m per year. However in order to achieve the 20 year programme and to cover increasing annual inflation rates funding will need to be increased to £4m per year.

Approval of this proposal will, by 2020, transform the Island community to one which has 95% of the population with drainage facilities. This fundamental public health facility is taken for granted in all other developed countries and should not be deliberately neglected once again by the States of Guernsey.

## Airport Pavements

| Submitting Department | | **Public Services Department – Ports** | |
|---|---|---|---|
| Estimated Capital Cost | **£84,500,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **2009** | | |
| Completion Date | **2011** | | |
| Duration | **2 years** | | |

### Summary of Proposal

The Guernsey Airport 'Pavements Rehabilitation Project' will realise the refurbishment and rebuilding of the various surfaced areas at Guernsey Airport, including the runway, taxiways and aprons (generically referred to as 'pavements'). In addition the proposed works include provision for improved drainage, pollution control, replacement of airfield ground lighting and relocation of navigational aids.

A baseline design has been determined through 2007 and 2008 by the Airfield Pavement Project Board and the Public Services Department (PSD). These options were presented to the States of Deliberation at its December 2008 meeting. Further work on the detail of those proposals and options is continuing with a view to representing the package to the States in 2009.

The proposed programme of works represents a major civil engineering project which will take around 24 months of construction work, some of it at night. This work has to be accommodated around the normal airfield operations, whilst maintaining emergency access at night.

The airport runway was last resurfaced in 1974. It has been subject to friction re-treatment on two separate occasions. During this time the pavement has, through routine use, worn down and this is reflected in a reducing runway classification number (PCN) over time. In addition, the runway lighting is now difficult to maintain, due to a lack of spares caused by obsolescence. The impacts of deterioration over time have also been realised in other paved areas, including the aprons (concrete parking areas for aircraft) and taxiways (routes between the aprons and the runways).

Whilst some restrictions are in place now as a result of the current pavement conditions, they are minimal and do not significantly affect the airport operation. However, any further delay in approving this major pavement rehabilitation runs the risk of bringing with it further restrictions on aircraft movements, or the need for abortive interim work, that would unnecessarily disrupt the routine business of the airport. A significant investment and programme of works at Guernsey Airport has to be progressed without further delay, in that respect this work is non-optional and cannot be further postponed.

The benefits to the Airport of carrying out this project are quite simply to ensure that the Airport can remain operational such that it can continue to generate revenue, but more importantly to continue to service each and every resident of the island, both for direct travel needs and indirectly through the availability of business travel, communications links etc. The programme of works will also seek to address as much current non-compliance against current aviation standards as can be reasonably achieved, thereby improving general standards of safety.

There remains the possibility, once the work is completed of attracting both new routes through existing operators and new operators to the island. This would lead not only to enhanced revenue growth of the Airport, but a wider contribution to the island economy. As a minimum, this development could accommodate the reintroduction of a jet service to London, which was suspended during the last quarter of 2008.

This project sits within the Government Business Plan where States Corporate Policies determine responsibility on the States to secure the provision of an infrastructure of resources and services for the People of Guernsey. The GBP Operational Summary for Public Services Department includes references to Guernsey Airport's aim to ensure the safe and expeditious movement of commercial and private aircraft, passengers and cargo to, from and at the Airport on the most cost-effective basis.

That duty includes responsibility for the provision of the airport infrastructure including runway, taxiways and aprons, technical aids and services for the landing, take off, ground movement and parking of commercial and private aircraft.

Further study on providing a runway extension as a second phase of works is currently being undertaken by the Policy Council. The budgeted sums above are based on the 'baseline' option as presented to the States of Deliberation at its December 2008 debate. No assessment in this capital prioritisation submission has been made by the Public Services Department to account for the potential costs of that additional work.

## Airport Radar

| Submitting Department | | **Public Services Department – Ports** | |
|---|---|---|---|
| Estimated Capital Cost | **£2,400,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **2010** | | |
| Completion Date | **2012** | | |
| Duration | **2 years** | | |

**Summary of Proposal**

The Air Traffic Control facility at Guernsey Airport provides a radar control service to aircraft operating within the airport's designated area of responsibility (including Alderney). The radar service is provided using a local, on-airfield, primary surveillance radar (PSR). This comprises of a tower, a rotating antenna, and various processors and feeds back to the administration/control tower buildings.

The principal role of the radar service is to enable ATC to maintain a safe separation distance between aircraft although it also provides some navigational assistance through the provision of headings and ranges to aircraft. The minimum permissible separation distance between aircraft is 3 nautical miles. In the event of a total loss of radar service the minimum separation distance would increase to 10 nautical miles, thus greatly reducing the rate of arrivals and departures. Due to the need to procedurally separate inbound and outbound aircraft, departures would also be severely restricted.

To ensure the availability of Guernsey's radar service, in the event that the local PSR is unavailable, data is also received from Jersey's PSR under a service level agreement. A reciprocal agreement also covers the provision of PSR data to Jersey from Guernsey.

There have been a number of times when one or other of the units has been temporarily removed from service for maintenance, failure or repair, and in such circumstances both islands have benefited from the agreement.

It is likely the replacement of Guernsey's PSR will be timed to coincide with the Jersey Airport PSR replacement, to ensure continuity of spares, bulk purchasing opportunities etc. It is hoped both islands will purchase the same equipment to maximise this opportunity.

The existing PSR (branded as a Watchman S system) was installed in March 1997 and had an expected operational life of 15 years. However, shortly after installation was completed the supplier, Siemens-Plessey, sold off its defence business to BAE Systems and merged its Air Traffic Management Division with Thomson-CSF of France creating a new company Airsys ATM, this was later re-branded as Thales ATM. This latter company terminated the Watchman S project in favour of its own development, Star 2000 and put a squeeze on funding to complete any further essential or future development of the Watchman S product.

Although six Watchman S systems were built, only two were installed and put into operation, one in Guernsey and one in Jersey.

Whilst the existing PSR is well maintained and has proven highly reliable the stock of spares we have is gradually diminishing and at some point we will pass the point where it will be considered safe to continue to maintain the current system in operation.

The PSR comprises a tower and rotating antenna, as well as an equipment cabin which houses the radar transmitter, receivers, signal and data processors and data distribution units. Radar data is sent from the radar cabin to the Air Traffic Control building, via a fibre optic link, where it is processed for display in both approach and tower facilities. The data is also sent via leased lines to Jersey ATC and a similar feed is received from Jersey. This facilitates the use of Jersey's radar as a backup for Guernsey and vice-versa.

It is worthy of note that, although the Jersey PSR has greater instrumented range than the Guernsey PSR (80 nautical miles rather than 60 nautical miles), due to its location the Guernsey PSR affords significantly better coverage to the North in the areas of interest to both Guernsey and Jersey ATCs.

Correspondingly, due to its location, the Jersey PSR suffers more from the limitations imposed by its operating environment as it has more visibility of the sea surface and therefore produces more "clutter" (unwanted echoes) and therefore its short range coverage is sometimes compromised where Guernsey's PSR coverage is solid.

## St Peter Port Harbour Pontoons

| Submitting Department | | **Public Services Department - Ports** | |
|---|---|---|---|
| Estimated Capital Cost | **£1,000,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **2009** | | |
| Completion Date | **2013** | | |
| Duration | **5 years** | | |

### Summary of Proposal

Guernsey Harbours provide pontoon mooring facilities for some 2,500 local boats and about 400 visitor boats at all times. This latter figure represents a substantial percentage of visitor bed stock. These pontoons are expected to be safe for public use and fit for purpose, representing for many, the first impression of the island. Existing marina pontoon equipment (except St Sampsons) is all in the order of 20 years old and has largely reached the end of its useful life. None can be properly inspected in situ and removal of large sections is not practicable without causing substantive disruption and costs.

Guernsey Harbours has instigated, with all necessary approvals, a rolling programme to replace existing pontoons over a 5-year period with a maximum capital sum allocation per annum of £250,000.

Since the marinas were built, the average sizes of both visiting and local yachts have increased such that much of our existing pontoons and mooring fingers are inadequate in size. Whilst some units can be refurbished, repaired and even re-used albeit in the most sheltered locations, the large majority of floating units now require replacement on a rolling basis.

Whilst it is accepted that this will not show an increased return on income, it is necessary to ensure that our customers, both local and visiting, receive the best facilities that Guernsey Harbours is able to provide. Guernsey Harbours, in relation to our visiting yacht numbers is in direct competition with marinas in Jersey, on the Normandy peninsular, North Brittany Coast and South Coast of England where standards are generally very good. It is only by providing the correct facilities that we can maintain our position in this competitive market.

Previous administrations have allowed that different pontoon suppliers be used to equip our marinas. This has shown to be a poorly thought out and non-cost effective strategy as there is a requirement for multiplicity of spares with the ability to interchange pontoon equipment between the marinas in the harbour.

Guernsey Harbours, after long-standing management experience of marina leisure pontoons and fittings, firmly believe that this rolling programme should run through one single supplier, thus ensuring continuity of supply, spares and service throughout the St

Peter Port marinas. The intention with a rolling programme such as this is to utilise Guernsey Harbours selected proprietary supplier which has previously been demonstrated to and agreed by both the Public Services and Treasury and Resources Departments.

This expenditure would prevent long-term accumulative repair/replacement costs and protect against possible substantial third party liability claims. It ensures continuity of present operational status and income streams for the various industries servicing the leisure marine market.

It is essential to continually demonstrate high quality mooring pontoons and facilities to marina users. This is partially achieved with the installation of quality moorings and pontoons. Any substantial delay to the rolling programme would clearly necessitate a large request to replace the moorings and pontoons.

It is, however, probable that revisions and upgrades within the Queen Elizabeth II Marina will need to be considered within the next few years, but probably as a standalone project to any other marina developments at the harbours.

The proposal ensures that the Public Services Department can deliver its mandate for Guernsey Harbours to operate in a commercial manner.

## Sarnia Work Boat

| | | | |
|---|---|---|---|
| Submitting Department | | **Public Services Department - Ports** | |
| Estimated Capital Cost | **£1,000,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **2010** | | |
| Completion Date | **2010/11** | | |
| Duration | **1 year** | | |

### Summary of Proposal

The “Sarnia” is a multipurpose vessel which is vital to the efficient management of Bailiwick marine operations. The current vessel was built in France and delivered in 1986. She is well maintained as evidenced by the numerous independent surveys carried out on her during her lifetime.

Sarnia was purpose built for Guernsey Harbours and has provided a first class service but some machinery and electrical parts are becoming increasingly difficult to source. She has already been re-engined once.

Industry standards and naval architects generally advise that 25 years is considered to be at the very limit of the useful economic life of such a hard working vessel and as such, Sarnia will be due for replacement in 2011 with a very similar size and specification of vessel. The approximate cost will be in the region of £1 million less a modest residual value of the Sarnia. The cost will ordinarily be funded from the Ports Holding Account.

The Sarnia is a vital component in the effective and efficient management of marine operations in the Bailiwick waters. She provides the means for delivery against our International obligations to provide appropriate ‘Aides to navigation’. She provides a diving platform to assist with maintenance and inspection of essential Harbour and island assets such as beacons, lighthouses, moorings and pontoons, Belle Greve outfall, navigational marks and buoy moorings. She is used as a tug and has been called into service in numerous island emergencies. She is a declared Search and Rescue asset, is outfitted for pollution response measures and is often used in support of the Lifeboat and St. John Ambulance rescues as well as police work, bomb disposal and other routine yet important activities.

It is therefore crystal clear that the island requires a fully functional, well equipped and reliable workboat. There would be considerable disruption should the Sarnia be forced out of service and hence the need to acquire a replacement becomes evident.

Naval architects recommend that a vessel which is so heavily used as Sarnia be replaced at the absolute worst after 25 years. This time is shortly upon us.

The replacement of Sarnia has been considered within the long term capital programme of Guernsey Harbours. Consideration has been given to the functions that the Island workboat performs and has concluded that the most efficient and effective solution to providing the variety of functions that Sarnia has carried out is simply to replace her with a similarly designed and specified vessel.

If the vessel is not replaced there is an increasing likelihood of the functions performed by it not being carried out. This could have disastrous effects in any maritime emergency in addition to increased costs for survey work etc. Maintenance of maritime navigational aids would not be possible leading to heightened risk to travellers and consequences for commercial passenger and freight sailings i.e. failure to meet our International obligations.

This purchase integrates with Strategic Policy 23 External Transport Links, the vessel is instrumental in assuring that these links stay operational.

This proposal has an impact on many other departments and their functions for example, Liquid Waste monitoring and surveys, Environment Department survey requirements, Commerce and Employment Department in connection with strategic links to Guernsey and Fuel import security.

The purchase is sensitive in that the current craft is operating at the very limit of its life expectancy. Any delays could a) add to the cost of a replacement, b) lead to increased maintenance costs of Sarnia and c) lead to potential catastrophic costs to the community were services be jeopardised by the workboat going out of service. The likelihood of service interruptions would have potential serious repercussions on the island economy.

The vessel will be built to current standards which will include provision for future advances in pollution control and electronics.

The proposal ensures that the Public Services Department can deliver its mandate for Guernsey Harbours to operate in a commercial manner.

## St Peter Port Harbour Careening Hard

| | | | |
|---|---|---|---|
| Submitting Department | | **Public Services Department - Ports** | |
| Estimated Capital Cost | **£23,000,000** | Estimated Additional Revenue Cost | **£50,000 per annum *** |
| Start Date | **2009 or 2010** | | |
| Completion Date | **2012** | | |
| Duration | **2 years** | | |

∗ It is anticipated that this proposal would generate significant income.

**Summary of Proposal**

Guernsey Harbours considers that the development of the Careening Hard as a long term marina solution to provide capacity for vessels is advantageous to satisfy both the need and the market for additional berths, particularly for larger vessels. This development would also stimulate associated businesses, not only for the harbour, but local marine businesses and local businesses on the waterfront.

The Careening Hard, presently, represents a very low earning capacity area of the harbour. The area is occupied by a limited number of drying moorings for smaller vessels, all of which could be accommodated elsewhere in the marinas.

The layout of a harbour determines its operating capacity, particularly the number of moorings available. Marinas have been built in both the Victoria and Albert Basins and the Queen Elizabeth II extension added to accommodate leisure market needs. These marina berths, of which there are some 2,500 are fully utilised and are operating at maximum capacity. There is also a waiting list of some 1,300 which shows no sign of decreasing. There is considerable disquiet in respect of the waiting list. Most recently, the inner areas of the St Sampson’s harbour were converted to provide an additional 300 or so smaller local moorings, offsetting some of those being lost through reclamation at Longue Hougue but making little or no long term inroad to the waiting list.

Larger vessels, offer a substantive income generating opportunity. It is clear there is a case for provision of additional moorings, particularly in the larger boat sizes, especially above 45 feet length overall, which will satisfy the aspirations of existing mooring holders and the wealthier end of the market alike. It is this sector of the market where the greatest opportunity exists for added value, as such vessels are more complicated, require more maintenance and technical support and most often, require full time or semi-permanent crew/support.

The proposal provides an opportunity for creation of a number of permanent marine jobs, principally boat maintenance, support and crewing. The proposed development offers an opportunity to better develop the marine tourism/activity, chandlery and engineering support sectors, which remains, as yet, untargeted.

The project would in practice be self-financing. Market comparison with other locations, both locally and on the South Coast, clearly suggest that income generated from mooring fees alone would be sufficient to justify the expenditure. ‘Public Purse’ funding is not required, although alternatively, some form of Private/Public Partnership could be contemplated.

Guernsey Harbours seeks initial approval to tender to employ specialist consultancy and if possible, local support for the project to provide contract administration and survey capabilities and the preparation of a Detailed Option Survey for consideration and approval.

States Property Services has indicated a top end estimated cost of £22.5m. Nevertheless, considerable income could be generated from the additional moorings and the payback period would be between seven and eleven years even using the cost of £22.5m.

Larger vessels offer a substantial income generating opportunity. Overall, there is a trend in the last 20 years towards a larger craft. This proposal will enable income generated currently at £10,000 per annum to increase to a figure, depending on what levels fees are set, in the order and upwards of £2 million. The suggested cost of £22.5 million would be offset by a payback period of between 7 and 11 years. If, as expected, build costs are below that, the period would be less.

A number of customers and marine businesses have stated that there is no point in putting a large boat on the waiting list because the likelihood of such requirement ever being met is so remote. Some customers have been on the list for 15 years and there is still no sign of a berth meeting their needs. For the larger sized boats, the waiting time is indefinite. This is a situation that on a general note is unacceptable both in terms of the commercial operations of Guernsey Harbours and the perception of Guernsey as a marina friendly environment.

Currently visiting yachts of more than 42 feet length and/or 8 feet draught can only moor at the ‘Swan’ pontoons in the Pool from which there is no access to shore. For these vessels, St Peter Port is an unwelcoming prospect. The development of a new marina would also therefore increase the attractiveness of Guernsey as a destination for owners of larger craft. Such tourists would likely have a higher disposable income to provide a boost to Guernsey’s economy.

The proposal would firstly positively impact upon the economy for the duration of the construction of the marina. Thereafter there would be increased growth in the economy and provide revenue for businesses from maintenance. More importantly it would continue to benefit from increased footfall in St Peter Port and increased tourism.

The proposal would allow 24 hour 7 days a week access to deep water that is a fundamental business requirement for stimulating marine business activities.

Expected completion could be by 2012 should the overwhelming business case be accepted and supported at political level.

It will be a landmark in itself and a vast improvement on the existing layout of the area. No other listed buildings will be affected.

Finally, this proposal ensures that the Public Services Department can continue to deliver its mandate for Guernsey Harbours to operate in a commercial manner, as determined by the States of Guernsey.

## St. Sampson's Marina Wave Screen

| | | | |
|---|---|---|---|
| Submitting Department | | **Public Services Department - Ports** | |
| Estimated Capital Cost | **£1,400,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **2010** | | |
| Completion Date | **2010/11** | | |
| Duration | **1 year** | | |

### Summary of Proposal

The St Sampson's Marina outer harbour was operational from 2004. Due to public objection and the political climate prevailing at the time, the original designed wave wall was rejected in favour of wave attenuation pontoons. These also carried with them a cost benefit, i.e. a cheaper option, and were installed on the south side only, as the design and layout of the north side did not facilitate the use of these pontoons.

As Guernsey Harbours feared at the time, damage has been sustained to both pontoons and fixtures on the north and south side due to swell action. The provision of a wave wall (or another suitable improvement scheme) will more readily protect the marina facilities against this swell action.

To date, damage to the value of £30,000 has already occurred to pontoons and fittings during periods of less than severe weather. With time, the rate of damage caused is extremely likely to increase, as the designed 'factor of safety' is continually eroded by 'wear and tear'.

The current Guernsey Harbours Management Team are of the opinion that the present infrastructure in the outer marina is not of a sufficiently robust design to withstand severe swell action. In the event of a severe swell action the probability of major (possibly total) damage to the existing facilities is (extremely) high, as evidenced by unexpectedly early failures. The implications of this are:

- Financial
    - Purchase of replacement pontoons and fittings (£150,000 at today's prices).
    - Removal of damaged pontoons and facilities (£40,000+).
    - Third Party insurance claims for damage to vessels (£1,000,000+).
    - Labour charges for fitting new pontoons/fixtures etc (£30,000).
    - Estimated loss of revenue in marina income (£150,000).

- Marine Community Confidence

    - Local loss of confidence in the States of Guernsey's management in this particular project.

    - Locally, Nationally and Internationally, loss of confidence in Guernsey to supply safe and secure moorings to the marine fraternity leading to loss of income to Guernsey Harbours in mooring fees and loss of income to Guernsey in visiting yachts spend. This, in the present highly competitive marina market could have a lasting effect.

It can be seen that current income together with Guernsey marinas worldwide reputation is at stake against an investment of £1,400,000.

If the wave wall (or another suitable improvement scheme) is not accepted as being essential, every storm, however minor, will always result in damage and therefore an ongoing cost to Guernsey Harbours. It is almost guaranteed within a 10 to 15 year period, that accumulative exponential damage repair costs and probably substantial financial implications will occur as a result of severe or very severe storms.

As a result of the most recent storm damage, Guernsey Harbours management, being ever mindful of their responsibilities to their customers, considered the worst case scenario plus the accumulative case scenario and determined that the most cost-effective solution is the installation of a wave wall to safeguard our customers assets at a previously estimated cost of £1,400,000 (subject to tender).

If the installation of a wave wall is not carried out we will continue to sustain damage to pontoons and fittings, which will increase exponentially as the assets age.

The vagaries of seasonal weather patterns indicate that the sooner this project is undertaken and completed the more secure St Sampsons marina facilities will be. However within the financial timetable of harbour works, we believe that it should be completed by 2011.

This solution would provide 'Peace of mind' to marina users that their vessels would have better protection in all weather scenarios and that Guernsey Harbours has acted in their best interests. Guernsey Harbours considers that any marine orientated engineering practice would support its conclusions.

The proposal ensures that the Public Services Department can deliver its mandate for Guernsey Harbours to operate in a commercial manner.

## Social Security/Income Tax IT system

| Submitting Department | | **Social Security Department and Treasury & Resources Department** | |
|---|---|---|---|
| Estimated Capital Cost | **£11,500,000** | Estimated Additional Revenue Cost | **None (Saving of £0.5million per annum)** |
| Start Date | **2009** | | |
| Completion Date | **2014** | | |
| Duration | **5 years** | | |

**Summary of Proposal**

Both the current Income Tax collection and administration system and the Social Security contributions system are running bespoke IT applications which utilise an outdated operating system, programming language, database structure and transaction processing system, support for which is not guaranteed beyond 2020. This combined structural platform is predominantly run in UK government departments and not elsewhere in the world. This means that expert knowledge and support for running these systems is both dying out and becoming more costly to obtain. The States of Guernsey must move away from this platform if it is to avoid the risks of falling into the situation of a major system failure from which there is no recovery or the inability to implement necessary legal and operational changes in income tax and contribution assessment and collection systems.

Priority 4 of the Government Business Plan ("Distribute wealth wisely in the community") highlights the strategy of the Treasury and Resources and Social Security Departments working more closely together to "Consider how savings might be achieved by merging and consolidating the collection, payment and treasury systems which, at times, overlap." A joint-Department working party has confirmed that the best opportunities for rationalisation are in the registration, revenue collection and debt management systems of both Departments. A new IT system will better enable this strategy to be implemented at the operational level.

The Treasury and Resources and Social Security Departments are estimating £11.45 million may be required for this project which will be funded 50:50 from the Capital Reserve and the Guernsey Insurance Fund. Although a contingency of 10% has been included, the reader should not interpret the estimated costs as a quote - they are intended to show an order of magnitude only. A more accurate figure will be obtained when a programme specification has been written and a full understanding of the business processes has been established.

The savings in the annual running costs for the new system – currently estimated to be £500,000 p.a. – would be returned to general revenue and the Guernsey Insurance Fund.

**Outline Business Case**

The States of Guernsey cannot afford to carry on developing and maintaining its existing Income Tax and Social Security mainframe-based IT Systems if it is to manage its costs wisely and provide a high level of service to the residents of Guernsey and Alderney. Options are therefore to either:

1. Migrate the two existing mainframe systems, substantially unchanged, on to a common server-based platform which has a longer predictable life span, or

2. Redesign the business processes of the two Departments, particularly in the areas of overlap, and develop the new systems onto a modern, well supported infrastructure, or

3. Find an existing package that substantially meets the needs of the respective businesses, with bespoke development to close the gaps between the requirements and the package solution.

The first option would do nothing more than remove the threat of the technology becoming obsolete and the availability of technicians with those skills sets becoming increasingly rare. Investing in the first option would ignore a golden opportunity to rationalise common functionality.

The second option would take advantage of the fact that the Income Tax system and the Social Security contributions system (not the benefits system) are for the first time coincident in the systems life-cycle of computerisation where both systems need to leave their mainframe platforms and to migrate to a server-based platform. Taking this option would need a substantial investment in analysis and business process re-engineering before developing a largely bespoke single system to deliver the common and individual requirements of both Departments.

The third option has the same objectives as the second option, but would look to achieve these through maximising the use of an existing package, such as SAP. The presumption is that the use of a package solution would be a lower-cost than a nearly wholly bespoke one. However, while the States strategy is to use an “off the shelf” solution wherever this is practicable, at this stage it is not possible to determine the best fit solution to the Income Tax and Social Security requirements.

The replacement of the existing Income Tax and Social Security Contributions IT systems, and their combination into one solution, is essential if the States is to meet the strategic objectives of the Government Business Plan in bringing Social Security and Income Tax procedures closer together. The new system will form the underlying secure and robust platform on which a fully integrated system can be built in order to meet business needs and achieve long term savings and efficiencies (for government, businesses and the general public).

**Estimated Replacement Costs**

| Item | Capital Cost | Revenue p.a | Notes |
|---|---|---|---|
| Programme specification | £1,000,000 | | Based on SSD experience |
| Programme Manager | £210,000 | | Based on 3 years full time |
| Hardware purchase | £500,000 | | One common hardware platform for live & business continuity purposes. Includes 3 year warranty |
| Operating Software | £150,000 | | Operating, security and backup software for 3 years |
| Contract Backfill | £350,000 | | Based on 10 EGIII staff over an equivalent of one year full time |
| Income Tax Implementation | £3,900,000 | | Includes internal resources of 2,650 man days and external resources |
| SSD Implementation | £4,300,000 | | Includes internal and external resources, pro rated based on size of income tax system |
| System & application support | | £350,000 | Based on current support costs |
| Contingency @10% | 1,040,000 | | Allowing for variables and unknowns |
| **TOTAL** | **£11,450,000** | **£350,000** | |

**Risks**

This will be the biggest ICT project ever undertaken by the States. There are potentially high risks in all categories. A further, significant, risk is in the bringing together of the functionality of two Departments with different core activities, business processes and culture.

## Cabernet Limited Recapitalisation

| | | | |
|---|---|---|---|
| Submitting Department | | **Treasury & Resources Department** | |
| Estimated Capital Cost | **£6,000,000** | Estimated Additional Revenue Cost | **None** |
| Start Date | **2009** | | |
| Completion Date | **2009** | | |

### Summary of Proposal

Cabernet Limited (the parent company of Aurigny Air Services Limited and Anglo Normandy Aero Engineering Limited) was purchased by the States of Guernsey in 2003 in order to secure the lifeline links into Gatwick Airport. The decision to hold the airline was reconfirmed by the States in 2005 as being the best strategic option for the island.

The shareholder guidance under which Cabernet Limited operates is to protect the landing slots at Gatwick Airport together with maintaining the 'lifeline' Channel Islands routes and the Manchester route in a cost effective manner.

The group operates with significant external debt financing and minimal equity and the Board of Cabernet Limited has requested that the balance sheet should be recapitalised by an injection of £6million of capital by the shareholder. This would enable the company to repay its existing short term borrowing facilities (which are guaranteed by the States).

In order for the Treasury and Resources Department to be able to recommend to the States the most appropriate long term funding model for the group, Cabernet Limited has commissioned a wide ranging independent report to, inter alia, analyse profitability and cash flow forecasts and review the efficiency and effectiveness of the utilisation of aircraft and other assets. This report will form the basis of Treasury and Resources Department's States Report on the strategic direction and funding arrangements of Cabernet Limited.

**Corporate Asset Management IT System**

| | | | |
|---|---|---|---|
| Submitting Department | | **Treasury & Resources Department** | |
| Estimated Capital Cost | **£600,000** | Estimated Additional Revenue Cost | **£16,700 per annum licence & maintenance costs** |
| Start Date | **2009** | | |
| Completion Date | **2011** | | |
| Duration | **18 months** | | |

**Summary of Proposal**

The greater responsibility for all States-owned property assets, now vested with the Treasury and Resources Department, initiated a search for a more robust proprietary data system. This needs to be used corporately by all States Departments and support a future move to asset based accounting which will require a formal asset register. The demands on any property database will be many and varied, but most importantly the database must be kept up to date with routine currently undertaken tasks, rather than separate dedicated administrative routines which attract varying levels of commitment. This is vital in the support of asset based accounting.

Experience with other property management systems has shown that they are most liable to “fail” due to the demands of the administrative commitment associated with maintaining the data. The data must be “live” so that it can be used with confidence. It would be difficult to justify the additional resources necessary just to populate and maintain the property data. Old fashioned, irregular manual updating, is more likely to lead to inconsistency of data input dependent upon the interest and commitment in the Departments concerned.

The solution is not simply the purchase of property portfolio software and a data population exercise. The success of the project will be judged by the management of change to encourage all States users to make the best use of the systems provided and support the management information streams. This is a valuable part of their existing routines and will better inform property initiatives, allowing the best performers to be promoted as benchmark standards with the poorest performer prioritised for improvement.

This data will inform strategic decision making for future disposals and property usage, while permitting dynamic asset management linkages to the general ledger.

**SAP Solution**

SAP is the corporate accounts package in which the States has invested considerable resources to obtain a consistent and comparable platform for all financial transactions.

The issues of security and access to information will be an extension of existing processes, covered and maintained by existing corporate policies. Dedicated property modules are available which fulfil the needs of property data collection. This also offers, an added benefit for asset based accounting, including moveable assets, which is a current work stream for the Treasury Section of T&R.

The Real Estate module provides the property database attribute repository and commercial transaction management, while the planned maintenance module provides the cyclic maintenance and moveable asset control systems. This will facilitate asset stock checks and enable the tracking and maintenance of these moveable items which has an added Health & Safety responsibility benefit.

Together the modules, in conjunction with the existing accounts processes, offer a viable solution, without the proliferation of multiple packages which may not communicate with existing software. Although there are other corporate property systems available, the States have already invested heavily in SAP.

The major benefits to be gained from a fully functioning system will include improved efficiency in terms of space usage, properties fit for purpose, reduced energy usage, increased life spans due to improved maintenance programmes and clear identification of redundant properties available for disposal. As a subsidiary benefit the States will be able to demonstrate a duty of care for all properties from a Health & Safety Legislation compliance aspect, ensure that any property related issues consider the definitive list of States properties, provide comparable data sources for all properties and the opportunity to set data lead benchmarks and the ability to provide graphical representations of these assets located within the island. This will mean that, for the first time in the history of the States land and property portfolio decisions can be made on the use of the assets with regard to their true corporate worth, both in the short, medium and long term.

| | | |
|---|---|---|
| IMPLEMENTATION SERVICES | | |
| Blue print for Real Estate & Financial Asset Management modules<br>Realisation of the Guernsey implementation<br>Authorisations module | | |
| | £344,500 | |
| LICENCES | Fixed charge | Annual Charge |
| Nett Licence Fees | £148,220 | £16,698 |
| **Total capital cost of software** | **£492,720** | |
| **Add contingency ( 20% )** | **£ 98,544** | |
| **Total Software budget (@ Feb 2008)** | **£591,264** | |

## IT Wide Area Network

| | | | |
|---|---|---|---|
| Submitting Department | | **Treasury & Resources Department** | |
| Estimated Capital Cost | **£3,600,000** | Estimated Additional Revenue Cost | **None (Saving of £1.25million per annum)** |
| Start Date | **2009** | | |
| Completion Date | **2012** | | |
| Duration | **3 years** | | |

**Summary of Proposal**

On 31st October 2003, the States approved the mandate for the Treasury & Resources Department (Billet XXIV, October 2003) which included responsibility for the States Wide Area Network (WAN) and expressed as: - "*The development of corporate policies concerning the States use of information and communication technology & the provision, administration & security of the States ICT network.*"

Since that time, the Department's corporate IT Section has managed and supported around 80% of the cross States WAN. A Review of the network is one of the key priorities of IT Section in the Department's Business Plan.

The States WAN has developed over the years in a fragmented fashion. While still meeting business needs it is doing so in circumstances where the telecommunications world has been changing rapidly as have business demands for the transfer of data, voice, CCTV and multi-media across the enterprise. It is for this reason an independent review of the Wide Area Network was conducted in the first half of 2008. The principal recommendation arising from the review is to create a business class network that supports the convergence of voice, data and image. In other words, allows all these services to run across a single digital network. This is in line with trends in the telecommunications industry and the strategy adopted by other organisations including the governments in Jersey and the Isle of Man.

The characteristics of a business class network are for a predefined end to end 'Quality of Service' that dictates the speed, capacity and resilience of the connectivity rather than whether the network is composed of fixed line or radio, wide or narrow bandwidth. In practice, 'Quality of service' is the ability to manage resources in order to provide different priority to different applications, users, or data flows, or to guarantee data flow performance levels.

The proposal is to then run telephony and CCTV as services upon this Business Class Network providing a resilient, reliable, secure and scalable solution. In delivering such a technical strategy, there has to be one network owner - the corporate IT Section, which reinforces the position agreed by the States in 2003. A further recommendation arising from the review is that the business class network is provided by a third party as a managed service, while a single government telephony service could be handled by an existing in-house team. CCTV would continue to be in line with existing strategy. This allows the in-house ICT teams to concentrate on business strategy and supporting ICT requirements rather than on the backbone infrastructure on which ICT is running.

The review indicated that local network service providers are already starting to build new networks with the support of UK based partners. They have a desire to support the States of Guernsey and bring new technologies to the Bailiwick - the island infrastructure will be the poorer without the States of Guernsey's business.

Further work would be necessary before the proposal can be formalised in terms of the more detailed and technical requirements and then subsequently put out to tender. The network is likely to take at least three years to become truly business class.

**Drivers for Change**

There are three principal drivers of change that have been identified for this project:

1. Delivery of public services to our Bailiwick community in the future requires a stable and secure underlying infrastructure.

2. To influence economic growth and to support innovations in health, education, public safety and public services requires a robust States network infrastructure.

3. Technology is changing - data, voice and media transmission can be run over one digital network and many recent technologies are now sufficiently developed to be regarded as mainstream with UK telecommunications companies already altering their infrastructure.

**Business Objectives**

From an operational perspective a number of strategic options have been considered which were measured against the following criteria:

- Delivering improved services to the public
- The ability to operate more cost effectively
- Establishing a secure, stable, confident and capable e-business environment
- Providing high levels of telecommunication resilience and connectivity
- Supporting government commitment to e-business and technical infrastructure
- Consolidation and enhancement of services
- Reduction in the sum currently spent on infrastructure services

**Costs**

| | *Estimated Capital Investment* | *Current Revenue Costs p.a.* | *Expected Revenue Costs p.a.* | *Revenue Savings Post Operational* |
|---|---|---|---|---|
| *WAN* | *£910,000* | *£2,456,000* | *£1,417,400* | *£1,038,600* |
| *Telephony* | *£1,845,000* | *£1,164,000* | *£952,000* | *£212,000* |
| *LAN* | *£500,000* | *Not determined* | *£100,000* | *Not determined* |
| *Programme Mgt* | *£300,000* | | | |
| *Total* | *£3,555,000* | *£3,620,000* | *£2,469,400* | *£1,250,600* |

**Risks**

A detailed risk analysis will be carried out and included within the States report that will be prepared if this project is prioritised for funding. However if the proposal is not accepted we run the risks of:

- Escalating running costs now and higher costs for change in the future
- Duplicating effort and an un-integrated approach
- Incapability to deliver some services
- Inability to make substantial savings
- Greater disruption to networks as changes are made
- Incapacity to take advantage of latest technologies and its efficiencies
- Reduction in local available skills in support of our existing technology
- Lack of supplier support for existing telephony switch network

## Corporate SAP Initiatives

| | | | |
|---|---|---|---|
| Submitting Department | | **Treasury and Resources Department and Policy Council** | |
| Estimated Capital Cost | **£2,100,000** | Estimated Additional Revenue Cost | To be assessed (although significant economies of scale could be achieved by utilising the existing SAP Support infrastructure) |
| Start Date | **Early 2010 (to allow sufficient time for the States Report to be completed and for a period of pre-project Change Management)** | | |
| Completion Date | **2013 (anticipated)** | | |
| Duration | **2 to 3 years (estimated)** | | |

**Summary of Proposal**

Proposal includes the following:

1. Primary element

   Extending the SAP Management Information System to include a Corporate Human Resource Management System – SAP HR

2. Secondary elements

   - Finalising the rollout of SAP Procurement
   - SAP Audit and Compliance Tool (or similar SAP audit tool)
   - Supporting the rollout of SAP Shift Planning
   - Additional SAP licensing

**Outline Business Case**

In January 2001 the States resolved to invest in a new approach to managing business information as provided by SAP.

SAP consists of a wide range of business modules, ranging from financial management and accounts, purchasing, real estate and plant maintenance, tax and revenue management, advanced reporting through to Payroll and Human Resource Management.

People are the most valuable and expensive resource available to the States. With in excess of 4,000 employees and an annual pay bill of some £165m the ability to monitor and manage this resource is critical. Such management and monitoring depends on timely access to up to date information about individuals and groups.

The current fragmented approach with disconnected bespoke systems scattered across the Departments is inefficient, time consuming and costly and, as a consequence, the States is seriously deficient in this area. Such deficiencies have been recognised specifically by:

- The GBP

- The Robinson Report into the Role of the States as Employer

- The “Developing Our Public Sector” initiative

- Various reports by outside bodies into the management of staff and access to key HR information.

Furthermore, these fragmented bespoke systems are now nearing the end of their useful lives and need to be replaced.

Benefits brought about through SAP HR would include sickness management; E-recruitment; reduced duplication; cost reductions through automation and work flow; increased productivity and improved strategic planning.

The States has already invested several million pounds in SAP which provides a platform on which to build the Human Resource Management system. As previously indicated, SAP HR is a critical element for supporting other corporate initiatives such as the Development of Our Public Sector the concept of shared services and responding to the Fundamental Spending Reviews - without which our ability to bring about greater efficiencies and better management would be greatly curtailed.

The Chief Officer Group recognises that the States will struggle to achieve meaningful efficiencies amongst its staff and ensure consistent processes and data collection without a modern corporate solution. In addition, initiatives such as performance and talent management, improved workforce planning, absence, management etc. would struggle to deliver meaningful benefits in the absence of one corporate HR solution.

The introduction of the HR module would help realise these benefits and enable the States to maximise the return on the investment it has already made in SAP.

**Appendix D**

STATES OF GUERNSEY

# Project Norman

## Phase One Report

ROTHSCHILD

12 February 2009

# Disclaimer

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This Phase One Report is being provided by Rothschild solely to the States. The Phase One Report is confidential and is provided pursuant to and subject to the terms of Rothschild's service contract with the States dated 12 November 2008.

The purpose of the Phase One Report is to help ascertain the capital requirements of the States and preferred debt funding strategy relating to the States' proposed capital expenditure programme, based upon forecast taxation receipts and other revenues, as well as planned expenditures and funding of specified reserves. The Phase One Report should not be used for any other purpose without the prior written consent of Rothschild. Under no circumstances shall Rothschild have any liability, whether in contract, tort (including negligence) or otherwise, for any use made of the Phase One Report for any purpose other than that for which it was provided or for any use made of the Phase One Report by any person other than the States.

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# Contents

# 1. Executive summary

## 1.1 Background

Thanks to its conservative fiscal policies and robust economy supported by a dynamic financial sector and a stable political environment, the Bailiwick of Guernsey ("Guernsey") has a long history of budget surpluses and has traditionally used its cash reserves to fund capital expenditures. Consequently, Guernsey has no material debt outstanding as of this date.

The new Zero-Ten tax regime, introduced by the States of Guernsey ("the States") in 2008 to maintain Guernsey's tax competitiveness with other jurisdictions, has had and will continue to have a significant impact on the States' corporate income tax revenues. The States have planned a two stage adjustment programme to accommodate the impact of the Zero-Ten regime. In the first stage, the States expect to fund budget deficits with cash accumulated in the contingency reserve, while economic growth and revenue enhancement measures implemented by the States help re-establish a budget surplus. In the second stage, additional measures will be taken as necessary to rectify any remaining fiscal imbalance and restore Guernsey to a stable financial position.

In parallel with the introduction of Zero-Ten, the States have launched a capital prioritisation process to identify the capital expenditure projects which should be progressed over the next four years. It is anticipated that funding for these projects will come from current cash reserves, future revenues and the proceeds of debt issued by the States.

## 1.2 Rothschild's scope of work

In November 2008, the States appointed NM Rothschild & Sons Limited ("Rothschild") to review:

i) Guernsey's financial condition following the implementation of the Zero-Ten tax regime and

ii) The funding requirements arising from the States' proposed capital expenditure programme.

As part of this mandate, Rothschild undertook the following in collaboration with Guernsey's Treasury & Resources Department ("T&R"):

- Review of the States' strategic objectives and fiscal policies
- Preparation of a cash flow model (the "Forecast Model") forecasting the States' future revenues, expenses, capital expenditures, reserve account balances and funding needs
- Analysis of the States' funding requirements in relation to its capital expenditure programme over the next four years
- Evaluation of the principal debt funding options available in the current markets
- Preparation of indicative financing terms based on feedback from a short-list of financial institutions active in both bond and bank markets.

This report ("The Phase One Report") presents the results of Rothschild's analysis and the recommended debt funding option to meet the States' objectives.

# 1. Executive summary

## 1.3 Key objectives of the States

We understand that the States have the following objectives:

- Estimate the financing requirements arising from the States' proposed capital expenditure programme
- Determine the optimal funding strategy to meet those financing requirements
- Optimise funding terms
  - Lowest possible cost of finance
  - Fixed interest cost for the lifetime of the debt
  - Long-term maturity to match the economic life of the underlying assets
  - No financial covenants to preserve maximum flexibility
- Maintain the Bailiwick's strong credit standing in the capital markets

While current debt markets are extremely challenging, we believe that debt solutions are currently available to meet each of these objectives.

## 1.4 Funding requirements

### *1.4.1 Capital expenditure programme*

Various Departments of the States have identified capital projects totalling approximately £354m intended to improve the infrastructure of the island over the next four years. All main sectors are represented: healthcare, education, transport and environment. The precise scope and content of the island's capital expenditure programme will be the subject of a special debate in the States in March 2009 (the "Capital Prioritisation Process"). In preparation for this process, T&R has evaluated the projects submitted by the various Departments and assigned them an indicative priority level: Priority 1 or Priority 2. Priority 1 projects, which are likely to be approved by the States, total £286m, with the majority of expenditures anticipated between 2009 and 2014. Priority 2 projects total £68m. A final decision as to which projects should be approved and funded will be made by the States in March 2009. However for the purpose of this Report and the financial forecasts set forth below, we have been asked to assume that only the Priority 1 capital projects, totalling c. £286m, will be approved.

The capital expenditure programme will likely be funded from the following sources:

- Existing cash in the capital reserve (£42m) and related interest income
- Annual transfers from the budget (£23m in 2009, which we assume will be kept constant in real terms in future years)
- Additional revenues from the capital projects themselves (e.g. solid waste solution project)
- Potential increases in tax revenues

# 1. Executive summary

- New debt issued by the States.

Based on our financial modelling, we estimate that the States will need to raise c.£175m of new debt between 2009 and 2010 to fund the Priority 1 projects.

### *1.4.2 Revenue shortfall following introduction of "Zero-Ten"*

The introduction of the "Zero-Ten" tax regime has significantly reduced the States' corporate income tax revenues. Corporate and bank income tax collections are expected to decline by c.£101m between 2007 and 2009. Consequently, we expect cash deficits to be realised over the next few years until the fiscal and economic growth measures implemented by the States successfully rebalance the budget. We have estimated that in the absence of measures taken to increase tax revenues or reduce revenue expenditure and ignoring the impact of the proposed capital expenditure programme (i.e. excluding the annual transfers to the capital reserve), the States will incur annual cash deficits of approximately £37m during the period 2009-2017. We understand that T&R does not wish to use debt proceeds to fund these budget deficits. Rather, funds accumulated in the contingency reserve will be drawn down as an interim measure to fund the revenue gap while measures designed to promote economic growth and increase other sources of tax revenue take effect. In authorising the use of the contingency reserve for this purpose, the States have stipulated maintaining a minimum cash balance in the reserve of c.£105m (plus accrued interest) as at 31/12/08.

### *1.4.3 Additional revenue required to support capex programme*

Adoption of a capital expenditure programme by the States will clearly increase the new revenue requirement, insofar as regular transfers to the Capital Reserve will be necessary to fund projects and any associated debt service.

As part of our financial modelling exercise we have been asked to estimate the quantum of additional tax revenue that would be required to restore fiscal balance by 2017 and support the States' proposed capital expenditure programme (see section 3 below). Our financial modelling suggests that based on reasonable assumptions the States will need to raise c.£52m p.a. of additional revenue from 2011 onwards (increasing with inflation) to balance the budget by 2017. This assumes that aggregate drawings of c.£138m from the contingency reserve are available during 2009-2017 to supplement the projected growth in tax revenue. Our forecasts suggest that this level of reliance on the contingency reserve will be consistent with the minimum balance threshold stipulated by the States.

While the identification of the source of this additional revenue is outside the scope of our Report, the scale of the additional revenue required suggests that only modest changes to property or individual income tax rates would be necessary to balance the budget.

## 1.5 Principal debt funding options

While a number of debt options are available, we consider that the most economical and practical funding solutions open to the States would be:

- A committed credit facility provided by a syndicate of banks

# 1. Executive summary

- A public or private bond issue in the capital markets

The table below summarises the pros and cons of these two funding options.

**Table 1. Pros and cons of a bank facility**

| Pros | Cons |
|---|---|
| No need for rating | Short-term funding (maturity typically up to 5 years in current market) |
| Private transaction | Commitment fees payable on undrawn facility |
| No minimum amount | Limited bank capacity and appetite in current market |
| No negative carry as capex can be funded as and when incurred | Typically floating rate of interest based on a spread over Libor and therefore would require interest rate hedging |

**Table 2. Pros and cons of a public bond issue**

| Pros | Cons |
|---|---|
| Long-term funding (up to 20-30 years) | Need for rating (but the States is now rated AAA by S&P) |
| Public or private transaction | Minimum issuance amount (c.£100m+) |
| Pricing based on Gilt yields, which are currently at very low levels | Risk of negative carry if capex is pre-funded |
| Fixed interest coupon | Challenging debt markets increase execution risk |

By agreement with T&R, we approached a small group of financial institutions active on both the bank and bond markets. The Bank feedback can be summarised as follows:

- There is a very wide range in indicative terms and pricing across the banks polled. This is reflective of the current high level of volatility and uncertainty in global financial markets.
- Certain banks are willing to consider arranging a credit facility to fund the States' capital expenditure programme. However, current market terms (short maturity and higher pricing) make this option sub-optimal.
- All banks suggest that the capital markets would welcome a bond issued by the States thanks to Guernsey's strong credit profile and AAA rating. However market conditions are currently challenging and pricing (both benchmark rate and credit margin) is volatile. Greater certainty as to investor appetite, term and pricing will only follow detailed discussions with investors on a name-disclosed basis.

# 1. Executive summary

## 1.6 Recommended debt funding strategy

### *1.6.1 Long-term Sterling fixed rate bond issue*

We believe that the capital markets currently offer the most optimal debt funding option for the States' long-term capital expenditure programme for the following reasons:

- Guernsey's AAA rating is likely to attract debt investors looking for high quality credits
- Bond markets offer long-term funding options, with maturities of up to 20-30 years, which will match the economic lives of the underlying assets and reduce the States' refinancing risk
- Long-term Sterling bond issues are priced off UK Gilt yields, which are close to cyclical lows resulting in a low overall cost of funds
- Long-term Sterling bond issues typically have fixed coupons, which provide a fixed interest cost and reduce hedging costs
- The capacity of the bank market for syndicated loans is currently limited

In our view, issuing debt in a currency other than Sterling (e.g. Euro or USD) is unlikely to offer material benefits in terms of market capacity or pricing given the size of the States' funding requirements. In addition, any foreign currency funding would introduce additional hedging costs for the States. Therefore we recommend that the States meet their funding requirements through long-term sterling bond issues.

### *1.6.2 Pre-funding of capex programme*

The timing of any capital markets issue will partly be a function of when the funds are required. As part of our mandate we have prepared a consolidated forecast of the expected timing of the capital expenditures planned by the various Departments and this is set forth in detail below.

Generally, there are three possible approaches to the funding of the capex programme:

- Fund as you go
- Partial pre-funding (up to a year in advance)
- Full pre-funding of the entire capex programme

Each of these approaches has its advantages and disadvantages. The main advantages of prefunding are to:

- Fix the States' cost of finance ahead of time
- Reduce execution risk
- Launch a larger and therefore more liquid bond issue, which would be more attractive to investors and receive better funding terms
- Take a more opportunistic approach to the timing of debt issuance based on changing market conditions

The main disadvantage of prefunding is the risk of negative carry, i.e. the risk of a negative differential between the interest cost payable on the prefunded debt and the (possibly lower) interest income that can be earned on the excess cash. The main advantage of funding on an "as you go" basis is the avoidance of negative carry. Its main disadvantage is execution risk, i.e.

# 1. Executive summary

the risk that capital markets are not as attractive as one would like at the very moment when a new issue must be raised to meet a funding gap.

An intermediate approach, which we have assumed for the purpose of our financial modelling exercise, is partial pre-funding, under which the States would issue debt up to one year ahead of the planned capital expenditure, to fix its interest costs, reduce execution risk and allow some flexibility if the States' capex programme is subsequently altered.

Under this approach, we have assumed for modelling purposes that the £175m of estimated debt proceeds required to fund the indicated level of capital expenditures would be raised as follows:

- c.£100m in 2009; and
- c.£75m in 2010.

### *1.6.3 Hedging considerations*

Long-term Sterling investors (including insurance companies and pension funds) tend to prefer fixed rate or index-linked bonds. If the States turn to the long dated fixed rate Sterling bond market to raise the required funds, the States' cost of funds will be fixed and no hedging will be required. If index-linked bonds were issued, the States' real cost of funds would be fixed but the States would remain exposed to future changes in inflation. As detailed later in this report, we are not convinced that index-linked bonds offer any compelling advantages to the States.

Depending on market conditions, the States should consider pre-hedging the cost of any debt issue. Considerable time may elapse from the date the States decide to launch a bond issue to the date of final pricing and funding, during which time market pricing can move substantially. During this time the States would need to run a competitive tender to appoint a lead manager, prepare the bond documentation and hold an investor roadshow. The cost of funds, which is determined by i) the underlying Gilt yield and ii) the credit spread required by investors, can fluctuate widely, particularly in the current economic environment. While it is difficult to fix credit spreads, the States can certainly lock the Gilt yield ahead of time, which represents the majority of the funding cost.

### *1.6.4 Rating considerations*

The States are rated AAA by Standard & Poor's, the highest obtainable rating for a sovereign credit. Given the size of the targeted bond issue and the States' strong credit profile, we believe that the S&P rating is sufficient to support a bond issue of the size required to meet the States' funding needs.

## 1.7 Proposed next steps

If the States decide to implement the Sterling bond financing option as recommended, the execution phase is likely to take up to two months with the following key steps:

- Competitive tender to appoint lead manager of the bond issue (2-3 weeks)
- Competitive tender to appoint hedge provider (if pre-hedging option selected) (1-2 weeks in parallel with lead manager appointment process)
- Execution of pre-hedge (if option selected)

# 1. Executive summary

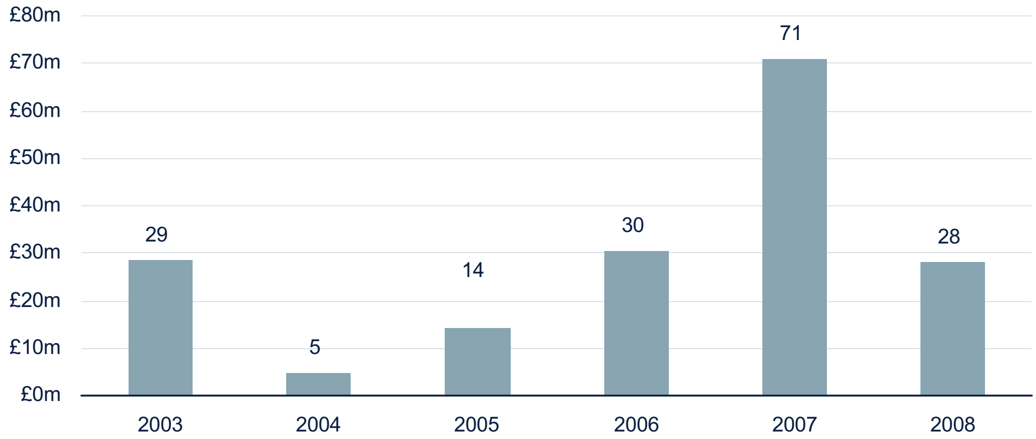
- Preparation of the legal documentation: offering circular, listing etc (up to 2 months)
- Confirmation of rating by S&P (1-2 weeks)
- Investor roadshow (1-2 weeks)
- Pricing of bond issue and close (1 week)

# 2. Guernsey's current financial condition

## 2.1 Historical budget performance

Due to its conservative fiscal policies, the States has a long history of budget surpluses, supported by significant tax collections from individuals and corporations. In 2007, the Bailiwick's operating surplus reached a peak of £70.5m compared to £30.5m the previous year, on the back of a 12.3% increase in total income and a slight reduction of ongoing revenue expenditure. In 2008 the budget surplus is forecast to have declined to £28m.

**Chart 1. Historical budget surpluses**




Source **States of Guernsey annual reports**

Past budget surpluses have allowed the States to accumulate significant cash reserves, which totalled £293m as of December 2007 (equivalent to 17.5% of GDP).

Each reserve has a specific purpose:

- Contingency reserve (£223m as at 31/12/08) is available to balance the States' budget in case of deficits and to fund other contingencies
- Capital reserve (£42m) is used to finance capital expenditure projects (other than routine capital expenditures funded out of the budget)
- General revenue account (£25m) has traditionally been a repository for part of the budget surpluses. However we understand that the majority of the funds in this account (£20m) will be used to fund the 2009 deficit.

## 2.2 Impact of Zero-Ten

In 2006, the States decided to introduce the "Zero-Ten" regime to maintain Guernsey's tax competitiveness with jurisdictions such as Jersey and the Isle of Man.

The key terms of the "Zero-Ten" legislation can be summarised as follows:

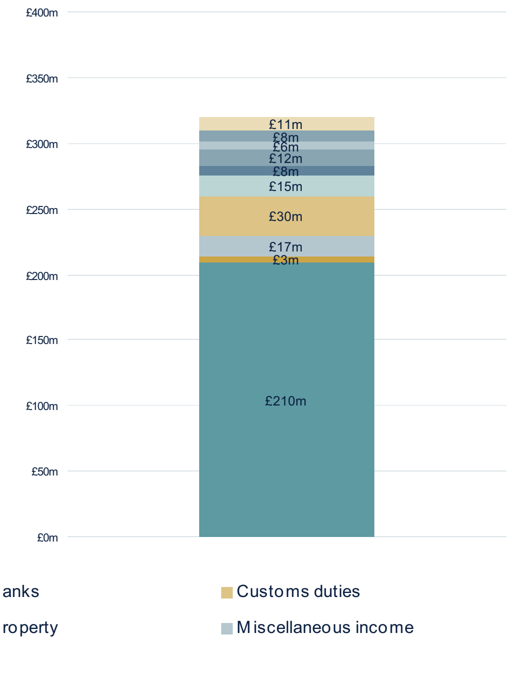
# 2. Guernsey's current financial condition

- 0% standard rate of tax on company profits
- 10% tax on some specific banking activities
- 20% tax on regulated utilities profits and property profits (in Guernsey)

This new tax regime has had and will continue to have a significant impact on corporate income tax revenues from 2008 onwards. Approximately 33% of Guernsey's total taxation revenues were formerly derived from corporate taxation on banks and other companies. This represented £121m of tax revenues in 2007. Following the introduction of Zero-Ten, income tax revenues from companies and banks are expected to decline to £20m in the 2009 budget, an 83% decrease.

**Chart 2. Revenue income analysis 2007 (£365m total)**


**Chart 3. Revenue income analysis 2009 (£320m total)**




Source **States of Guernsey annual reports**

Source **States of Guernsey annual reports**

In response to the challenges posed by the introduction of Zero-Ten, the States have adopted a two-stage action plan. The first stage, which commenced in 2007, includes the following:

- Measures to promote economic growth
- A shift of emphasis from corporate income tax to individual income tax
- Public sector expenditure restraint

# 2. Guernsey's current financial condition

- Increases in indirect taxes
- Increased collections from social security contributions
- If required, use of up to half of the funds in the contingency reserve to meet budget deficits (minimum floor of c.£105m)

The second stage will come into effect between 2011 and 2013. The nature and timing of the measures taken during the second stage will depend on the level of success achieved by the revenue enhancement measures introduced during the first stage, with a particular emphasis on:

- Performance of the economy
- Level of public sector income

The States' medium term goal is to achieve by the end of the second stage a proper fiscal balance and a sustainable tax base to support growth.

In responding to the challenges of Zero-Ten, the States enjoy a high level of tax flexibility. Current tax levels are low, even compared with levels in peer economies, and there is room for increases in tax rates (e.g. property tax rates) and/or the introduction of new taxes without jeopardizing Guernsey's competitive tax position.

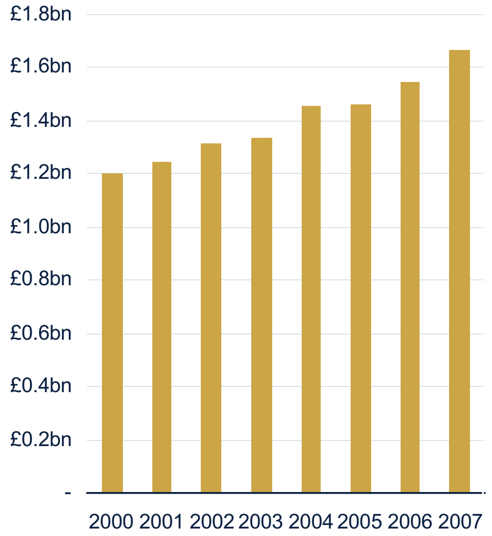
## 2.3 Impact of the current economic crisis

Guernsey has enjoyed strong economic growth and high levels of per capita wealth over the last few years:

- 4.7% annual average GDP growth over the last seven years
- GDP per capita of c.£27,000 in 2007, which is higher than Standard & Poor's median for AAA rated countries
- Very low unemployment rate (0.4% on average over the last 5 years)

# 2. Guernsey's current financial condition

**Chart 4. GDP growth**




Source **States of Guernsey**

**Chart 5. GDP per capita**


Source **States of Guernsey**

The current economic crisis, which has deeply affected the financial sector worldwide, is likely to have an adverse impact on Guernsey's economy, although we note that certain finance sub-sectors, particularly wealth management and captive insurance activities, have proved to be resilient in the past and some sectors such as tourism may benefit from the fall in the value of the pound, which is expected to prompt residents of the UK to take vacations in sterling-based locations rather than in Europe, the Americas or Asia.

In particular, the global economic recession is likely to have an impact on the States' revenues from individual income tax, which represented 48% of total revenues in 2007. In our financial model it is assumed that average individual taxable income changes in line with changes in real economic growth as measured by GDP. Our forecasts therefore assume a decline in average individual taxable income in 2009 and roughly flat growth in 2010 (in real terms) to reflect the likely impact of the current economic crisis.

## 2.4 Guernsey's credit profile

In January 2009, Standard & Poor's ("S&P") assigned its AAA long-term and A-1+ short-term sovereign credit ratings to the Bailiwick of Guernsey with a stable outlook. Guernsey's strong credit profile is supported by:

- Its robust economy
- Its flexible fiscal position, with room for new/increased taxes without challenging the island's competitive position
- Its significant cash reserves, providing a cushion against revenue shortfalls and additional capital expenditures
- Lack of any material existing debt

# 2. Guernsey's current financial condition

This new AAA rating by S&P should provide the States with price-competitive access to the capital markets and help to secure a lower cost of funds than would otherwise be available. Maintenance of this rating over time will imply a certain fiscal discipline but we are satisfied that continuation of the States' traditionally conservative economic and fiscal policies should enable Guernsey to address the ongoing requirements of maintaining a satisfactory ratings level.

# 3. Proposed capex programme

The States have identified a number of capital projects expected to be required in the coming decade to develop and maintain the island's infrastructure. We understand that the precise scope and content of the capital projects to be undertaken during the next four years ("Prioritisation Period") will be the subject of the capital prioritisation process to be debated in the States of Deliberation in March 2009.

In preparation for the capital prioritisation process, all capital proposals submitted by the various Departments have been subject to strategic review by T&R and categorised as either

- Priority 1, i.e. recommended for inclusion in the capital programme for the Prioritisation Period; or
- Priority 2, i.e. recommended for inclusion in the capital programme but not necessarily in this Prioritisation Period; or
- Priority 3, i.e. not recommended for inclusion in the capital programme.

We understand that there are a number of other capex projects, such as La Mare de Carteret education project or the wastewater treatment project, which are anticipated to commence after the Prioritisation Period and are therefore not reflected in our analysis.

The following tables list the Priority 1 and 2 projects and associated costs.

**Table 3. Priority 1 projects**

| Proposal | Cost Estimate £'000 | Cumulative cost £'000 |
|---|---|---|
| Education – College of Further Education Phase 2b | 2,700 | 2,700 |
| Education – Les Beaucamps School | 38,150 | 40,850 |
| Environment - Cobo Bay Bunker / Sea Wall Repair | 350 | 41,200 |
| HSSD – Adult Acute Mental Health Facilities | 25,400 | 66,600 |
| HSSD – Homes for Adults with a Learning Disability | 5,300 | 71,900 |
| Home – eBorders IT system | 1,000 | 72,900 |
| Home – Police core IT system | 1,200 | 74,100 |
| Home – Tetra Radio | 1,800 | 75,900 |
| PSD – Belle Greve Wastewater Disposal Facility | 15,500 | 91,400 |
| PSD – Solid Waste Solution | 80,000 | 171,400 |
| Ports – Airport Pavements | 84,500 | 255,900 |
| Ports – Airport Radar | 2,400 | 258,300 |
| Ports – St Peter Port Harbour Crane Strategy | 10,000 | 268,300 |
| Ports – St Peter Port Harbour Pontoons | 1,000 | 269,300 |
| Ports – Sarnia Work Boat | 1,000 | 270,300 |
| Social Security / Income Tax IT System | 5,500 | 275,800 |
| T&R - Cabernet Limited Recapitalisation | 6,000 | 281,800 |
| T&R – Corporate Asset Management IT System | 600 | 282,400 |
| T&R – IT Wide Area Network | 3,600 | 286,000 |
| **Total Priority 1 projects** | | **286,000** |

Source **States of Guernsey**

# 3. Proposed capex programme

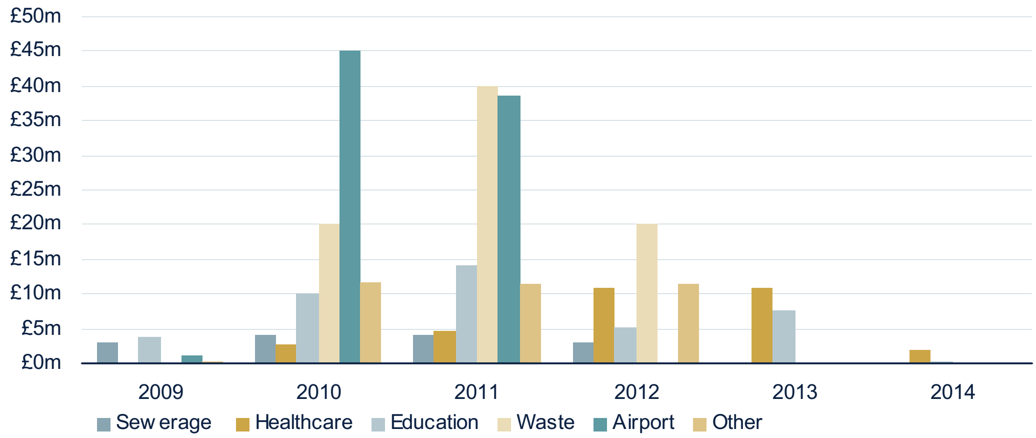
**Table 4. Priority 2 projects**

| Proposal | Cost Estimate £'000 | Cumulative cost £'000 |
|---|---|---|
| Culture & Leisure – Museums Store | 5,000 | 5,000 |
| Environment – Val des Terres Rockface | 200 | 5,200 |
| HSSD – Giffard Ward (Princess Elizabeth Hospital) | 500 | 5,700 |
| Home – Redevelopment of Maison Celine | 15,000 | 20,700 |
| PSD – Cobo Foul Water Pumping Station | 1,000 | 21,700 |
| PSD – Sewer Network Extension Plan | 20,000 | 41,700 |
| PSD – Permanent Civic Amenity Site | 1,200 | 42,900 |
| Ports – St Peter Port Harbour Careening Hard | 23,000 | 65,900 |
| Treasury & Resources – Corporate SAP Initiatives | 2,100 | 68,000 |
| **Total Priority 2 projects** | | **68,000** |

Source **States of Guernsey**

For the purposes of the financial forecasts underpinning this Report, we have at the request of T&R assumed that the projects to be funded following the capital prioritisation process will be the Priority 1 projects. These projects aggregate approximately £286m with the majority of capital expenditures anticipated between 2010 and 2012. The following graph illustrates the indicative timing of the expenditure.

**Table 5. Timing of Priority 1 capital expenditures**




Source **States of Guernsey**

The Solid Waste Solution project is expected to generate offsetting future revenues which are currently anticipated to be £5.0m per annum.

# 4. Financial forecasts

Following detailed discussions with T&R and in-depth analysis of the States' historical and budgeted revenues, expenditures and reserve balances, Rothschild prepared a model to forecast the States' revenues, expenses and capital expenditures (the "Forecast Model"). The key objective of the Forecast Model was to identify the likely quantum and timing of the funding and revenue requirements associated with the capital prioritisation process.

## 4.1 Forecasting the States' revenues - key assumptions

### *4.1.1 Inflation*

According to T&R, the majority of the States' revenues and expenditures are expected to grow with inflation. Guernsey's' RPI is therefore a key assumption in the Forecast Model.

For 2008, we have used the States' inflation assumption of 5.5% as per the 2009 budget. Our inflation assumption from 2009 onward is the sum of the following:

- The Bank of England's target UK CPI rate of 2% (This was adjusted down to 1% in 2009 and 1.5% in 2010 to reflect the current economic crisis)
- The historical average spread between UK CPI and UK RPI, estimated at 1.03%
- The spread between UK RPI and Guernsey RPI, estimated at 1.00% as per T&R's recommendation.

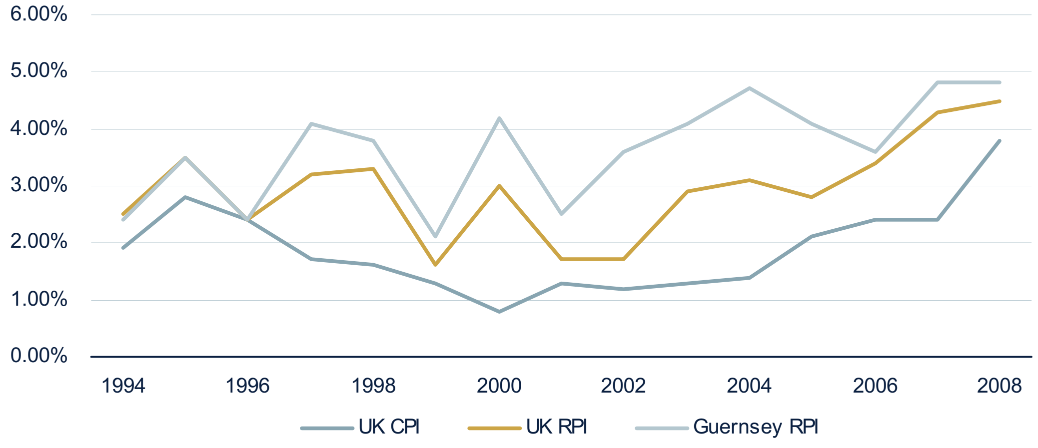
Based on this approach, our Guernsey RPI assumptions in the Forecast Model are as follows:

- 2008: 5.50%
- 2009: 3.03%
- 2010: 3.53%
- From 2011 onwards: 4.03%

It may be noted that the 2008 and 2009 inflation assumptions have a limited impact on the forecasts as the Forecast Model reflects the States' budgeted revenues (excluding individual income tax) and expenditures in these years.

# 4. Financial forecasts

**Chart 6. Historical inflation trends**




Source **Bank of England, Bloomberg**

### *4.1.2 Real Growth rate*

Our review of the States' individual income tax collections over the last 4 years demonstrated that this revenue line has grown at a higher rate than inflation (i.e. growth in real terms).

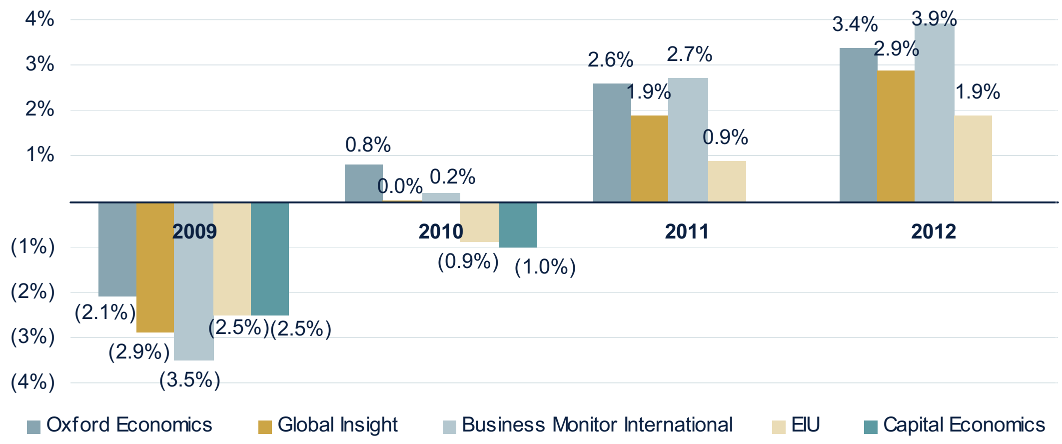
- 2003: RPI+2.14%
- 2004: RPI+0.46%
- 2005: RPI+0.35%
- 2006: RPI+2.23%

T&R's preliminary estimates of individual income tax collections for 2007 and 2008 also suggest a real growth rate (i.e. above inflation) of c.2.00%.

To forecast the future rate of growth of individual income tax collections, Rothschild has assumed that average individual taxable income increases or decreases over time at a rate equal to the sum of a) the inflation rate and b) the rate of real growth in the economy. For the rate of real economic growth in Guernsey Rothschild has used as a proxy the UK GDP growth forecasts of several economic forecasting agencies as illustrated in the graph below.

# 4. Financial forecasts

**Chart 7. UK GDP forecasts**




Source **Oxford Economics, Global Insight, Business Monitor International, EIU, Capital Economics**

For the purpose of the Forecast Model base case scenario, we have used the average of the UK GDP forecasts in the above chart:

- 2009: (2.7%)
- 2010: (0.2%)
- 2011: 2.0%
- 2012: 3.0%
- From 2013 onwards: 1.0%

We have also run a stressed case using the minimum UK GDP forecasts in the above chart:

- 2009: (3.5%)
- 2010: (0.9%)
- 2011: 0.9%
- 2012: 1.9%
- From 2013 onwards: 1.0%

This is a deliberately conservative approach but it is designed to ensure that the States' fiscal position will remain robust even in a severe economic downturn.

It should be noted that i) Rothschild is not an economic forecasting firm and relies on views published by third parties and ii) we have assumed for the purposes of the Forecast Model that Guernsey's economy would exhibit a similar real growth pattern as the UK's, even though our analysis did not indicate any particular short-term correlation between the UK and Guernsey's historic GDP growth rates.

# 4. Financial forecasts

### 4.1.3 Other key assumptions

Below is a non-exhaustive list of other important assumptions in the Forecast Model:

- Individual tax collection revenue
  - Number of tax returns stable at 46,246
  - Average pension contribution allowance (superannuation) grows at RPI + real growth assumption (as detailed above)
  - Ratio of main tax deductions to individual taxable income remains constant
  - Individual income tax rate remains at 20%
- Budgeted 2009 revenue and expenditure numbers (excluding individual income tax revenue)
- Additional £13m new non formula led expenditure from 2010 onwards
- Annual £23m transfer from budget to capital reserve (indexed at Guernsey RPI)
- Interest rate on contingency reserve set at UK RPI+2%
- Interest rate on other States' reserves set at 3%

Please note that the forecasts in this Phase One Report and our conclusions are based on a number of assumptions (only some of which are set forth above), which we believe are reasonable and have been agreed with T&R. Any changes in these assumptions, including the assumed inflation rate, real growth rate, revenue and expenditure growth rates, capex profile, delay and/or cost overruns among other factors could materially change these results.

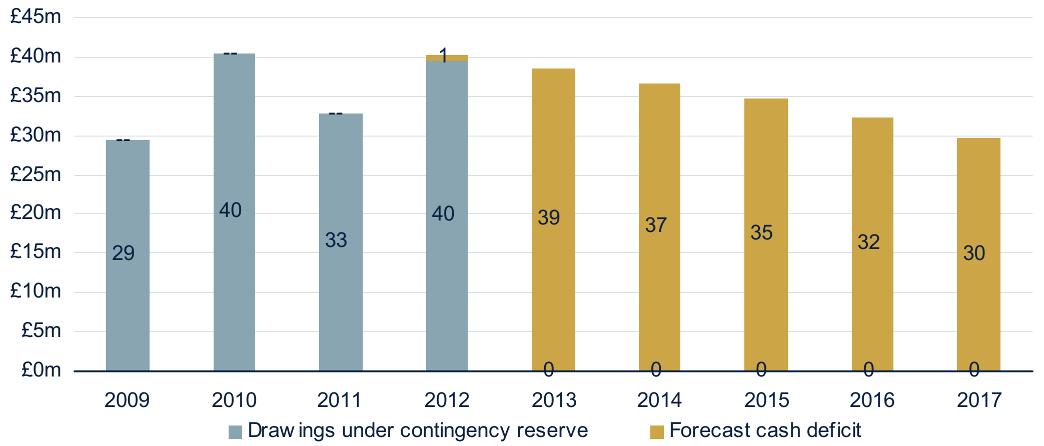
## 4.2 The funding gaps

### 4.2.1 Future budget deficits under Zero-Ten

The transition to the Zero-Ten tax regime has significantly altered the quantum and composition of the States' tax revenues. The following graph illustrates the forecast revenue deficits after payment of routine capital expenditures and before any transfers to the capital reserve (i.e. excluding the impact of the proposed capital expenditure programme).

# 4. Financial forecasts

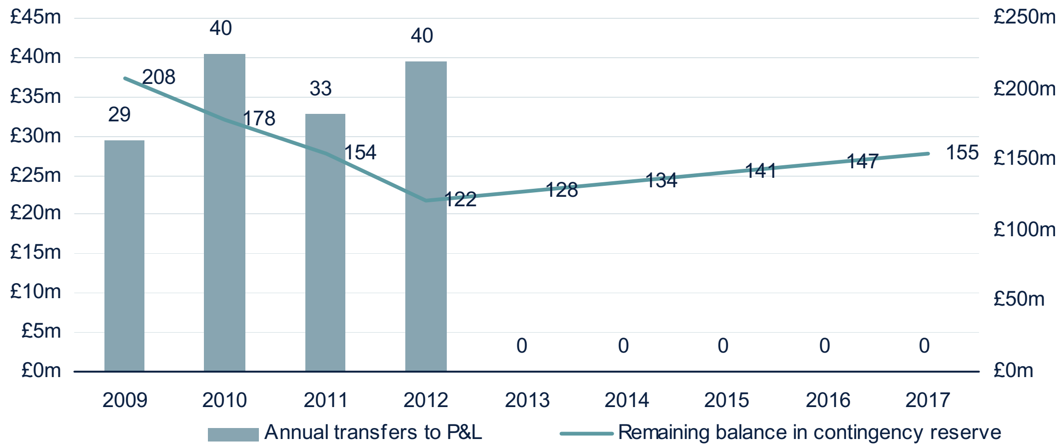
**Chart 8. Annual drawings from contingency reserve and forecast cash deficit**




Source **Forecast Model**

The chart above shows that during 2009-2012, drawings from the contingency reserve should suffice to meet projected budget deficits. However in 2013 and subsequent years the amounts available to be drawn from the contingency reserve fall to zero because the minimum balance stipulated by the States is reached. This creates an estimated revenue gap during 2013-2017 of c.£173m. While the balance of the contingency reserve stood at £226m as of 2008, the States resolved in June 2006 that only half of the contingency reserve (plus accrued interest) would be made available to fund deficits arising from the introduction of Zero-Ten. Hence in 2013 and subsequent years, additional sources of revenue will be required to balance the budget (we understand that the States do not intend to raise debt to fund budget deficits).

**Chart 9. Contingency reserve transfers to budget and remaining balance**




Source **Forecast model**

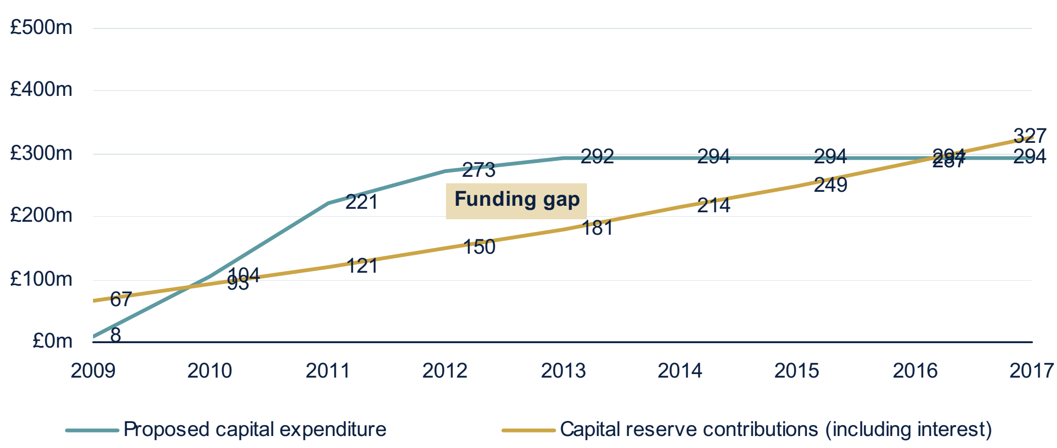
# 4. Financial forecasts

### *4.2.2 Capex funding*

The States expects to fund its capital expenditure programme with i) cash accumulated in the capital reserve, ii) revenues from specific capital projects such as the Solid Waste Solution (£5.0m indexed from 2009) and iii) borrowings.

As of 2008, the capital reserve balance stood at £42m. Going forward, we understand that the States will transfer £23m per annum (indexed with inflation) from the budget to the capital reserve. Our financial model suggests that this level of funding will, over the long term, suffice to fund the Priority 1 projects. However the timing of the proposed expenditures will precede the build-up of cash in the capital reserve. Consequently there is a funding gap that will have to be met through issuance of debt. This is illustrated in the graphs below.

**Chart 10. Funding gap (Priority 1 projects only)**




Source **States of Guernsey**

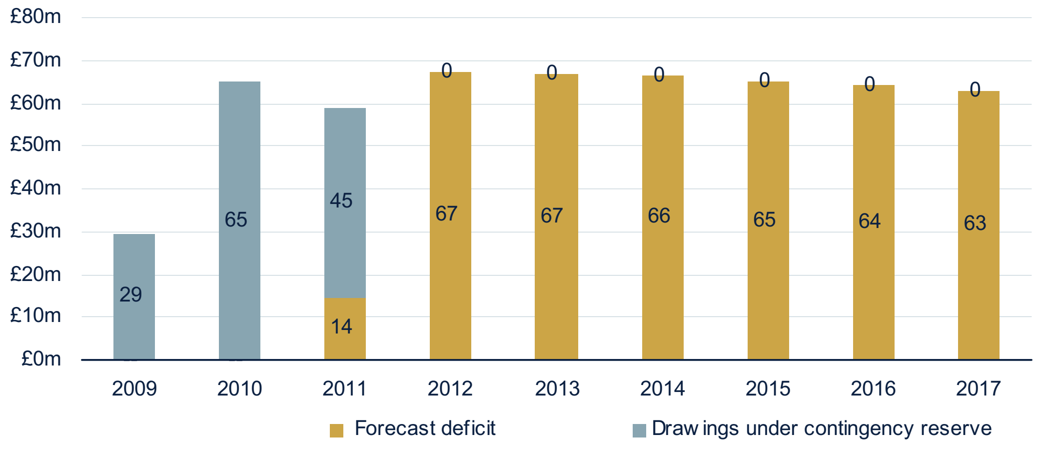
The foregoing chart illustrates the funding gap for Priority 1 projects only (including provision for inflation). Should the States approve additional projects, the funding gap will widen and the annual transfer to the capital reserve will likely have to be increased.

We understand that the States is prepared to consider financing this funding gap with debt. Section 5 of this report reviews the main debt financing options of the States.

The following chart shows how overlaying the proposed capital expenditure programme (Priority 1 projects only) on top of the Zero Ten deficits impacts the timing and quantum of drawings from the contingency reserve and future revenue requirements. In summary, the contingency reserve floor is reached two years earlier (2011 instead of 2013) and the additional revenue requirement is higher.

# 4. Financial forecasts

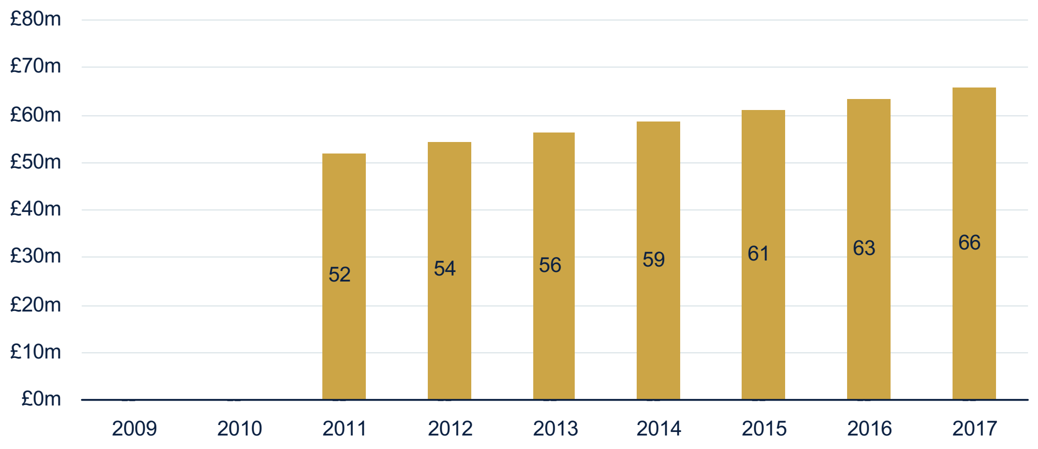
## Chart 11. Annual drawings from Contingency Reserve and forecast cash deficit




Source **Forecast Model**

At the suggestion of T&R, we have modelled the potential impact on future budgets and the contingency reserve of introducing new or increased taxes starting in 2011, on the assumption that the additional tax revenues grow in line with inflation. On this assumption, overlaying the capital expenditure programme (Priority 1 projects only) on the post Zero-Ten revenue forecast, we have estimated that incremental tax revenues of £52m in 2011, growing thereafter with inflation coupled with £138m of drawings from the contingency reserve, will be necessary in the base case economic scenario to offset the impact of Zero Ten and the capex programme and balance the budget by 2017. The following graph shows the profile of these additional revenue requirements.

## Chart 12. Additional revenues required to balance budget by 2017

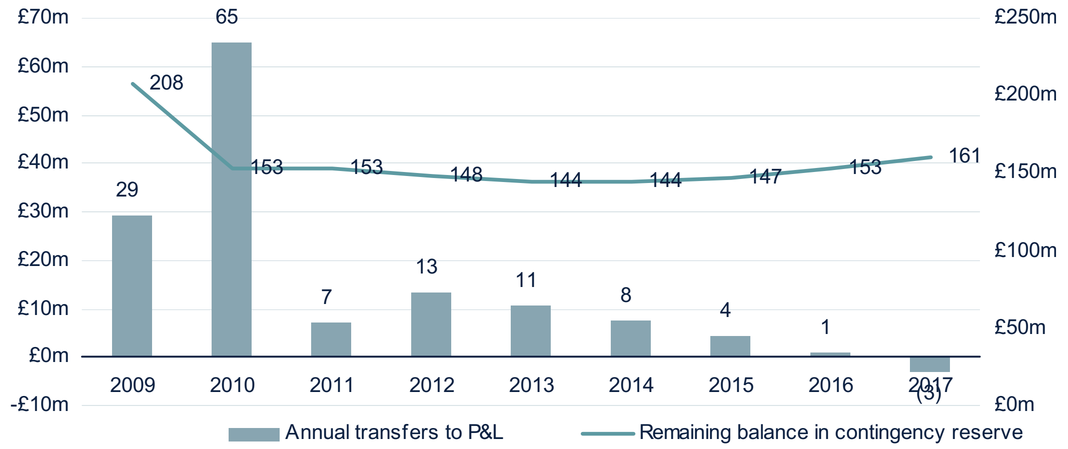



Source **Forecast Model**

# 4. Financial forecasts

The following graph shows the profile of the drawings from the contingency reserve under this scenario, which combined with the additional revenues illustrated above are necessary to balance the States' budget by 2017.

**Chart 13. Contingency reserve transfers to budget and remaining balance**




Source **Forecast Model**

## 4.3 Potential solutions

In order to close this revenue gap and fund the capital programme, the States are likely to require some combination of i) additional tax revenues and/or ii) expenditure restraint.

### *4.3.1 Additional tax revenues*

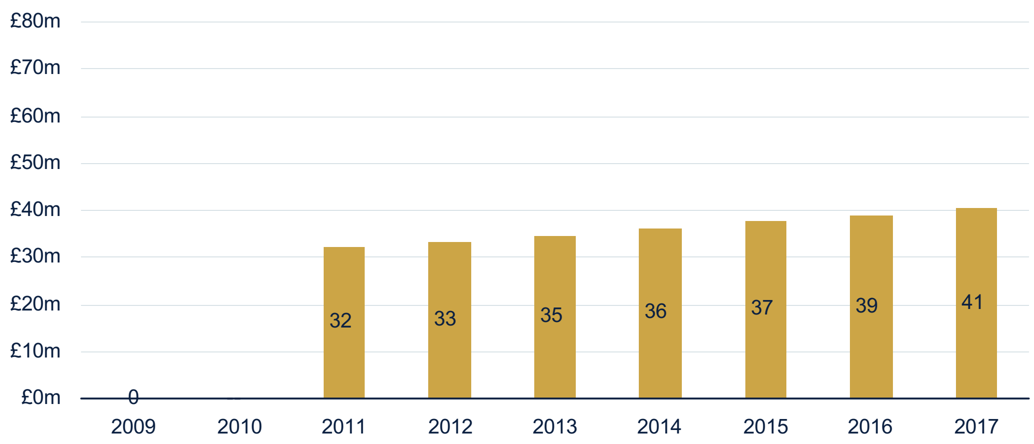
As pointed out by S&P, the States' traditionally conservative fiscal policies give it considerable flexibility of approach in deciding how to raise new revenues. Possibilities include increases in property taxes, increases in personal income tax rates, rises in indirect taxes etc. Given the modest scale of the additional revenue requirement, it is likely that only modest increases in tax rates are required. Measures to raise the incremental revenue are, however, outside the scope of our work.

### *4.3.2 Reduced budget expenditures*

As an alternative to tax increases, the States could seek to control the growth of expenditures. Following discussions with T&R, we have run a scenario where budget expenditures grow at (RPI-2%) over the 4 year period from 2010 to 2013 and at RPI thereafter. Our model suggests that such budget tightening measures would reduce the size of the deficit but would not alone be sufficient to eliminate the need for additional revenues as illustrated by the graphs below.

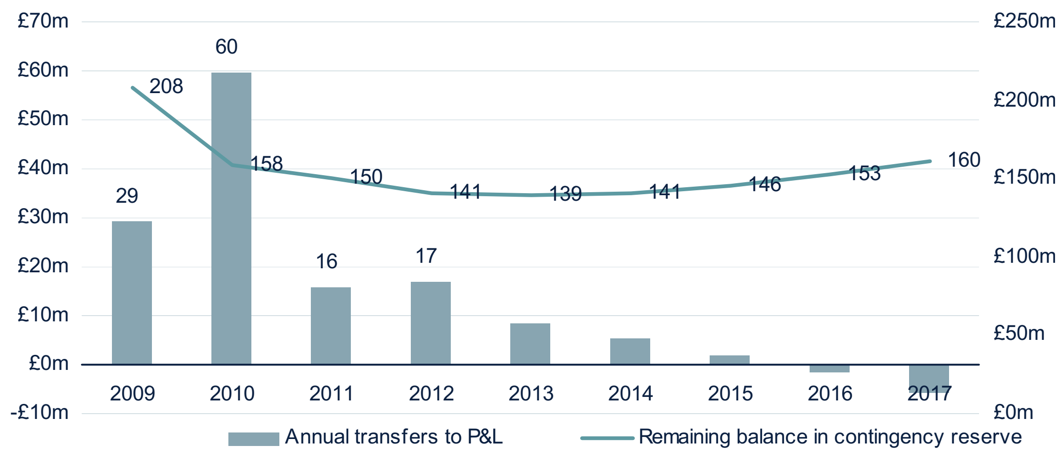
# 4. Financial forecasts

**Chart 14. Additional revenues required to balance budget under "expenditure restraint" scenario**




Source **Forecast Model**

**Chart 15. Contingency reserve transfers to budget and remaining balance**




Source **Forecast model**

### *4.3.3 Reduced capex programme*

Another way to reduce the States' deficit would be to scale back the capital expenditure programme, thereby reducing the need to transfer cash from the budget to the capital reserve.

### *4.3.4 Conclusion and recommendation*

Based on the results of the financial model and discussions with T&R, we have settled on a "base case" financial forecast that involves the following:

# 4. Financial forecasts

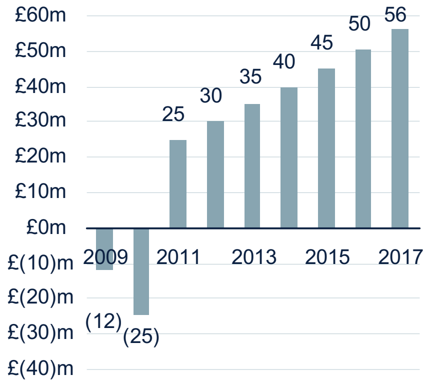
- £175m of debt issuance in 2009-2010, the proceeds of which are credited to the capital reserve
- Introduction of £52m of new revenues starting in 2011, rising thereafter with inflation
- Drawings under the contingency reserve as required to fund projected budget deficits (£138m over 2009-2017)

Under this scenario, using our "base case" GDP growth assumptions and the other modelling assumptions outlined above, it would appear that Guernsey could:

- Fund the Priority 1 projects as currently scheduled;
- Limit drawings under the contingency reserve in accordance with the guidelines previously adopted by the States and;
- Restore fiscal balance by 2017

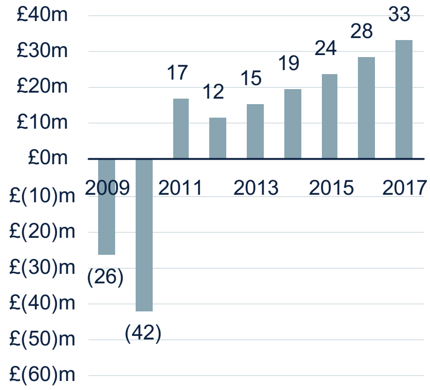
The following graphs illustrate the outcome of the base case scenario. Please note that the forecasts and our conclusions are based on assumptions that we believe are reasonable and have been agreed with T&R. Any changes in these assumptions, including the assumed inflation and real growth rates, revenue and expenditure growth rates, capex profile, delay and/or cost overruns among other factors could materially change these results.

**Chart 16. Revenue surplus (deficit)**




Source **Forecast model**

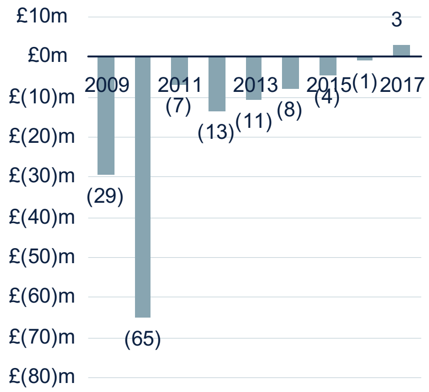
**Chart 18. Operating surplus (deficit)**




Source **Forecast model**

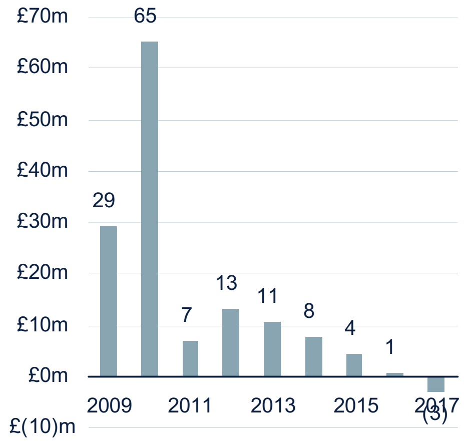
# 4. Financial forecasts

**Chart 19. Cash surplus (deficit)**



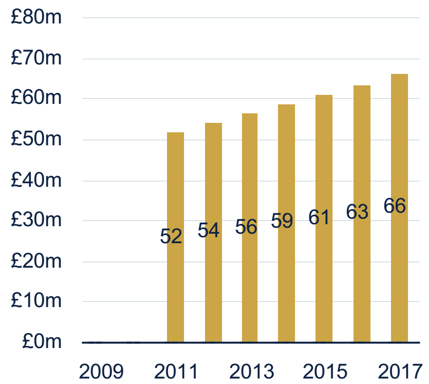

Source **Forecast model**

**Chart 20. Transfer from Contingency reserve**



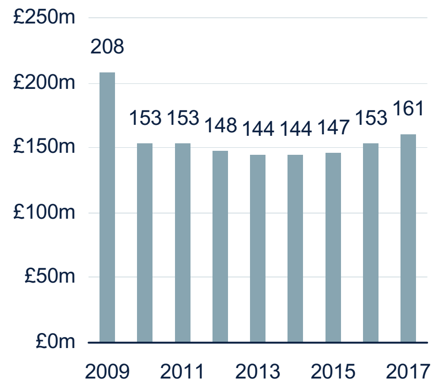

Source **Forecast model**

**Chart 21. Additional revenues required**




Source **Forecast model**

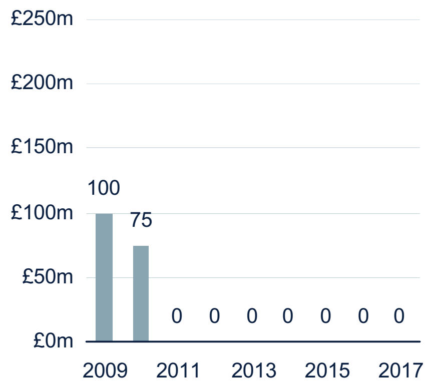
**Chart 22. Contingency reserve balance**




Source **Forecast model**

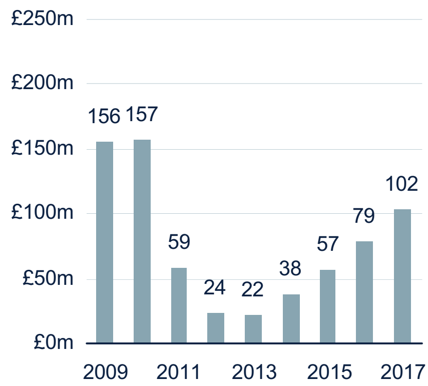
# 4. Financial forecasts

**Chart 23. Illustrative debt issues**



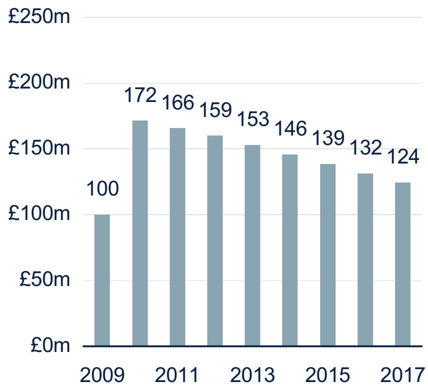

Source **Forecast model**

**Chart 24. Outstanding capital reserve balance at end of year**



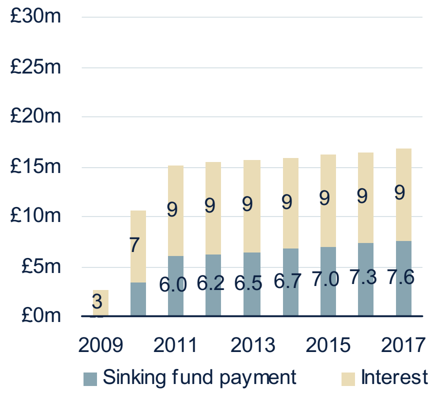

Source **Forecast model**

**Chart 25. Total net debt (net of sinking fund balance)**




Source **Forecast model**

**Chart 26. Debt service (interest plus sinking fund contribution)***




Source **Forecast model**

* Debt service assumptions are detailed further in section 5.

We have run a number of alternative scenarios, whose results are presented in the appendix, including

- Funding of all Priority 1 and 2 projects (appendix A)
- Expenditure growth restraint (appendix B)
- Downside economic scenario (appendix C)

# 5. Debt financing options

This section reviews the principal debt options available to the States to finance the capital expenditure programme. We consider that the States' two main debt funding options are i) a committed bank credit facility and ii) capital market issuance(s). There are other funding options, which the States could investigate, such as project finance, however we believe that they would not offer competitive funding costs under current market conditions given the States' new AAA credit rating from S&P.

## 5.1 Bank debt

### *5.1.1 Overview*

A bank facility could be arranged to fund the capital expenditure programme. The facility would be available for general purposes (i.e. it would not need to be restricted to certain projects) and could be drawn down as capital expenditures are incurred. While commitment fees would be payable on the undrawn portion of the facility, this option would avoid any potential negative carry cost associated with prefunding through a bond issue where proceeds are raised ahead of time[1].

The facility is likely to have a floating rate of interest, which can be hedged through an interest rate swap.

### *5.1.2 Current market conditions*

Banks remain under significant pressure to reduce lending and conserve capital. As a result lenders are focussing on limiting/reducing total exposure including uncommitted facilities, hedging arrangements and other ancillaries. Even strong credits rated A and above are affected.

In the current market environment, when banks are willing to lend, they typically do not underwrite more than their target hold amount and "club deals" are now the norm. While some large banks are willing to hold £100-150m for good credits, many banks will only take exposures of £25-50m, which creates the need to arrange club financings with a large number of banks.

Banking terms have steadily worsened during the credit crisis with significantly higher pricing and shortened maturities:

- Margins for strong credits are now often above 100bps over swap, even for AAA credits
- Lenders are focused on amortisation profile with maturities of 3 years as the new standard for corporate bank debt. Whilst occasionally possible, 5 years is more difficult to achieve
- Credit committees are now much more demanding in terms of information and due diligence requirements

While Guernsey could certainly expect to achieve lending terms superior to those available to strongly rated corporate credits, the fact remains that credit market conditions are suboptimal for bank finance at the moment.

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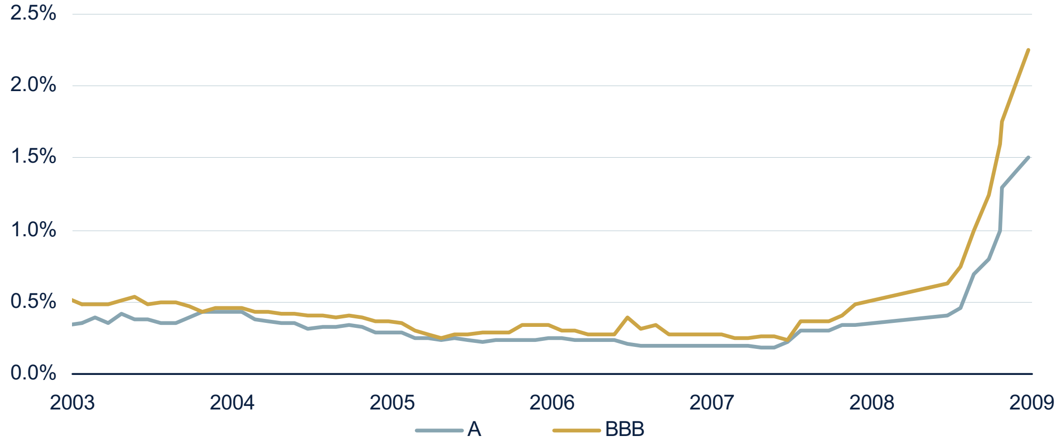
[1] "Negative carry" refers to the negative differential (if any) between the cost of borrowing and the yield obtainable on a deposit of surplus cash.

# 5. Debt financing options

**Chart 27. UK corporate loan spreads per rating level**




Source **LoanConnector, Rothschild analysis**

## 5.2 Bond issue

### *5.2.1 Overview*

Standard & Poor's have now confirmed a AAA rating for the States of Guernsey. Thanks to this rating, the States can consider the option of issuing a public or private bond on the capital markets. The main advantages of a bond issue over a bank facility are:

- Access to longer term maturities (up to 20-30 years)
- Access to the fixed rate investor base removing the need for an interest rate swap to fix the States' cost of funding
- Pricing over Gilt yields, which are currently at or near cyclical lows (4.5% for 20 year)

The main drawbacks of this option are as follows:

- Documentation and listing costs
- Minimum issuance amount for public issue (typically around £100m) although private placement can be explored
- Risk of negative carry if debt is issued ahead of the actual capex funding need and deposit rates on the excess cash are lower than the bond coupon

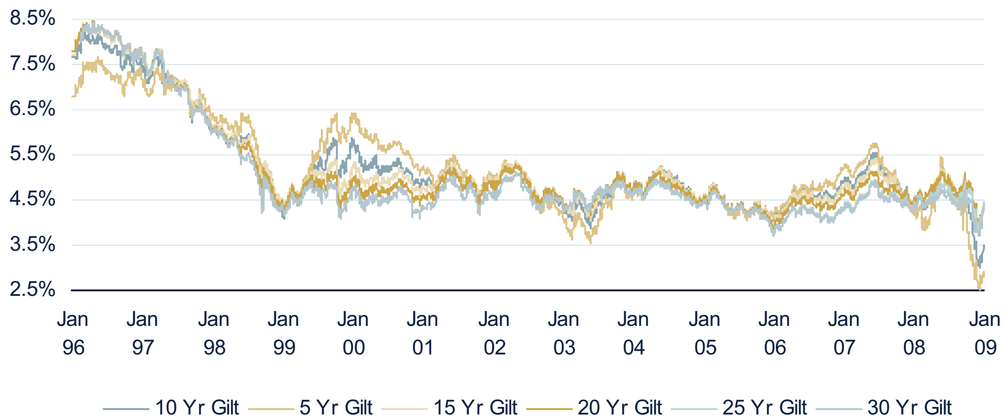
### *5.2.2 Update on current bond market conditions*

Following Lehman's liquidation in September 2008, activity in the European capital markets came to a virtual standstill. Issuance started to recover in October and November with a number of bonds issued by utilities, which are typically rated A or above. Bond issuance in the wider corporate market finally resumed in December and January 2009 with investment grade borrowers across the rating spectrum successfully (but expensively) tapping short and long maturities in both Euros and Sterling.

# 5. Debt financing options

As the corporate bond market was struggling, investors' flight to quality intensified and pushed Government bond yields down as illustrated in the graph below.

**Chart 28. UK gilt yields**




Source **Bloomberg**

In 2009, European governments' plans to recapitalise/nationalise their financial sectors are expected to trigger a large volume of Government issues which, combined with bank guaranteed debt, could severely test market appetite (more than €2.6tn of debt issues is expected in 2009). The table below shows the forecast European Government bond issuance in 2009.

**Table 6. Forecast European bond issuance in 2009**

| €bn | Recapitalisation plan | Total maximum gross issuance |
|---|---|---|
| Germany | €80bn | €238bn |
| France | €40bn | €175bn |
| Italy | €20bn | €220bn |
| Spain | €30bn | €80bn |
| Holland | €37bn | €70bn |
| Belgium | €1bn | €24bn |
| Austria | €15bn | €32bn |
| Finland | -- | €6bn |
| Ireland | -- | €15bn |
| Greece | €13bn | €53bn |
| Portugal | -- | €12bn |
| **Total** | **€236bn** | **€925bn** |

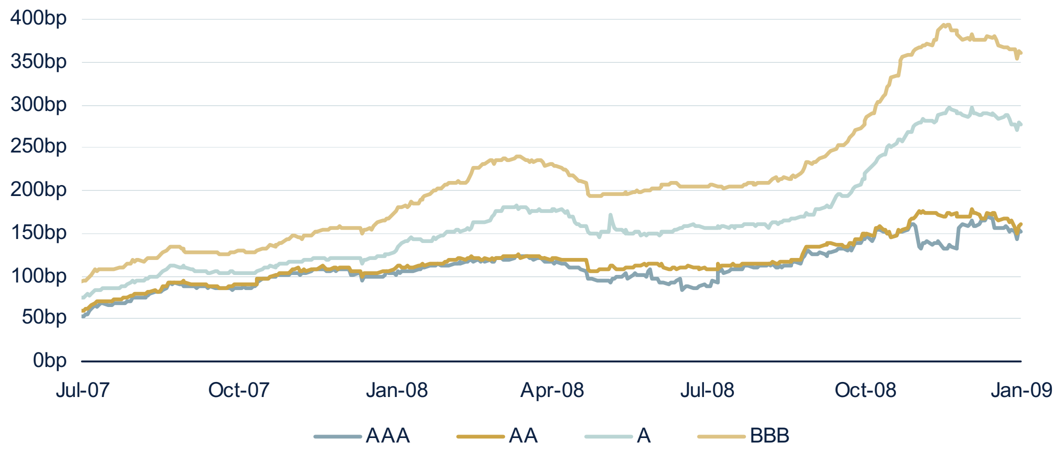
Source **The Financial Times**

# 5. Debt financing options

This record issuance is likely to push yields up (Government bond yields have already increased since the beginning of January 2009) and may well test the limits of market capacity.

Meanwhile, credit margins have increased significantly since the beginning of the credit crisis. The following graph shows average corporate credit spreads over Gilts by rating level.

**Chart 29. Sterling corporate spread over Gilts per rating level**

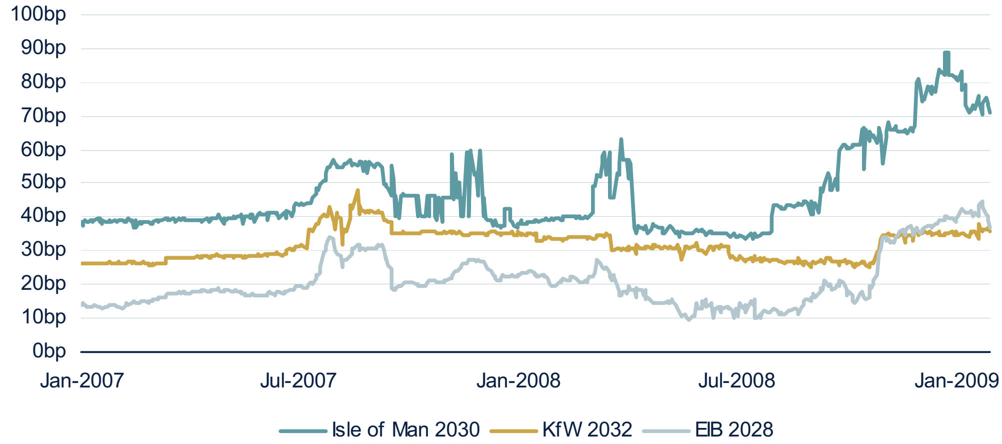



Source **Bloomberg**

One relevant price comparison for Guernsey is the outstanding bond issue of Isle of Man, who issued £75m of bonds in 2000 paying a 5.625% coupon with a 2030 maturity. The bonds are rated AAA. As illustrated below, the spread of the bond currently stands at c.73 bps over Gilts. Other relevant comparables include bonds issued by EIB (the largest non-UK issuer of Sterling bonds rated AAA) and KfW (guaranteed by Germany and rated AAA).

# 5. Debt financing options

**Chart 30. Spread over Gilt of selected bond comparables**




Source **Bloomberg**

Spreads on primary issuance (i.e. on new bond issues) typically exhibit a premium over secondary market (i.e. trading) spreads. In the current market, the new issue premium can be very volatile and is very borrower specific. In December and January this premium has been falling (an example: Total Oil paid a 65bp premium in November but only 43bp in January). The following table gives an indication of the new issue premia paid by recent issuers over their existing bond yields.

**Table 7. Recent new issue analysis**

| Company | Rating | Date of issue | New issue premium |
|---|---|---|---|
| Total Oil | AA | 20 Jan 2009 | 43bp |
| Telekom Austria | BBB+ | 19 Jan 2009 | 62bp |
| EdF | A+ | 16 Jan 2009 | 90bp |
| Carrefour | A | 05 Dec 2008 | 50bp |
| Total Oil | AA | 20 Nov 2008 | 65bp |

Source Bloomberg, Rothschild

### *5.2.3 Specific feedback from banks approached*

As part of our review of the States' funding options and in agreement with T&R, we approached a short-list of banks. Their feedback was utilised in our financial modelling process and in the development of our conclusions.

# 5. Debt financing options

## 5.3 Conclusion

### *5.3.1 Recommended debt funding option*

We believe that the capital markets currently offer the most optimal debt funding option for the States' long-term capital expenditure programme for the following reasons:

- Guernsey's AAA rating is likely to attract debt investors looking for high quality credits
- Bond markets offer long-term funding options, with maturities of up to 20-30 years, which will match the economic lives of the underlying assets and reduce the States' refinancing risk
- Long-term Sterling bond issues are priced off UK Gilt yields, which are at or close to cyclical lows resulting in a low overall cost of funds
- Long-term Sterling bond issues typically have fixed coupons, which provide a fixed interest cost and reduce hedging costs
- The capacity of the bank market for syndicated loans is currently limited and expensive

At the same time, we note that the range of indications banks have provided with respect to bond pricing, maturities and fees is very wide. This is a reflection of the high degree of volatility and uncertainty in global financial markets. Greater certainty as to investor appetite, bond pricing and maturity will follow name-disclosed discussions with key institutional investors.

### *5.3.2 Currency of bond issuance*

In our view, issuing debt in a currency other than Sterling (Euro or USD) is unlikely to offer material benefits in terms of market capacity or pricing given the size of the States' funding requirements. In addition, any foreign currency funding would introduce additional hedging costs for the States. Therefore we recommend that the States meet their funding requirements through long-term sterling bond issues.

### *5.3.3 Fixed vs. index-linked coupon*

Long-term Sterling bonds typically have a fixed coupon but given their AAA rating the States also have the option to consider an index-linked bond.

The main advantages of an index-linked bond are i) lower coupon (in line with real interest rates) and ii) natural hedge if revenues are linked to inflation.

The main drawback is that the principal of the bond increases with inflation (typically UK RPI), thereby potentially introducing higher refinancing risk at maturity.

We do not believe that an index-linked bond issue would bring significant benefits to the States because:

- The impact of the lower coupon will be offset by the funding requirements associated with the recommended sinking fund mechanism (see next section), which is designed to mitigate refinancing risk
- This type of bond would introduce exposure to the spread between UK and Guernsey RPI, which may increase the States' risk or hedging costs

# 5. Debt financing options

### *5.3.4 Debt assumptions in the financial model*

In our financial model, we have made assumptions with respect to the debt funding of the States that are consistent with the feedback received from the banks polled. These include:

- Amount: £175m
- Maturity: 20 years
- Repayment: bullet
- Coupon: 20 year UK Gilt yield plus a spread

Given currently volatile and uncertain conditions in global financial markets, bond pricing available to Guernsey could change substantially between now and any decision by the States to issue a bond. We have estimated that each 1% increase in the coupon of the bond issue, due to a rise in Gilt yields and/or higher credit margin, would increase the debt funding requirements by c.£10m.

# 6. Other key considerations

## 6.1 Timing of debt issue

The States of Guernsey currently have ready access to £65m in cash to finance their capex programme:

- £42m standing in the capital reserve
- £23m transfer from budget in 2009

This would be sufficient to fund the Priority 1 project expenditures planned in 2009 but not in 2010. The States therefore have the option of waiting until 2010 to raise the required debt financing.

However we would recommend that the States consider pre-funding a portion of the capex programme for the following reasons:

- Certainty of funding

As a matter of prudence, to minimise execution risk, the States should consider funding the capex ahead of the due date of the related capital expenditures, provided that the financing terms achievable in the capital markets are acceptable. This would allow the States to fix the cost of funds over the life of the capital expenditure programme (Priority 1) thereby removing a potential element of volatility from the budgeting process.

- Attractive Gilt yields in current markets

While credit spreads have widened considerably during the current credit crisis, yields of long-term Gilts are currently are at near cyclical lows. Consequently the all-in cost of a debt issue (benchmark yield + credit spread) in the current markets could be attractive.

- Flexibility to accelerate the capex programme

Raising debt finance in the first semester of 2009 would allow the States to launch selected projects initially planned for 2010 ahead of schedule, i.e. during the second half of 2009.

There are however drawbacks to pre-funding portions of the capital expenditure programme:

- Risk of negative carry

The States could incur additional costs if the rate at which surplus cash raised in the pre-funding is invested is lower than the bond coupon.

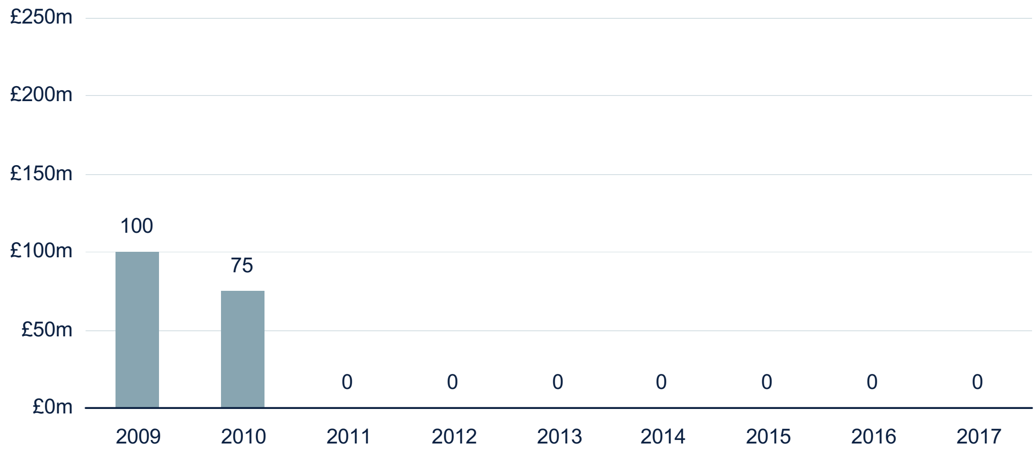
- Possibility of better financing terms in 2010

It is not possible to predict the evolution of credit markets as the economic crisis proceeds. It is possible that credit spreads will contract as the economy emerges from recession. On the other hand, expected strong levels of Government bond issuance could cause Gilt yields to rise significantly from their current levels. If this occurs the States could achieve a lower cost of funds by launching a single large bond issue in early 2009.

For the purpose of the financial model, we have assumed the following debt profile.

# 6. Other key considerations

**Table 8. Debt issuance profile (Priority 1 projects only)**




Source **Forecast Model**

## 6.2 Refinancing risk

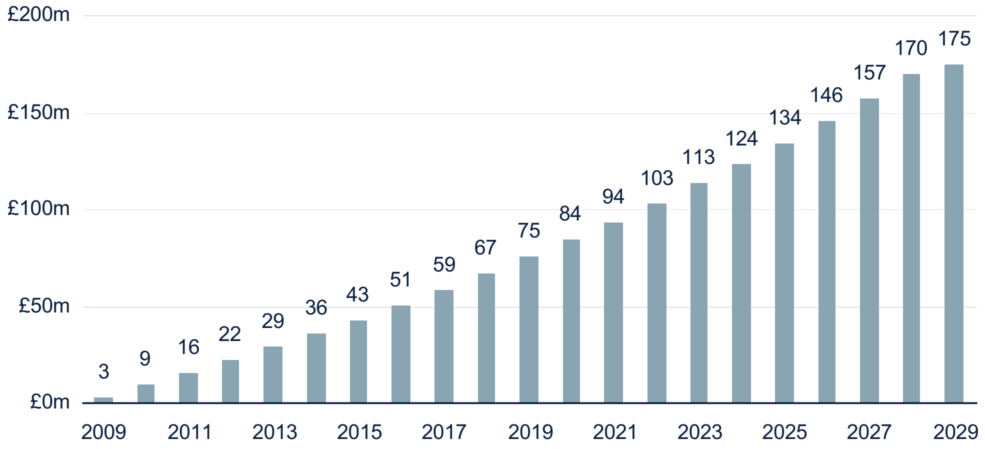
Given its strong credit profile and AAA rating, the States could raise a "bullet" financing with no principal repayment due until the maturity of the bond/facility. In such case, the States could elect simply to refinance the bond at maturity through a new issuance. While this would give the States enhanced flexibility, it introduces some refinancing risk because capital markets may not be as attractive or receptive in the future when the time comes to refinance the debt.

To mitigate this risk, the States could implement a sinking fund mechanism. Under this mechanism, the States would set cash aside in a dedicated account such that the amount accumulated by the maturity date of the facility/bond would be sufficient to redeem the debt. This is the approach we have taken in the Forecast Model. Under the Forecast Model, we have assumed that the amount transferred each year to the sinking fund increases with inflation so that it represents a constant amount in real terms. The longer the maturity of the bond/facility, the lower the annual payment to the sinking fund would have to be.

The following graph shows the cash accumulation in the sinking fund over the maturity of the bond in the base case scenario.

# 6. Other key considerations

**Table 9. Sinking fund profile**




Source **Forecast model**

## 6.3 Hedging issues

### *6.3.1 Overview*

Prudent risk management suggests that the States should hedge any interest rate, inflation or other market risks created by any new debt raised:

- Interest rate risk

If debt is issued with a floating rate of interest (which is likely if the States elect to raise a bank credit facility), the States will be exposed to changes in the benchmark floating rate (typically Libor). This risk can be mitigated through an interest rate swap. One should note that long-term Sterling bonds typically have fixed coupons and therefore do not introduce any interest rate risk.

- Inflation risk

A majority of the States' revenues is expected to grow with inflation. This suggests that an index-linked bond could be an option to be considered. However we note that issuance of index-linked debt would introduce a mismatch between UK RPI (the inflation rate commonly used in such bonds) and Guernsey's RPI. An inflation swap could be used to mitigate this risk but this would be an illiquid risk to hedge. Consequently we are not convinced that an index-linked issue would provide the States with any compelling advantages. In the Forecast Model, we assume that the annual transfers from the budget to the capital reserve (£23m in 2009) grow with inflation.

- Foreign exchange rate risk

In the unlikely event that the States raise debt in a currency other than Sterling, they will be exposed to foreign exchange rate movements, which can be hedged through a swap. However under current market conditions, we do not see any material benefit in terms of pricing or market capacity that non-sterling markets could offer, after taking into account hedging and other transaction costs.

# 6. Other key considerations

### *6.3.2 Pre-hedging*

Up to two months may be necessary to arrange a bank facility or bond issue (competitive tender process, documentation phase etc.). During this time, swap rates / Gilt yields can fluctuate and change the economics of the debt issuance. The States should therefore consider pre-hedging the interest cost of any debt funding to lock in current rates: either a forward starting interest rate swap (for a bank facility) or Gilt lock (for a bond issue).

The objective of the Gilt lock is to mitigate the risk of Gilt yields increasing between the date when the States decide to launch a bond issue and the actual pricing date. The hedge consists of shorting the relevant benchmark UK Gilt in an amount equal to the target bond issue. The short position will mature on the target date of the bond issue. If the yield of the shorted Gilt increases, the value of the short position will be positive and offset the increased coupon payable on the bond. If the yield of the shorted Gilt falls, the value of the short position will be negative and offset the lower coupon of the bond. The States' AAA credit rating should limit the cost of such a hedge.

## 6.4 Impact of future capex programmes

In addition to the projects listed as Priority 2, the States are likely to launch other capital expenditure projects over the next ten years, which will need to be considered as part of any future funding strategy.

## 6.5 Rating considerations

The States are rated AAA by Standard & Poor's, the highest obtainable rating for a sovereign credit.  Given the size of the targeted bond issue and the States' strong credit profile, we believe that the S&P rating is sufficient to support a bond issue of the size required to meet the States' funding needs.

# 7. Recommendations

## 7.1 Recommended debt funding strategy

- We believe that in the current markets a long-term fixed rate Sterling bond issue is the most optimal debt funding option for the States' capital expenditure programme. Such a bond issue will leverage Guernsey's AAA rating and appeal to debt investors looking for high quality credits.

- Based on the financial model developed with T&R, we estimate the debt funding requirement of the States to fund the Priority 1 projects to be c.£175m.

- We recommend that the States select a long-term maturity (between 15 and 30 years depending on market appetite and pricing at time of issue) to match the economic lives of the underlying assets and reduce the States' refinancing risk.

- We recommend that a sinking fund mechanism be established under which cash is progressively accumulated to fully repay the debt when it comes due. We believe that this would be consistent with Guernsey's tradition of prudent fiscal and economic policies and reduce refinancing risk at maturity.

- While the majority of the capital expenditures of the Priority 1 projects will be incurred between 2010 and 2013, we recommend that the States launch its debut bond issue in 2009 possibly followed by one additional issue in 2010. We believe that the benefits of pre-funding a portion of the capital expenditure in 2009, namely certainty of funding and fixed cost of debt together with the benefit of current low Gilt yields could outweigh the risk of negative carry cost.

- If and when the States decide to launch a bond issue, we recommend that the underlying benchmark Gilt yield of the planned bond issue should be pre-hedged, i.e. fixed ahead of the actual pricing date. This pre-hedge will partially mitigate the risk of the cost of debt increasing during the time required to issue the bond.

## 7.2 Proposed timetable and next steps

Following the planned debate in the States of Deliberation, if Guernsey decides to launch a bond issue, we propose the following next steps:

- Competitive tender to appoint lead manager of the bond issue
- Competitive tender to appoint the hedge provider (if pre-hedging route is selected)
- Execution of pre-hedge (if selected)
- Preparation of legal documentation (offering circular, listing etc.)
- Confirmation of rating by S&P
- Investor roadshow

# 7. Recommendations

- Pricing of bond issue
- Closing and funding

The following timetable gives an indication of the likely timing of each workstream.

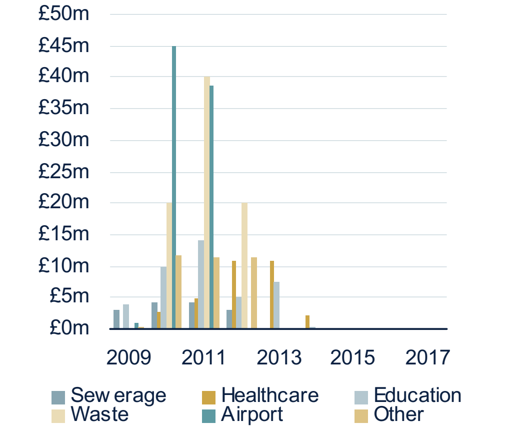
# 7. Recommendations

**Table 10. Proposed timetable**

| Month | Apr-09 | | | | May-09 | | | | Jun-09 | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Week** | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 |
| States decide to launch bond issue | | | | | | | | | | | | |
| Appoint legal counsel | | | | | | | | | | | | |
| Select shortlist of potential bond lead managers / hedge providers ("Banks") | | | | | | | | | | | | |
| Sign confidentiality agreements with Banks | | | | | | | | | | | | |
| Prepare request for proposals (RFP) | | | | | | | | | | | | |
| Send RFP to banks | | | | | | | | | | | | |
| Banks respond to RFP | | | | | | | | | | | | |
| Selection of lead manager / hedge provider | | | | | | | | | | | | |
| Execute pre-hedge | | | | | | | | | | | | |
| Prepare documentation (offering circular, listing) | | | | | | | | | | | | |
| S&P confirms ratings | | | | | | | | | | | | |
| Prepare investor roadshow material | | | | | | | | | | | | |
| Meet with investors | | | | | | | | | | | | |
| Launch of bond issue and pricing | | | | | | | | | | | | |
| Closing and funding | | | | | | | | | | | | |

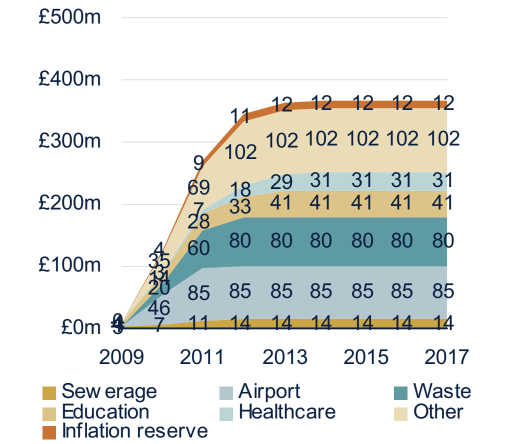
# A. Full capex scenario (Priority 1 and 2)

## Chart 31. Annual capex profile



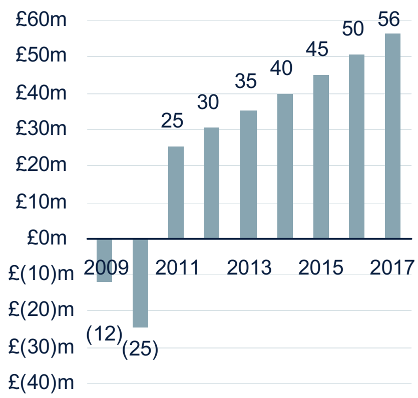

Source **Forecast model**

## Chart 32. Cumulative capex profile



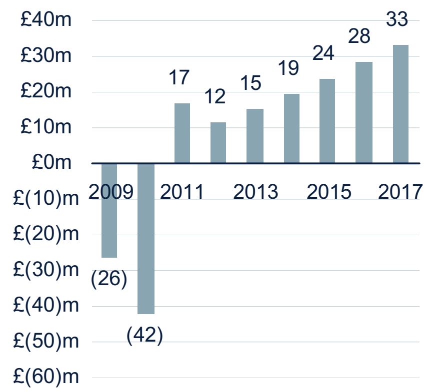

Source **Forecast model**

## Chart 33. Revenue surplus (deficit)




Source **Forecast model**

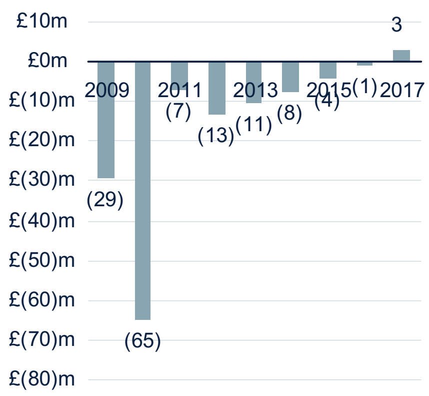
## Chart 34. Operating surplus (deficit)




Source **Forecast model**

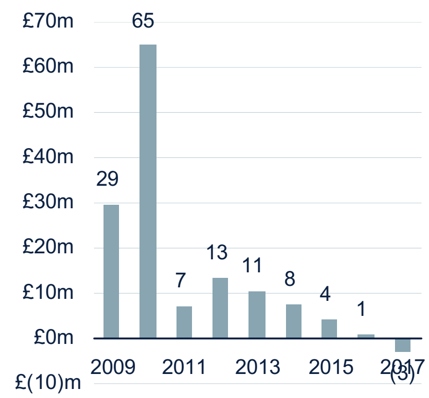
# A. Full capex scenario

**Chart 35. Cash surplus (deficit)**



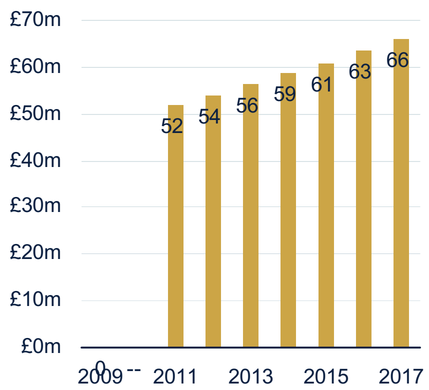

Source **Forecast model**

**Chart 36. Transfer from Contingency reserve**



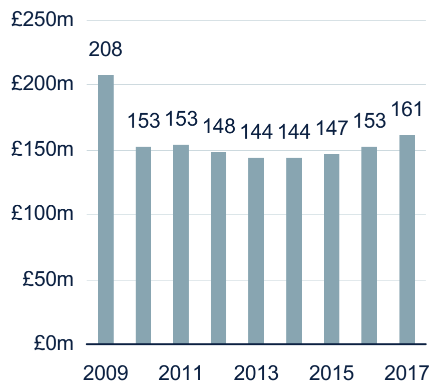

Source **Forecast model**

**Chart 37. Additional revenues modelled**




Source **Forecast model**

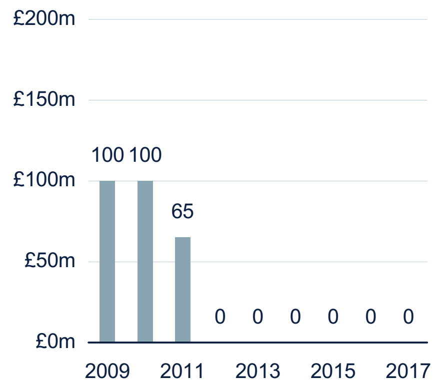
**Chart 38. Contingency reserve balance**




Source **Forecast model**

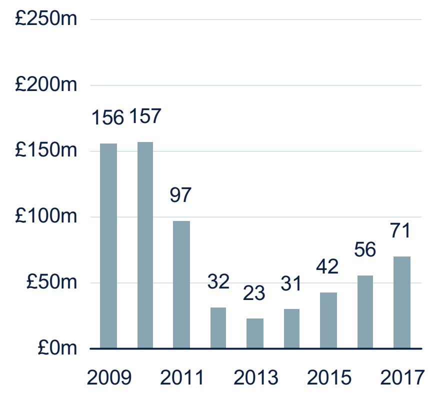
# A. Full capex scenario

**Chart 39. Illustrative debt issues**



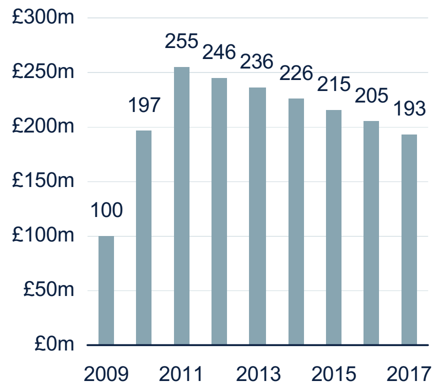

Source **Forecast model**

**Chart 40. Outstanding capital reserve balance at end of year**



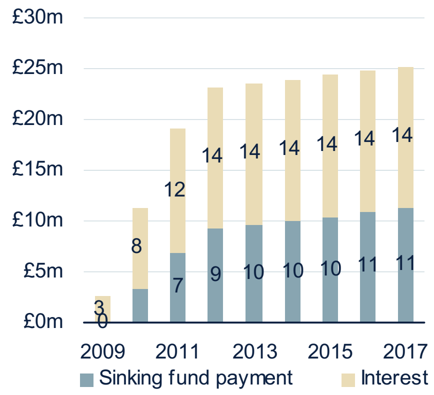

Source **Forecast model**

**Chart 41. Total net debt balance (net of sinking fund)**




Source **Forecast model**

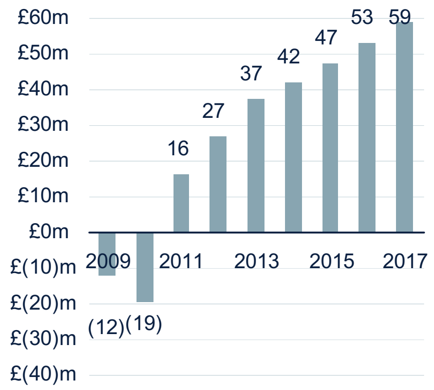
**Chart 42. Debt service**




Source **Forecast model**

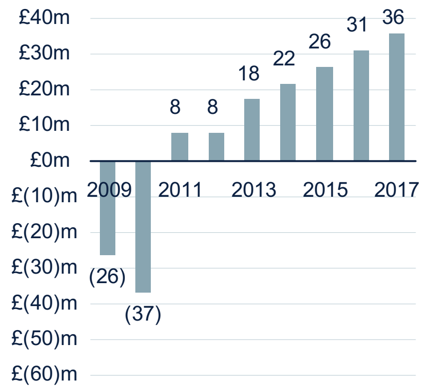
# B. Reduced expenditure scenario

**Chart 43. Revenue surplus (deficit)**



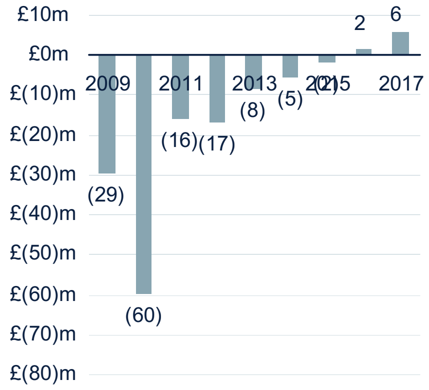

Source **Forecast model**

**Chart 44. Operating surplus (deficit)**



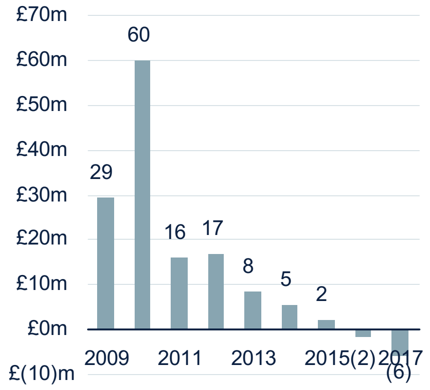

Source **Forecast model**

**Chart 45. Cash surplus (deficit)**




Source **Forecast model**

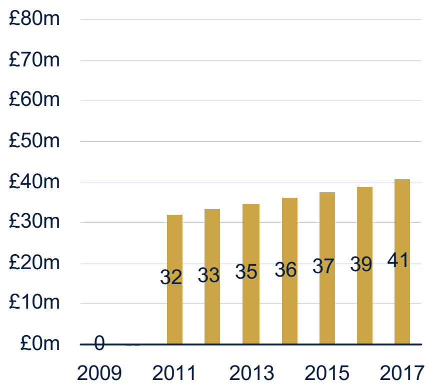
**Chart 46. Transfer from Contingency reserve**




Source **Forecast model**

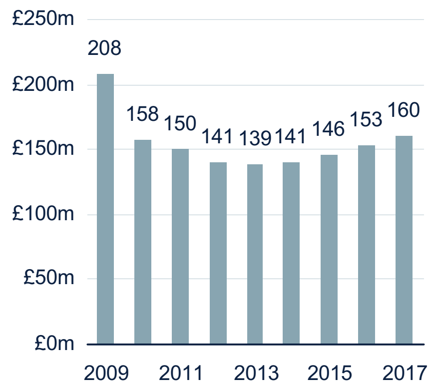
# B. Reduced expenditure scenario

**Chart 47. Additional revenues modelled**



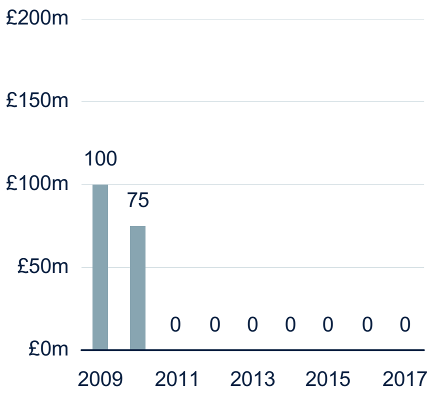

Source **Forecast model**

**Chart 48. Contingency reserve balance**



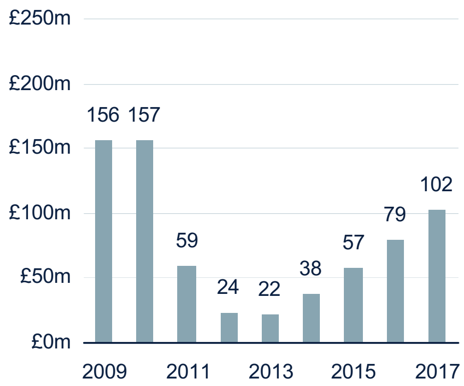

Source **Forecast model**

**Chart 49. Illustrative debt issues**




Source **Forecast model**

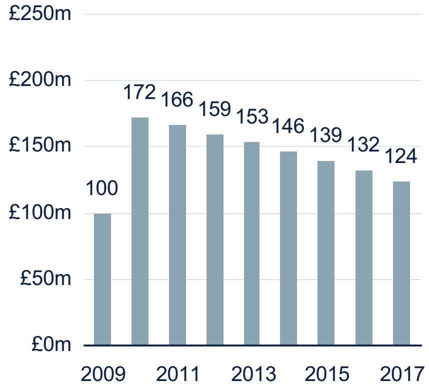
**Chart 50. Outstanding capital reserve balance at end of year**




Source **Forecast model**

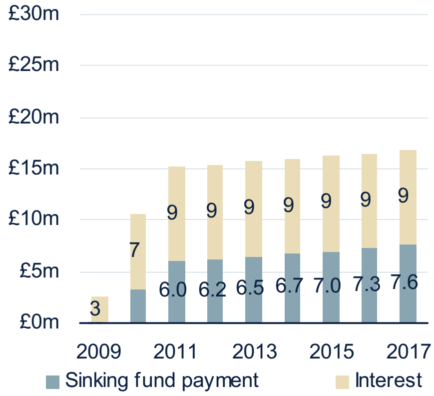
# B. Reduced expenditure scenario

**Chart 51. Total net debt balance (net of sinking fund)**




Source **Forecast model**

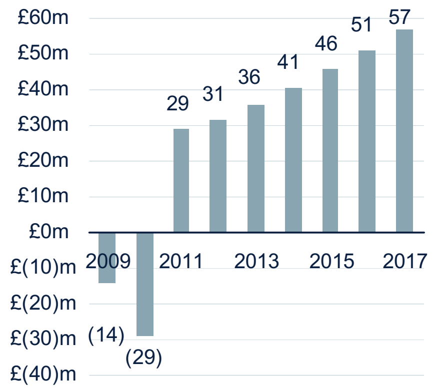
**Chart 52. Debt service**




Source **Forecast model**

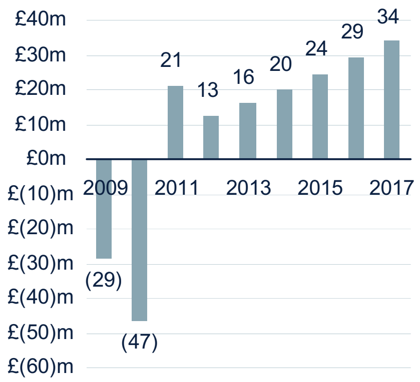
# C. Downside economic scenario

**Chart 53. Revenue surplus (deficit)**



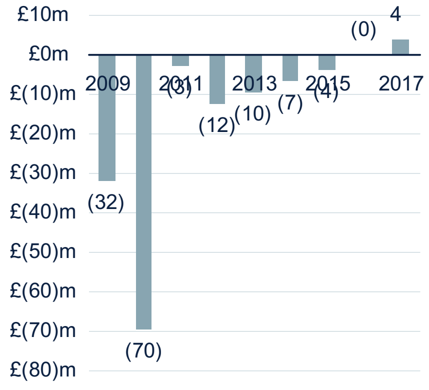

Source **Forecast model**

**Chart 54. Operating surplus (deficit)**



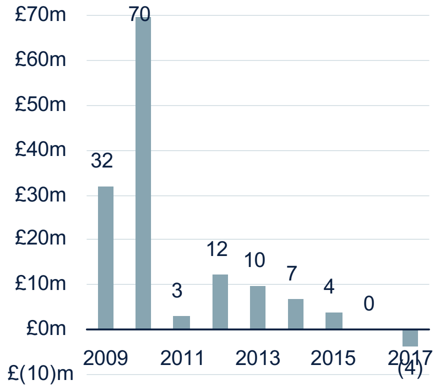

Source **Forecast model**

**Chart 55. Cash surplus (deficit)**




Source **Forecast model**

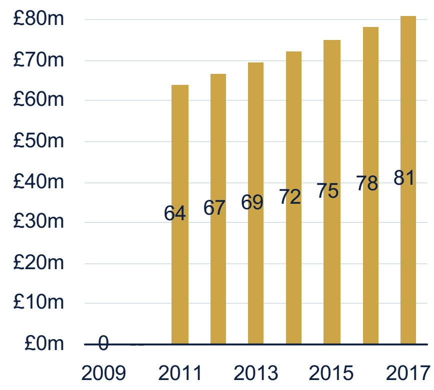
**Chart 56. Transfer from Contingency reserve**




Source **Forecast model**

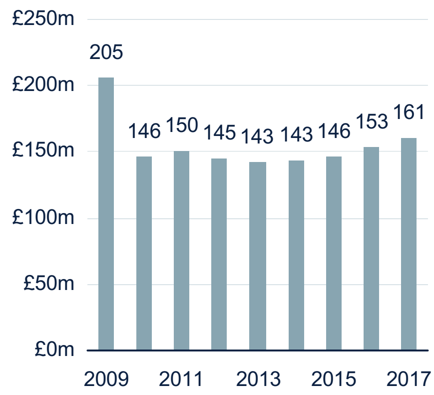
# C. Downside economic scenario

**Chart 57. Additional revenues modelled**



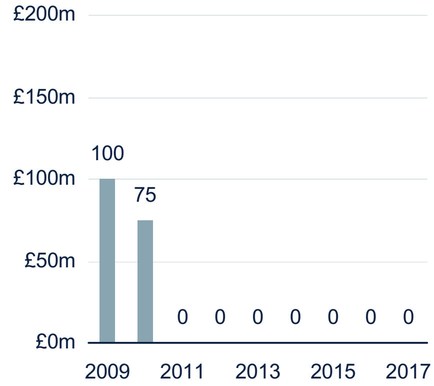

Source **Forecast model**

**Chart 58. Contingency reserve balance**



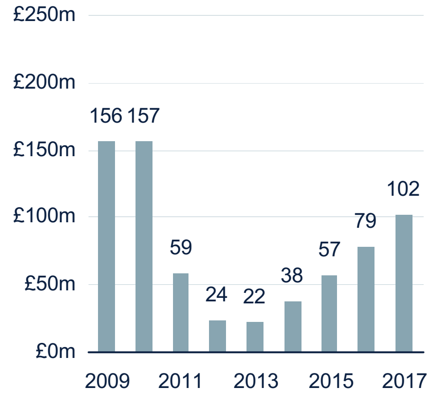

Source **Forecast model**

**Chart 59. Illustrative debt issues**




Source **Forecast model**

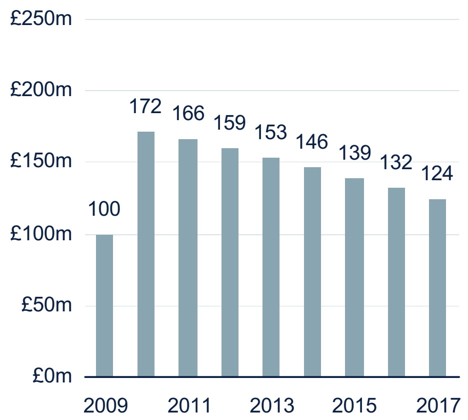
**Chart 60. Outstanding capital reserve balance at end of year**




Source **Forecast model**

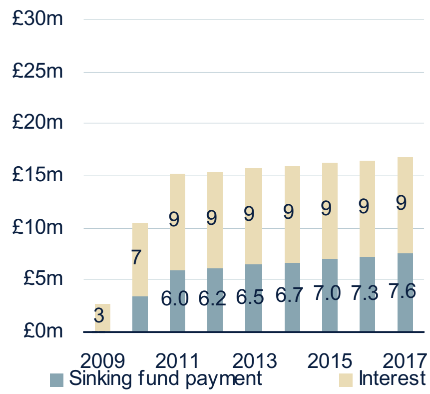
# C. Downside economic scenario

**Chart 61. Total net debt balance (net of sinking fund)**




Source **Forecast model**

**Chart 62. Debt service**




Source **Forecast model**

# Financial glossary

The following definitions apply throughout this document unless the context otherwise requires:

| | |
|---|---|
| “Benchmark rate” | A market interest rate (such as Libor or the appropriate gilt yield) providing a benchmark for pricing a bond or bank loan |
| “Bond” | A debt obligation issued to an investor by an issuer (usually a corporation or government) |
| “Bullet” | A one-time lump-sum repayment of a loan |
| “Commitment fee” | A fee lenders charge borrowers for undrawn committed lines of credit |
| “Coupon” | The interest rate stated to be payable on a bond when it is issued |
| “Credit margin” | The portion of the all-in interest rate payable on a bank loan above the relevant benchmark rate |
| “Covenant” | A contractual promise made by an issuer to investors or by a borrower to its lenders. Financial covenants can be restrictive and, if breached, can trigger early repayment, default etc. |
| “Gilt” | A bond issued by the British government |
| “Hedging” | A transaction designed to reduce or eliminate exposures to changes in market rates (such as interest rates or currency exchange rates) |
| “Index-linked bond” | A bond the principal amount of which accretes over time in accordance with a specific financial index, usually the Retail Price Index (RPI) |
| “Libor” | The London Interbank Offered Rate, a benchmark rate often used to price bank loans |
| “Negative carry” | The risk of a negative differential between the interest cost payable on prefunded debt and the (possibly lower) interest income that can be earned on the excess cash |
| “Rating” | An evaluation of an issuer’s financial strength provided by an independent credit rating agency such as Standard & Poor's, Moody's or Fitch. Ratings provide an indication of the likelihood of timely repayment of the principal and interest due on a bond |
| “Spread” | The differential between the yield on a bond or bank loan and a specified benchmark rate |

# Financial glossary

| | |
|---|---|
| "Swap" | A contract for the exchange of cash flows commonly used to convert one type of market rate exposure to another, e.g. convert a floating rate to a fixed interest rate. |
| "Syndicated loan" | A loan offered by a group of lenders (called a "syndicate") that collectively provide funds to the same borrower |

**Appendix E**

# Guernsey Assigned 'AAA/A-1+' Ratings; Outlook Stable; 124th Rated Sovereign

**Primary Credit Analyst:** Marko Mrsnik, London, (44)20-7176-7116; marko_mrsnik@standardandpoors.com

**Secondary Credit Analyst:** David T Beers, London, (44) 20-7176-7101; david_beers@standardandpoors.com

**Additional Contact:** Sovereign Ratings; SovereignLondon@standardandpoors.com

## Rationale

On Feb. 10, 2009, Standard & Poor's Ratings Services assigned its ‘AAA’ long-term and ‘A-1+’ short-term sovereign credit ratings to Guernsey. The outlook is stable. The Transfer & Convertibility assessment--our opinion of the probability of the sovereign restricting nonsovereign access to foreign exchange needed for debt service--is ‘AAA’. Guernsey is the 124th sovereign rated by Standard & Poor's.

The ratings on Guernsey reflect the government’s robust financial position, including negligible public debt, and a prudent fiscal policy track record which we expect will be maintained over the medium term.

Guernsey’s high per capita income also supports the ratings. At an estimated $39,100 in 2009, Guernsey’s per capita GDP is similar to that of peers such as Isle of Man ($40,200), Andorra ($41,400), and Singapore ($34,300).

Fiscal flexibility is a critical factor underpinning Guernsey’s creditworthiness. In our view, Guernsey's tax levels are low and, under adverse financial circumstances, there would be room for increases in rates (such as property tax rates) and for the introduction of new taxes without jeopardizing Guernsey's competitive advantage. Past fiscal soundness has allowed for the accumulation of substantial financial assets, which we estimate at over 100% of GDP in 2008. Over 2009-2011, Guernsey's public finances are likely to be challenged by subdued output growth and the introduction of the zero-ten corporate tax, although the fiscal impact of the latter should be cushioned by higher indirect taxes if needed.

Contingent liabilities are in line with levels in peer countries. We estimate the maximum risk to the government--mainly stemming from a large financial sector--at 60% of GDP for 2009.

Guernsey has been part of a monetary union with the United Kingdom since 1921. The Treasury issues notes and coins at par with the pound sterling, operating a de facto currency board. The pound sterling is also legal tender on the island. The long-standing monetary union insulates Guernsey’s economy from balance of payments risks and strengthens the economic links with the U.K. mainland.

Guernsey’s low-tax policies, well-regarded regulatory framework, skilled work force, and good infrastructure have supported a moderate pace of output growth over the past two decades. However, the economy can be volatile due to its reliance on the financial services sector. Despite efforts to diversify–-for example by promoting e-business and tourism--the financial sector accounts for the largest share of income (over 30% in 2007) and employment (24% of the workforce in 2007). We expect little change in the financial sector’s dominance in the economy over the medium term. Given these factors, we believe Guernsey requires a substantially stronger fiscal buffer to manage external shocks than larger and more diversified sovereigns with more flexible monetary and exchange rate regimes.

## Outlook

The stable outlook reflects our expectation that the government’s financial position will remain very strong, with a large and liquid public sector net asset position over the medium term despite the challenging global financial and economic environment. We expect Guernsey's growth to be subdued, however, and the ratings could come under pressure if multi-year budget deficits emerge that put the government’s net asset position under sustained downward pressure. Although the rating on Guernsey is not directly tied to that on the U.K., a prolonged downturn in the U.K.'s financial services sector and broader economy could negatively affect Guernsey's credit standing because of the economic and financial linkages between the two jurisdictions.

## Ratings List

Sovereign credit ratings assigned

AAA/Stable/A-1+

Transfer & Convertibility assessment

AAA

**Appendix F**

**ANALYSIS OF ON-ISLAND EXPENDITURE OF RECOMMENDED CAPITAL PROGRAMME**

| Proposal | Best Estimate £'000 | % of value on island | Value on island £'000 | Investment in Building on island £'000 | Investment in Engineering on island £'000 | Investment in Equipment on island £'000 | Finance £'000 | Investment in IT on island £'000 | Inflation Allowance £'000 |
|---|---|---|---|---|---|---|---|---|---|
| College of Further Education Phase 2b | £2,700 | 95% | £2,565 | £2,565 | - | - | - | - | - |
| Les Beaucamps School | £38,150 | 60% | £22,890 | £22,890 | - | - | - | - | - |
| Cobo Bay Bunker/Sea Wall Repair | £350 | 90% | £315 | - | £315 | - | - | - | - |
| Adult Acute Mental Health Facilities | £25,400 | 70% | £17,780 | £17,780 | - | - | - | - | - |
| Homes for Adults with a Learning Disability | £5,300 | 90% | £4,770 | £4,770 | - | - | - | - | - |
| eBorders IT system | £1,000 | 5% | £50 | - | - | - | - | £50 | - |
| Police Core IT System | £1,200 | 5% | £60 | - | - | - | - | £60 | - |
| Tetra Radio | £1,800 | 5% | £90 | - | - | - | - | £90 | - |
| Belle Greve Wastewater Disposal Facility | £15,500 | 75% | £11,625 | - | £11,625 | - | - | - | - |
| Solid Waste Solution | £80,000 | 25% | £20,000 | - | £20,000 | - | - | - | - |
| Airport Pavements | £84,500 | 35% | £29,575 | - | £29,575 | - | - | - | - |
| Airport Radar | £2,400 | 10% | £240 | - | - | £240 | - | - | - |
| St Peter Port Harbour Crane Strategy | £10,000 | 50% | £5,000 | - | £5,000 | - | - | - | - |
| St Peter Port Harbour Pontoons | £1,000 | 10% | £100 | - | - | £100 | - | - | - |
| Sarnia Work Boat | £1,000 | 5% | £50 | - | - | £50 | - | - | - |
| Social Security/Income Tax IT System | £5,500 | 5% | £275 | - | - | - | - | £275 | - |
| Cabernet Limited Recapitalisation | £6,000 | 100% | £6,000 | - | - | - | £6,000 | - | - |
| Corporate Asset Management IT System | £600 | 5% | £30 | - | - | - | - | £30 | - |
| IT Wide Area Network | £3,600 | 10% | £360 | - | - | - | - | £360 | - |
| Inflation Allowance | £15,000 | 40% | £6,000 | - | - | - | - | - | £6,000 |
| **TOTAL** | **£301,000** | | **£127,775** | **£48,005** | **£66,515** | **£390** | **£6,000** | **£865** | **£6,000** |

**(NB Following the submission of the Treasury and Resources' ('T&R'), Capital Prioritisation Report the Policy Council agreed to the recommendations of its Fiscal and Economic Policy Group ('FEPG') that, before debating the specifics of the proposals contained in T&R's report, it would be prudent for the States first to debate and discuss a formal fiscal policy framework to ensure continued conservative fiscal policy of the States.**

**In considering the recommendations of the FEPG, the Policy Council noted that, whilst there is nothing inherently unorthodox with the T&R proposal to use borrowing to finance public sector expenditure, this method of financing is a clear departure from recent historical experience and will require a fundamental change in the mindset of policy makers, in particular a need for increased fiscal discipline. The Policy Council believes that a formal fiscal framework will provide credibility to fiscal policy and provide reassurance to taxpayers about the sustainability of future States spending plans. The Policy Council has accordingly requested the FEPG to draft a fiscal framework to be proposed by the Council for discussion and debate at the April States Meeting.**

**The Policy Council welcomes T&R's proposal to proceed with publication of its Capital Prioritisation report with debate delayed until the May States meeting to first allow for a debate on a fiscal policy framework. This will provide the States with a sufficient opportunity to fully consider the future ramifications of the report's recommendations, especially in relation to the principles of borrowing, will give first consideration to the prudent step of setting guidance for the conduct of future policy and will facilitate separate debates on the principles and the practicalities of fiscal policy.)**

The States are asked to decide:-

Whether, after discussion of the Report dated 24th February, 2009, of the Treasury and Resources Department, they are of the opinion:-

1. To approve the recommended programme for capital projects totalling £301million as set out in Programme C of Section 6 of that Report.

2. To note that each project that is included within the capital programme will be the subject of a separate Report before the project can commence unless the Treasury and Resources Department has delegated authority to approve a capital vote.

3. To authorise the Treasury and Resources Department to approve capital votes for expenditure on progressing to tender stage those projects that have been included in the capital programme, funded by transfers from the Capital Reserve.

4. To authorise the Treasury and Resources Department to transfer from the Capital Reserve such sums that are necessary to fund approved capital votes.

5. To authorise the Treasury and Resources Department to enter into a borrowing arrangement at the best available terms for a sum not to exceed £175million, repayable over a maximum period of 20 years.

6. To establish a Sinking Fund to accumulate annual transfers from the Capital Reserve such that, by the end of 20 years, the principal borrowed can be repaid in full.

7. That the Ports Holding Account shall be collapsed and to direct the Treasury and Resources Department, following consultation with the Public Services Department, to recommend in the annual Budget Report appropriate short and long term accounting arrangements.

# IN THE STATES OF THE ISLAND OF GUERNSEY ON THE 27th DAY OF MAY, 2009

**The States resolved as follows concerning Billet d'État No IX dated 6th March 2009**

## TREASURY AND RESOURCES DEPARTMENT

CAPITAL PRIORITISATION

TO POSTPONE CONSIDERATION of this Billet d'État until the June meeting of the States.

S M D ROSS
HER MAJESTY'S DEPUTY GREFFIER

# IN THE STATES OF THE ISLAND OF GUERNSEY ON THE 26th DAY OF JUNE, 2009

**(Meeting adjourned from 27th May, 2009)**

**The States resolved as follows concerning Billet d'État No IX dated 6th March 2009**

## TREASURY AND RESOURCES DEPARTMENT

CAPITAL PRIORITISATION

After discussion of the Report dated 24th February, 2009, of the Treasury and Resources Department:-

1. To approve the recommended programme for capital projects totalling £301million as set out in Programme C of Section 6 of that Report, subject to the proviso that the timetable for undertaking the projects shall be determined by availability of funding.

2. To note that each project that is included within the capital programme will be the subject of a separate Report before the project can commence unless the Treasury and Resources Department has delegated authority to approve a capital vote; and to agree that the States will not be asked to approve the replacement of the Sarnia Work-Boat, either directly or through the Treasury and Resources Department acting under its delegated powers, unless an independent vessel survey has indicated that the vessel has reached the end of its safe working life or is likely to do so within four years.

3. To authorise the Treasury and Resources Department to approve capital votes for expenditure on progressing to tender stage those projects that have been included in the capital programme, funded by transfers from the Capital Reserve.

4. To authorise the Treasury and Resources Department to transfer from the Capital Reserve such sums that are necessary to fund approved capital votes.

5. That the Ports Holding Account shall not be collapsed in advance of the consideration by the States of a report from the Public Services Department in December 2009 on the options for moving the trading entities of Guernsey Harbours and Guernsey Airport into a different business environment, BUT THAT, in any event, the operating surplus before depreciation shall be transferred to the Capital Reserve from the Ports Holding Account from 2010 until such time as the Ports Holding Account may be discontinued.

6. That the Treasury and Resources Department shall loan to the capital reserve, from the general revenue cash pool and/or the contingency reserve, up to £83 million, accruing interest at the States Treasury interest rate (subject to proposition 9), and to be allocated strictly against the solid waste solution.

7. That the internal borrowing referred to in proposition 6 shall be repayable over a 20 year period from income generated by the solid waste solution.

8. That all other capital expenditure as may be agreed by the States as part of this approved programme of capital projects shall be financed from the funds available to the capital reserve, including;

   (a) appropriations from general revenue in the years 2009, 2010, 2011, 2012, 2013 and 2014;

   (b) an additional surplus from the ports holding account from 2011 of £1.775 million per annum at 2009 values (adjusted and maintained in real terms)

   (c) the additional operating surplus for 2008 of £22 million, which shall be transferred immediately.

9. To direct the Treasury and Resources Department to investigate the feasibility of arranging an interest rate swap to substitute a fixed interest rate for the variable States Treasury interest rate in respect of the internal borrowing referred to in proposition 6, and authorise that Department to enter into such an arrangement if thought appropriate.

10. To re-affirm the principle that States borrowing (whether internal or external) should be approved only for capital projects with a secure, associated income stream.

S M D ROSS
HER MAJESTY'S DEPUTY GREFFIER