

The financial performance of Scottish Futures Trust (SFT) 'hub' schemes: the case for better monitoring and rethinking their rationale

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Abstract

This paper is based on the analysis of the financial projections for three of the Scottish Futures Trust hub schemes. The paper develops a range of financial indicators, designed in particular to throw light on the following questions. Namely, what is the opportunity cost to the public sector of the hub approach: and what are the potential profits to private sector investors in the risk capital of hub projects. The paper concludes that the existing availability of information to the public and Scottish Parliament on hub schemes is inadequate, and that a standard set of indicators should be specified, and produced as a required by-product of the financial models for all hub projects. More broadly, the evidence suggests that there should now be a wider consideration as to whether the advantages of the hub approach justify the costs to the public sector, and the potentially large profits for private sector investors.

I Introduction

When it came to power in 2007, the SNP led Scottish Government introduced a new type of public private partnership, (PPP), known as the non-profit distributing, (NPD), model. This was designed to remedy some of the acknowledged defects in the old Private Finance Initiative (PFI) system, principally by reducing the scope for the equity owners to remove large profits as dividends. When the Scottish Futures Trust, (SFT), was set up in 2008, it took over and developed the NPD programme. In addition, in 2010 the SFT introduced the hub approach, a further type of PPP arrangement, to facilitate smaller public infrastructure projects by collaborative working, and, where appropriate, by bundling projects together.

Under the hub initiative, Scotland is divided into five hubco areas, where each hubco is a partnership between the SFT, public bodies like local authorities and health boards, and private sector partners. The hubcos are responsible for developing projects for the provision of new public infrastructure in their areas, like schools, health centres etc. Each project which goes ahead is a self-standing PPP funded by a mixture of senior debt and subordinate debt, and with

limited equity input. To date, there has been over £2 billion of capital investment either undertaken or in the pipeline via the hub programme.

Both the SFT and the Scottish Government publish periodic reports on the hub programme. These contain, for example, the key dates for each scheme, the capital value, the annual unitary charge to be paid by the public sector client, and the names of the lenders of senior and sub debt. What is not available from these reports, however, is crucial information on the financial characteristics of hub schemes. It is not possible, for example, to answer the following types of question – either for individual hub schemes, or for aggregates of hub schemes:

a) what is the opportunity cost to the public sector of the hub approach: that is, if the public sector had been borrowing at the same interest rates at which it could have borrowed from the National Loans Fund, how much capital investment could have been undertaken for the cost of the unitary charge payments which the public sector has contracted to make? (leaving aside that element of the unitary charge which will pay for ongoing services.)

b) what are the potential profits to private sector investors in hub sub debt if, for example, they were to decide to sell their holdings in the secondary market?

Yet, without answers to questions like these, it is impossible for the public, or the Scottish Parliament, to form a judgement as to whether the hub approach is likely to be delivering value for money for the public sector: or whether private sector participants may be in a position to extract excess profits, as was the case with the old PFI initiative which was superseded in Scotland by the current hub and NPD approaches. (See, for example, a recent paper by Whitfield, (2017), which records that the average annual rate of return to equity holders in PFI projects who sold their equity stakes in the secondary market was 28%, based on 110 transactions in 277 projects.)

This paper uses financial projections for three hub schemes, obtained under Freedom of Information, to derive indicators which are relevant to answering the above types of question. A number of clear conclusions emerge from this process and they fall under three main headings: monitoring; the need to re-assess the rationale of the hub programme; and, the need for greater support of the Scottish Parliament's Public Audit Committee in scrutinising SFT activities.

More specifically I conclude that:

On monitoring

- i) a standard set of indicators should be specified, (potentially based on those indicators analysed in this paper), which should be produced as a required by-product of the financial models for all hub projects.
- ii) the indicators for each scheme should be reported to SFT. In addition to assessing these indicators for their own purposes of monitoring the operation of the hub programme, SFT should publish, as soon as possible after the end of each year, annual average values for these indicators.
- iii) Two years after each scheme becomes operational, SFT should publish the values of the indicators for that scheme. This would be consistent with SFT's policy that the financial projections for individual schemes should cease to be confidential after this lapse of time.

Re-assessing the rationale of the hub programme

There should be active consideration, by the Scottish Government and public authorities, as to whether the advantages of the hub approach justify the costs to the public sector, and the potentially large profits for private sector investors. Even if it is too early yet, given the limited information currently available, to make a final decision, these questions should be kept under active review, in the light of whatever trends might emerge from the improved monitoring system.

Role of Scottish Parliament's Public Audit Committee

The Scottish Parliament's Public Audit Committee clearly struggles with its role of scrutinising SFT's activities. The Committee would find it much easier to discharge its role if it insisted that the SFT reported to it regularly on the basis of a specific, and detailed, set of indicators. It is recommended that the Audit Committee should adopt this approach: and that, as regards financial indicators for the hub programme, the Committee should take as its starting point the list of indicators considered in this paper.

II Indicators of the financial performance of hub projects

For hub projects, as for other public private partnership schemes, the key financial document is the set of financial projections produced at the time that the contract for the scheme is signed. These projections are produced by the Special Purpose Vehicle, (SPV), undertaking the project, and are shared with the public sector clients. The projections give a detailed breakdown, (typically six monthly or yearly), of all the sources of finance for the project: that is, by means of senior and subordinate debt input, equity input, capital contributions, (if any), and, during the operations phase of the project, unitary charge payments from the public sector client. The projections also give all financial outflows: that is, construction and development costs, the cost of providing services during the operations phase, SPV running costs, lifecycle costs, repayment of borrowed capital and interest, dividend payments, and tax. In other words, the projections give a complete, and very detailed, picture of income and expenditure of the project through its life, on the assumption that all goes according to plan with the project.

SFT's policy is that the financial projections should be regarded as being commercial in confidence for an initial period, to protect the interests of the participants and funders: but that the projections should become publicly available two years after the project becomes operational: that is, approximately two years after the completion of construction. SFT have also stated their intent to publish all hub financial models on SFT's website, once the relevant period of confidentiality is over: (refer SFT: contract website). This is a relatively liberal policy on confidentiality, and is to be welcomed. It contrasts favourably, for example, with the difficulty of obtaining financial projections for many schemes under the former PFI initiative.

However, SFT do not appear to be accessing or assimilating such information for their own purposes, or for the purpose of informing the Scottish Parliament's Public Audit Committee. For example, when he appeared before the committee on 7 December 2017, the then Deputy Chief Executive of SFT gave the following very limited information to the committee on the cost of finance for hub, and non-profit distributing, (NPD), schemes:

“The average senior debt rate is 4.09 per cent and the average for junior debt is 10.8 per cent which leads to an all in weighted cost of capital of 4.74 per cent.”

For the purposes of the present paper, an exercise was conducted by the author, using Freedom of Information, to obtain the financial projections for six hub schemes which had passed SFT's confidentiality time limit. (Freedom of Information was used to avoid delays in information on financial projections appearing on SFT's contract website.) Three of the projections obtained proved to be fairly readily analysable. What this section does is to develop a set of financial indicators, illustrated with reference to these three projections, and designed to elucidate important aspects of the financial performance of hub schemes. Along the way, the process of developing these indicators will illustrate how the information given by SFT to the committee is too limited, and also potentially misleading.

The financial models analysed here are for the following schemes. Namely, Alford Academy, an £18.4 million project for Aberdeenshire Council in the North Hub area, with an operational date of October 2015; James Gillespie's High School, a £33.9 million capital value project for the City of Edinburgh, in the South East Hub area, operational in August 2016; and the North Lanarkshire Health Centres Bundle project, for NHS Lanarkshire, a £38.9 million capital value project in the South West Hub area, operational in May 2015. Note that the three projections chosen for analysis here are for illustrative purposes only, rather than being a representative sample of hub financial models. In particular, since all of these projects fall, necessarily, fairly early in the hub programme, their senior debt interest rates are probably fairly high, since the base government gilt edged interest rates have fallen since the early days of the hub programme. The levels of senior debt interest rate observed for these projects should not, therefore be taken as indicative of all hub projects.

It should be noted also that in calculating the indicators in this paper there are some elements of judgement, for example about attribution of certain borderline expenditures to the construction or operations phase. This is unlikely to have any significant impact on the indicators as calculated: but may mean that the values derived here would not agree exactly with those that might be derived by another agent repeating the calculations.

The specific topics, and indicators, dealt with in this section are as follows:-

The need to state the cost of finance separately for NPD and hub schemes

In his evidence to the Public Audit Committee, quoted above, the Deputy Chief Executive of SFT was quoting a cost of debt averaged over two major SFT initiatives – namely, the NPD and hub programmes. NPD projects tend to be large, (an example is the £469 million value Aberdeen Bypass), and, as such, have been able to attract a portion of their senior debt funding from the European Investment Bank, (EIB). EIB funding is cheap: for example, one loan by the EIB to a UK water utility was at a real interest rate of 1.2%. As a result, the average cost of senior debt, averaged over NPD and hub projects, may well understate the actual cost of senior debt for hub projects. However, it is not possible to quantify any such bias, given the lack of published information. The important conclusion is that figures on the cost of finance should always be quoted separately for hub and NPD projects, rather than combined.

The effect of fees on senior debt interest rates

In a typical PPP project, the interest rate for senior debt will be based on the UK government gilt interest rate at the time the contract for the project is signed, to which is added an additional funder’s margin. The resulting interest rate, of gilt rate plus margin, is one commonly used measure for denoting the cost of senior debt: and, (as has emerged from correspondence with SFT), is the rate normally quoted by SFT. The following table shows this rate for the three projects considered here.

Table 1 Senior debt interest: gilt rate plus margin

	percent
Alford Academy	5.01
James Gillespie’s	5.40
North Lanarkshire Health Centres	5.36

However, quoting this rate does not give a full picture of what the borrower is actually paying. In addition, the borrower will typically be charged a fee, covering aspects like “arrangement” and “commitment”, and amounting, very commonly, to 2% to 3% of the original capital sum being

borrowed. The following table shows senior debt fees for the three projects considered here, expressed as a percentage of the amount of senior debt borrowed.

Table 2 Senior debt fees, as a percentage relative to senior debt borrowing

	percent
Alford Academy	2.33
James Gillespie's	3.08
North Lanarkshire Health Centres	2.69

In PPP projects this fee is normally capitalised: that is, it is added to the sum borrowed, and paid off through a stream of capital repayments and interest charges during the life of the project. So if a borrower borrows £100 to spend on construction costs, what they will actually pay is the loan charges on, say, £103. From the borrower's point of view, therefore, the interest rate they are actually paying is better represented by the internal rate of return, (IRR), of a transaction which corresponds to an initial drawdown of £100, followed by the stream of repayments relating to the capital sum comprising original loan plus fees. The effect of excluding fees is to materially understate the actual interest rate being paid for senior debt by the borrower. For example, if fees have been charged at 3% of the capital raised, and if this fee has been capitalised, then this is likely to increase the actual IRR being paid by about 0.3 percentage points.

SFT have pointed out in correspondence that other factors come in to the assessment of the senior debt funding package, as well as interest rates. Such factors, for example, include debt service and loan life cover ratios, and requirements for reserves. For this reason, SFT do not use a version of the senior debt IRR which includes fees. This appears a weak argument. While it is true that the other factors specified by SFT are important, a balanced picture of funding costs should surely also take account of the impact of capitalised fees on the interest rate actually being paid.

It is also a good question, (to which SFT have not as yet provided an answer), as to why fees for senior debt of up to 3% appear to be commonly charged on hub projects. On the face of it, the

size of this margin is surprising, given that the provision of senior debt for hub projects is not approached on a one-off basis for each project, but is done through what is effectively an annual framework competition for all projects in each hub area. Indeed, one might have thought that this process would have been expected to result in low arrangement fees.

Use of WACC versus IRR

The indicator SFT quoted to the committee as a measure of the combined cost of senior and subordinate debt was the weighted average cost of capital, (WACC). This is calculated as the average of the senior and sub debt rates, weighted together by the relative amounts of capital raised through the senior and sub debt routes. Since senior debt in hub projects typically accounts for 90% of the total capital raised, the WACC, based on the figures quoted by SFT, is $4.09 \times 0.09 + 10.8 \times 0.1 = 4.76$: give or take rounding, this is the figure quoted by SFT.

The WACC is indeed a standard shorthand measure of the combined cost of capital. Unfortunately, it has a major drawback, in that it will only equal the actual interest rate paid by the borrower, (that is, the IRR of the overall transaction), if the repayment profiles of senior and subordinate debt are the same. Typically, however, subordinate debt will be repaid on a later time profile compared to senior debt: this is normally a condition stipulated by the senior debt lenders, who will insist that their loans are substantially repaid before the sub debt loans are repaid. Since sub debt has less security than senior debt, and is therefore riskier, sub debt interest rates will be significantly higher than senior debt interest rates. These two factors, namely, the later repayment profile of sub debt, and its higher interest rate, mean that the WACC for senior and sub debt will understate the actual combined interest rate being paid on senior and sub debt.

The following table shows, for the three projects analysed here, the WACC of senior and sub debt, and the combined IRR of senior and sub debt. (In both cases, the cost of fees has been included for senior debt.)

Table 3 WACC and combined IRR for senior plus sub debt (percent)

	WACC	Combined IRR
Alford Academy	5.65	5.83
James Gillespie's	6.46	6.60
North Lanarkshire Health Centres	6.39	6.55

In each case the WACC, as expected, understates the true combined cost of senior plus sub debt. The bias in these three examples is not large, (a maximum of 0.18 percentage points in the case of Alford), but it is still material.

Since the combined IRR is the more accurate measure, the conclusion to be drawn is that the IRR, rather than the WACC, should be quoted as the primary measure of the combined cost of senior and sub debt. However, there are also advantages in quoting the WACC alongside the combined IRR. The reason for this is as follows. If, through time, it was observed that the difference between IRR and WACC was tending to increase, this could indicate that, for the later projects, sub debt lenders are having their loans repaid on increasingly delayed timescales. Now, for a given sub debt IRR, the later the loan is repaid, the greater the potential value to the lender if they were to sell their sub debt holdings in the secondary market: (this point is explained in more detail in the section below on net present values.) So an observed increasing differential between IRR and WACC could indicate that the potential for increasing, and perhaps excessive, profits on sub debt was being built into later schemes.

Project IRR as against combined IRR of senior and sub debt

As seen in the previous section, the appropriate measure of the combined cost of senior and sub debt is the combined senior and sub debt IRR, rather than the WACC. But the cost of funding is only one component of the overall transaction in which the public sector is engaged. From the overall perspective of the public sector client, what they are getting is a capital asset, plus a stream of services through the 30 year life of the project: and what they are paying is a stream of unitary charge payments through the project's operational life. If we net off from the stream of unitary charge payments what is being spent on services each year, what is left is the

component of the unitary charge which is not about the provision of services: here this is called the non-service element, (NSE). So another way of looking at the project is that it involves a transaction where the public sector is getting a capital asset costing a specified amount: and is paying for that asset via the stream of NSE payments during the life of the project. It is simple to calculate the IRR of this transaction: it is commonly called the project IRR. The project IRR is probably the best measure of the effective interest rate the public sector is actually paying.

Using the detail in the financial projections, project IRRs were calculated for all three of the projects being analysed in this paper. In more detail, in each case the capital cost was taken as the cost of construction of the project, plus development costs: (in those cases where the authority made a capital contribution to funding the capital cost of the scheme, the amount of any such contribution was subtracted off the capital cost.) The NSE was calculated in each period as the unitary charge, less the following terms: projected payments for SPV admin; facilities management; and lifecycle costs, (that is, projected replacement of items and equipment during the project life). That leaves the question of tax. One of the financial outflows is the projected stream of corporate tax payments during the project's life. Should these tax payments be included as part of the project's NSE, or not? This can be argued both ways, as will be seen below. So in fact, for the purpose of this study, two alternative NSE streams were calculated, one including tax, the other not.

The project IRRs resulting from this process are shown in the following table – which also repeats, for comparison, the combined IRR of senior and sub debt.

Table 4 Project IRRs, together with the combined IRR of senior and sub debt (percent)

	Combined IRR	Project IRR, Excluding tax	Project IRR, Including tax
Alford Academy	5.83	6.00	6.67
James Gillespie's	6.60	6.80	7.28
North Lanarkshire Health Centres	6.55	6.97	7.86

There are a number of interesting things to notice about this table. First of all, excluding tax, the project IRR is materially higher in each case than the combined IRR of senior and sub debt. At first sight, this looks surprising, because, once services and tax are taken out of consideration, virtually all the remaining expenditure by the project will be on financing costs. The answer is largely to do with phasing. The project will initially be building up balances, and then running them down. Hence the payment profile of debt service will be phased later than the profile of NSE payments, lowering the IRR of the former relative to the latter. It is, however, the project IRR which corresponds to what the public sector is actually paying: and hence is the more informative indicator.

The second interesting question is which project IRR should be used, excluding or including tax? From the point of view of the overall public sector, corporate tax just goes out of one pocket and back into another: so there is an argument that the “correct” project IRR is that excluding tax. There are, however, two counter-arguments:-

- a) from a Scottish perspective, tax paid to Westminster is lost to the Scottish budget, (apart from possible second order effects via the Barnett formula.)
- b) whether the SPVs will actually pay the corporate tax originally projected is unclear, particularly if ownership of the SPVs were to move offshore.

There is thus a strong argument for saying that the project IRR, including tax, is the more informative measure of the actual effective interest cost to the public sector of obtaining capital assets using the hub model. In any event, the sensible conclusion to draw is that, in practice, both versions of the project IRR should be quoted.

The need to consider net present values as well as interest rates

Interest rates, like the (unreliable) WACC, and the IRR, are standard, but still only partial, indicators of the true costs of a transaction. To obtain a fuller understanding of the implications of a particular transaction, it is necessary to consider the net present value, (NPV), of the stream of payments involved in the transaction, discounted at an appropriate discount rate. (For a fuller discussion, see, for example, Cuthbert and Cuthbert, (2012)).

It is useful to give two examples to illustrate this point. Suppose a subordinate debt investor in a PPP scheme is projected to receive an IRR of 10.8% on their investment over the life of the project: (this would be a standard rate of return on hub projects). Suppose, however, that this investor decides, soon after the completion of the construction phase of the project, to sell their sub debt holding in the secondary market: and suppose they find a buyer in the shape of a pension fund, where this buyer has the target of achieving a 6% rate of return on their purchase. Knowing the figure of 10.8% tells us very little about what price the secondary market investor will be willing to pay. Instead, what we need to know is the net present value of the projected stream of sub debt returns, discounted at a discount rate of 6%. This is the price the pension fund will be willing to pay. And the really important point to remember is that the more the stream of sub debt payments is weighted towards the later years of the project's life, then the greater the NPV of that stream will be, when discounted at a discount rate less than the original IRR.

This is the trap that the Treasury fell into in the original version of PFI. They had set a target rate of return of about 15% as being a reasonable return for the equity investors in PFI projects: but did not realise that the equity investors were heavily end-loading their projected returns – so that the NPVs at secondary market discount rates were multiples of the original investment. This led to the grotesque profits realised on some early PFI schemes.

To give a second example of the importance of NPVs: suppose that a public authority has the option of conventional capital procurement, funded by a loan at National Loans Fund borrowing rates: or procurement via some form of PPP, like a hub project. What the authority will want to know is how much more it is paying, by going down the PPP route, than if it had borrowed from the NLF. The net present value of the projected stream of non-service element payments under the PPP route, discounted at the NLF borrowing rate, will indicate how much the public authority could have borrowed from the NLF, for the price of the same stream of payments. In comparison with the capital sum it would actually have to have borrowed under conventional procurement, this will indicate the opportunity cost to the public authority of having gone down the PPP route. Of course, other things also have to be borne in mind, (like risk transfer under the PPP route.) But nevertheless, the NPV comparison is fundamental to understanding what the cost of PPP procurement to the public sector actually is.

The following tables show the above two indicators, for the three hub models analysed in this note.

The first table shows the NPV of the stream of sub debt payments, discounted at a discount rate of 6%. In each case, the NPV has been expressed as a percentage of the capital originally raised by sub debt, (excluding fees and interest rolled up during the construction period.)

Table 5 The NPV of sub debt payments, discounted at 6%, as a percentage of the capital originally raised through sub debt

	NPV as % capital raised
Alford Academy	172.2
James Gillespie's	180.8
North Lanarkshire Health Centres	180.1

What the figures indicate is that, if the sub debt investors were to sell their sub debt holdings soon after the project became operational, they might anticipate receiving back their original investment, plus a profit margin of around 80% of their original investment. This is clearly a very material level of potential profit. It is lower than the kind of profit realised by equity holders in many early PFI schemes – but is still very significant.

In fact, the level of potential profit in the above table is a good deal less than that envisaged by at least one potential investor in hub sub debt. A document produced by Aberdeen City Council, (2015), about the opportunities for investing in the sub debt of other councils' hub schemes, envisaged that an investment of £1 million might yield a return of £2.7 million if the stream of potential rewards was capitalised: (as would be achieved, for example, by a secondary market sale.)

The next table shows the NPV of the non-service element of the three example schemes, discounted at a discount rate of 4%, (which is close to the NLF borrowing rate at the time in question for loans of this maturity.) The figures have been expressed as a percentage of the NPV

of construction and development costs: and have been calculated for both versions of the NSE, excluding and including tax.

Table 6 NPV of NSE discounted at 4%, expressed as a percentage of construction and development costs (percent)

	Excluding tax	Including tax
Alford Academy	116.1	122.9
James Gillespie's	131.1	138.6
North Lanarkshire Health Centres	131.5	144.3

As can be seen, the opportunity cost to the public sector of hub schemes is material. In line with the discussion in the previous section, the including tax figure is probably a better measure of opportunity cost from the point of view of a Scottish public body. Given this, it can be seen that, in two of the above examples, the public body could have borrowed 40% more from the NLF for the cost of going down the hub route. The question for consideration, of course, is whether the price of using the hub approach is a price worth paying: factors which would come into this assessment would exclude the extent of risk transfer to the private sector under the hub approach; the benefits of getting capital expenditure “off the books”, as is achieved with the hub programme; and what is the actual worth to the public sector of any dividends eventually reaped by the Hub Charitable Foundation.

III Consideration and conclusions

One of the things which the analysis in this paper has clearly established is how the kind of measure quoted by SFT to the Public Audit Committee gives only a partial, and potentially misleading, impression of the true costs involved in hub schemes. To illustrate this point, it is worthwhile comparing two extremal measures of the overall cost of hub financing. On the one hand is the WACC of senior and sub debt, excluding fees: (that is, the measure apparently quoted by SFT.) On the other hand is the overall project IRR, including tax. The difference between the two measures is very significant: in all of the three examples considered here it is more than one percentage point, and in one of the cases is almost two percentage points. It is not being suggested here that one of these measures is wrong, and the other right: they are both

legitimate indicators for different purposes. (Although the author personally thinks that the project IRR is much the more informative measure.) The crucial point is that a full picture of what hub financing involves cannot be obtained on the basis of a single indicator, or a limited range of indicators.

The first, and possibly most important, conclusion to be drawn is that, to give the full picture, a full palette of indicators has to be used to analyse hub financing. This set of indicators should include:

- The effective interest rate on senior debt, both including and excluding fees, and the interest rate on sub debt.
- The WACC of senior and sub debt, and the combined IRR of senior and sub debt.
- Both measures of project IRR, excluding and including tax.
- The net present value of sub debt payments, calculated at a discount rate reflecting conditions in the potential secondary market for subordinate debt: and the net present value of the non-service element of the unitary charge, calculated at a discount rate equal to the appropriate National Loans Fund interest rate.

There are, in addition, further important implications for monitoring. One thing that became very apparent to the author in the course of this exercise is that it is labour intensive to produce such a set of indicators for any given project from the detailed financial projections for the project. This leads to the immediate conclusion, that a specific set of indicators should be defined, and that it should be a requirement for all hub projects that these standard indicators should be produced as part of the financial modelling for the project.

That leaves the question of who should specify these indicators. This should presumably be SFT, possibly in conjunction with the Public Audit Committee or Audit Scotland.

But indicators are only of value if they are considered and used. So it is recommended:

- That for each hub project, the indicators should be reported to SFT when the contract for the project is being finalised – so that SFT can use the indicators in their ongoing scrutiny of the operation of the hub programme.

- That the indicators for each scheme should be published by SFT as soon as the two year confidentiality period for that scheme has passed.
- So that up to date information is available publically, but without breaching confidentiality on individual schemes, the SFT should publish annual average information for each for each indicator as soon as possible after the end of each year.

Looking beyond monitoring, there are also implications for the *rationale* of the hub programme itself. The information analysed in this paper, while limited, nevertheless suggests that the financing of hub projects involves a significant opportunity cost to the public sector, (with hub projects potentially costing up to 40% more than borrowing equivalent finance from the NLF); and also significant potential for the private sector investors in hub sub debt to realise large profits, (with sub debt investors potentially able to recover their capital, and make additional profits of 80% of the sum invested, on secondary market sales of their holdings). There should be active consideration, by the Scottish Government and public authorities, as to whether the advantages of the hub approach justify these costs and potential profits. Even if it is too early as yet, given the limited information currently available, to make a final decision, these questions should be kept under active review, in the light of whatever trends might emerge from the improved monitoring system.

There are also implications for the Scottish Parliament's Public Audit Committee. This committee has responsibility for, among other things, scrutinising the financial performance of the Scottish Government and public bodies, and for examining the economy, efficiency and effectiveness of the public sector. It is painfully obvious, however, (as can be seen, for example, by the committee's response to SFT's evidence on 7 December 2017), that the audit committee struggles with this role. This is where a change of tack in the committee's approach could greatly help them in discharging their remit. The committee would find it much easier to penetrate below the veneer covering SFT activities if they were to insist that SFT reported regularly to the committee on the basis of a detailed set of indicators specified by the committee. It is recommended that the committee should take this step. And, of course, as regards financial indicators, it would be hoped that the indicators outlined in this paper would provide a useful starting point.

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