THE SCOTTISH OFFICE

Department of Health

NHS
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Dear Colleague

APPROVAL OF CAPITAL SCHEMES

Enclosed with this letter is updated guidance on the process to be followed for the approval of capital schemes by NHS Trusts, Health Boards and other Health bodies.

The guidance reiterates, and in some areas clarifies, that given previously in MEL(1996)16 (Approval of Capital Schemes) and Annex 2 of MEL(1996)48 (Capital Management). The procedures detailed here replace the guidance given in the two earlier MELs.

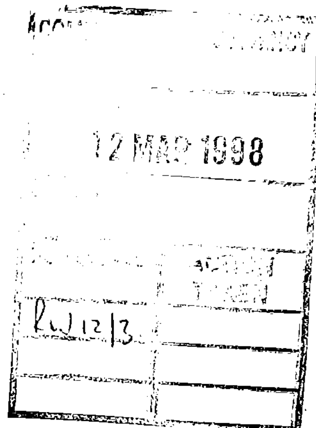
In particular, your attention is drawn to the following:
- all capital procurement should include consideration of PFI and if PFI is discounted, submissions must demonstrate why PFI is not an option (paragraph 2);
- for 1998-99 the capital plan has committed all available capital (paragraph 4);
- inclusion of a scheme in the capital plan does not guarantee funding (paragraph 6);
- the business case requirements detailed at paragraphs 8 to 14;
- the guidance on price bases at paragraphs 15 to 17;
- the approval process described in paragraphs 18 to 22 notably the central point (Ross Scott in the PFCU) for the submission of all Initial Agreements, Criteria Submissions and Business Cases; and
- the SCIM requirements for MCP returns (paragraph 24).

The revised procedures should be adopted with immediate effect.

Yours sincerely

Peter Collings

Dr PETER COLLINGS
Director of Finance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Recycled

APPROVAL OF CAPITAL SCHEMES

Background

1. The ME's role in managing capital is not that of determining centrally where capital investment will take place. Rather, capital proposals are built from the bottom up and although the ME retains a strategic role, its primary concern is in ensuring that proposed schemes can be afforded and offer good value for money whether funded conventionally with public sector capital or through the Private Finance Initiative.

2. However, the amount of public capital available to fund developments each year is limited and all capital procurement should include consideration of PFI. The PFCU will advise on the suitability of PFI but where, it is considered that a project has little chance of attracting private finance, for example refurbishment of existing facilities, it is the responsibility of each organisation to demonstrate that PFI is not an option. This should be clearly stated in the Initial Agreement, Criteria Submission, or Outline Business Case. While PFI will continue to play a role in funding certain types of developments, for example new build, equipment and IT, it is now clear that it is not appropriate to apply it to all projects.

3. With increased demand on public capital available, the ME has a key role in ensuring that the schemes which are funded are those which are of greatest priority to Health Boards and will provide most benefit to the patients of the NHS in Scotland as a whole. While a proportion of capital available will continue to be allocated to Trusts by way of a formula allocation (roughly 35%, at present, of the total capital), the balance of capital will be allocated to Trusts, Health Boards and Special Health Boards on a discretionary basis as part of the overall capital plan for the NHS in Scotland.

Schemes Bidding for Approval

4. In August 1997 all Trusts were asked to submit a five year capital plan. The proposals were provisionally prioritised by the ME in accordance with the strategic aims and priorities of the NHS in Scotland. Each Health Board was then asked to review the provisional prioritisation of schemes put forward by Trusts in their area and provide their own ranking. Having taken into account each Health Board's priorities for next year, the ME has now set out a capital plan for 1998/99. **The Capital Plan commits all capital resources available for 1998-99**. All Health Boards and Trusts have been informed of the schemes included in next year's plan.

5. Normally the ME will write out each year seeking Capital Plans which are consistent with Health Improvement Programmes (HIPs) and Trust Implementation Plans (TIPs). Health Boards and Trusts will therefore be informed annually of schemes included within the overall capital plan for future years. This will allow Trusts and Boards to progress with the preparation of the necessary business cases.

6. Inclusion of a scheme in the overall capital plan does not guarantee funding. As before, funding will be wholly dependant on the approval of the required business case and on demonstration that Health Boards support the scheme and its revenue consequences. This

will be demonstrated by the fact that the scheme and its financial consequences are included in the HIP.

7. Business cases bidding for public funding should only be submitted for those schemes identified in the five year plan. Only in exceptional circumstances will funding be considered for other schemes. In such cases, Trusts or Boards should contact the Management Executive Director of Finance before submitting a business case. Any such cases must be jointly agreed by Trusts and Health Boards if they are to be considered and their relationship to the HIP should be explained including, where necessary, the re-prioritisation of other capital investments within the Health Board area.

Business Case Requirements

8. So that proposals for schemes are presented as effectively as possible, the process described in the Scottish Capital Investment Manual (SCIM) will continue to be mandatory for all schemes which are bidding for funding approval. Separate guidance on business cases for IM&T schemes is provided in SCIM. **The following guidance applies to Trusts, Health Boards, Special Health Boards and CSA.**

Stage 1 - The Initial Agreement

◊ All schemes bidding for public funding
◊ All IM&T schemes
◊ All Trust non-IM&T PFI schemes over £1m
◊ All Board non-IM&T PFI schemes over £0.5m

9. For the above schemes an Initial Agreement document as outlined in SCIM should be submitted for approval by the Management Executive. The purpose of the Initial Agreement is to establish the schemes strategic context and priority, show a range of options, indicate a range of prices and consider the suitability of PFI. Initial Agreements should clearly state the relationship between the scheme proposed and the relevant HIP(s).

10. Where funding through PFI seems likely, an approved Initial Agreement will enable Trusts and Boards to bid for capital funding to cover fees for the preparatory work and for support through the Private Finance Process. A maximum of 1.5% of the total capital value of the scheme will normally be made available for this purpose with key milestones set allowing the release of fees over the project period. Generally, funding will not be provided to cover the fees on non-core schemes.

Stage 2 - Criteria Submission or Outline Business Case?

Stage 2A - Criteria Submission

◊ Trust Non-IM&T Schemes below £4m
◊ Trust Non-IM&T PFI Schemes above £1m but less than £4m
◊ Trust IM&T Schemes below £1m
◊ Health Board non-PFI Schemes below £0.5m

11. Following approval of the Initial Agreement, a brief submission should be prepared and forwarded to the ME which outlines evidence of how the scheme measures up against a set of key criteria. Annex 1 provides a list of the contents of the Criteria Submission. The Submission should be signed, in the case of Trusts by the Trust Chief Executive and Board General Manager, and in the case of Health Boards by the Board General Manager, and will be an auditable document.

- For schemes bidding for public capital, funding will be allocated on the approval of a Criteria Submission by the ME.
- For PFI schemes, once the Submission has been approved, the Trust or Board may proceed to OJEC advertisement, selection of preferred bidder and full business case stage. Although ME approval of the full business case will not be required, the FBC must demonstrate affordability and value for money.

Stage 2B - Outline Business Case

◊ Trust Non-IM&T Schemes above £4m
◊ Trust IM&T Schemes above £1m
◊ Health Board Schemes above £0.5m

12. Following approval of the Initial Agreement, Trusts/Boards must prepare an Outline Business Case for approval by the Management Executive. The OBC will set the scheme within a strategic context, identify and evaluate options and select a preferred option which is affordable and value for money. For PFI schemes, the OJEC advertisement should not be placed until the Outline Business Case has been approved by the Management Executive.

Stage 3 - Full Business Case

◊ Trust Non-IM&T Schemes above £4m
◊ Trust IM&T Schemes above £1m
◊ Health Board Schemes above £0.5m

13. Following approval of the Outline Business Case, Trusts/Boards must prepare a Full Business Case for approval by the Management Executive. The FBC will explore the detail of the preferred option in the OBC and, where a PFI option is developed compare it against a public sector comparator. For schemes bidding for public capital, funding will be allocated on the approval of the Full Business Case.

Overall Procedure

14. The overall procedure is shown in a diagram at Annex 2.

Price Bases

15. For the economic appraisal of schemes, present day prices should be used. That is, the estimated out-turn price of the scheme as if the construction works had been completed and the healthcare facility was moving into its operational commissioning stage. By this

means the capital estimates will equate more accurately with the present day revenue figures being used for economic appraisal and affordability purposes.

16. Where it has been confirmed that private finance is not an option, then at the FBC stage the present day price, as described above, must have added to it an estimate to bring the total up to the estimated out-turn price of the scheme based on the planned construction contract tender date(s) and construction periods. This total is important for resource allocation purposes. This provision for the difference between the present day price and the planned construction programme should be shown at item 11 of form FB1.

17. Where it has been confirmed that private finance should be pursued, the public sector comparator at the FBC stage should be compatible, i.e. the adjustment referred to in paragraph 16 should be built in to the PSC based on the planned private finance construction programme. The implications of a different provision timescale if the scheme had to revert to being publicly funded should be brought out in the risk analysis.

The Approval Process

18. All Initial Agreements, Criteria Submissions and Business Cases should be sent to Ross Scott, Private Finance and Capital Unit within the ME Finance Directorate. The PFCU will acknowledge receipt of the document within 5 working days and, because scheme titles often change, allocate a unique scheme reference number which must be used in all subsequent correspondence. Each document submitted will be circulated for comment within the ME and the appropriate regional Finance Manager will assess the comments and put a recommendation forward to the Capital Investment Panel, as appropriate.

19. The ME will continue to commit to providing a response to any submission made within 15 working days from the date of receipt. For schemes included in the five year capital plan, this response will be in the form of comments, an indication of whether the scheme is likely to receive approval or a request for re-submission with a statement of the areas to be addressed in order to bring the submission to an approvable state.

20. Approval or otherwise at each stage will be given at the monthly meetings of the Capital Investment Panel, in consultation with the Chief Executive of the ME, where appropriate.

21. Approval by HM Treasury is required for non-IM&T PFI schemes in excess of £10m and for IM&T PFI schemes above a capital value £1m. Approval by HM Treasury is required for non PFI schemes in excess of £100m. Once an FBC has been approved by the ME, it will be submitted to HM Treasury for their approval. Normally, HM Treasury turn round FBCs within two weeks. Liaison between HM Treasury and a Trust or Health Board is generally, in the first instance, at least, through the ME.

22. Furthermore, schemes with a capital value in excess of £40m require Ministerial approval.

Private Finance Initiative

23. Advice on Private Finance Issues should be obtained from the Private Finance and Capital Unit at the ME Finance Directorate.

Monitoring

24. Once funding approval has been given to a scheme, Trusts and Boards must ensure that the requirements described in the ' Management of Construction Projects' booklet within SCIM are observed. In particular, MCP returns (or the alternative NQS forms described in EPM(1998)2) are required for all schemes with a total cost exceeding £1 million in capital value (including VAT) using public funding. All MCP returns should be sent to Ross Scott, Private Finance and Capital Unit within the ME Finance Directorate.

25. The monitoring process and forms used are due to be reviewed over the next few months as part of an overall review of SCIM.

General

26. If the capital value of a project changes, previous ME approval will not necessarily apply to the revised costs and Trusts and Health Boards may have to make provision to fund additional costs from other sources. If the change in capital value takes a scheme outwith the delegated limit (e.g. from £3.8m to £4.2m for a construction project or from £0.9m to £1.1m for an IM&T project) the process must halt until all the procedures for the higher limit have been completed.

ANNEX 1

CRITERIA SUBMISSION CONTENTS

The Criteria Submission should contain the following information:

1. The title of the scheme as it appeared in the Capital Plan and as it will appear in Monitoring returns.

2. A brief narrative describing the preferred option, adding any relevant details not included in the option description in the Initial Agreement, and explaining the relationship between the proposed scheme and the relevant HIP(s).

3. Where the preferred option is to be publicly funded, a cost profile showing capital expenditure over the project period.

4. A summary clearly demonstrating the revenue impact of the scheme to Health Boards.

The Criteria Submission should also contain specific statements that confirm that:

a) the development fits with the agreed HIP(s) and the objectives of the Trust;

b) an appraisal of a full range of options has been considered and evaluated following the guidance in SCIM, considering costs, benefits and risks;

c) a business case has been approved by the Trust Board;

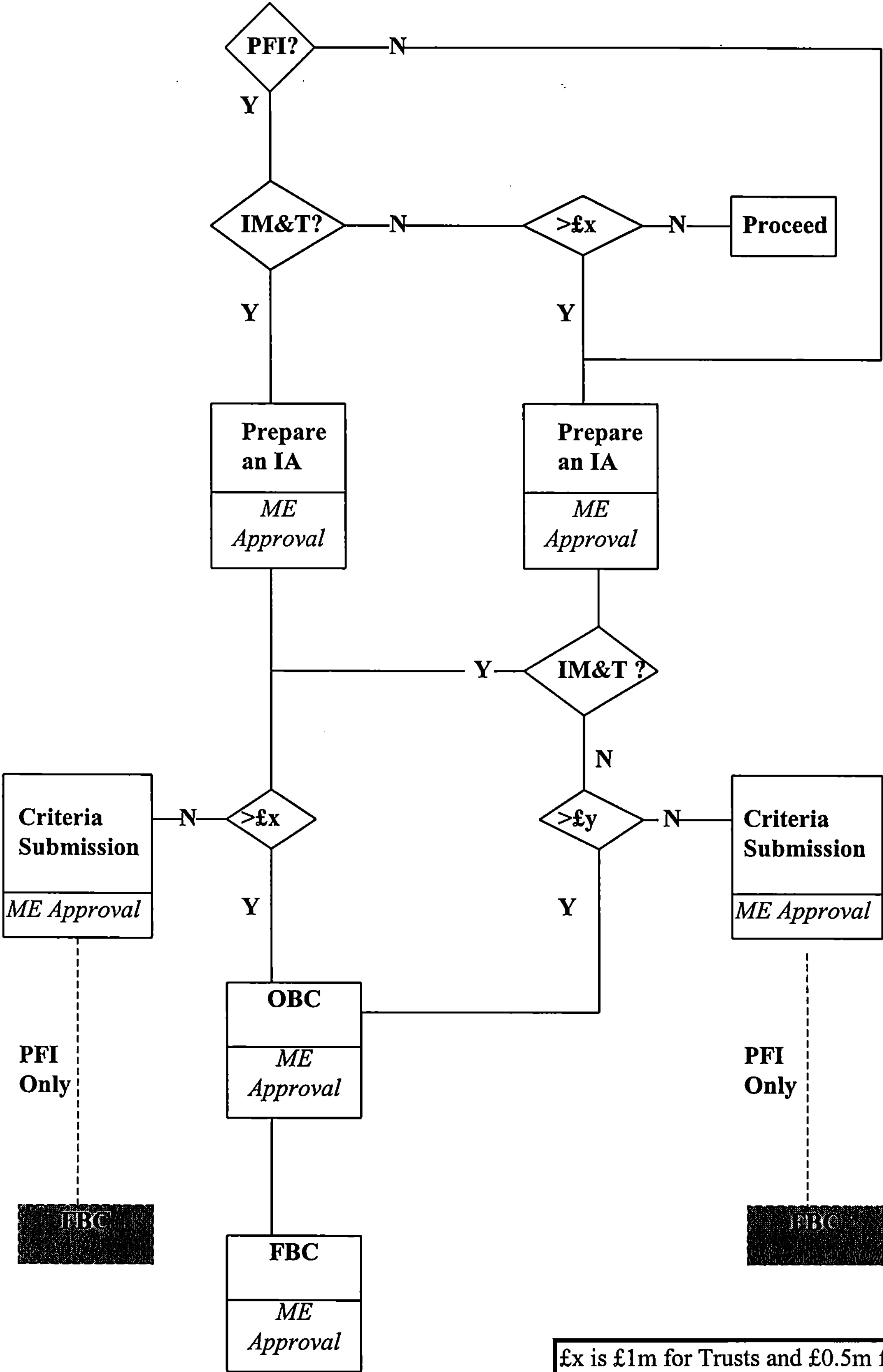
d) Health Board support for the scheme and any resulting revenue consequences has been obtained;

e) private finance has been adequately explored - if a private finance route is not to be followed, then the reasons why should be outlined;

f) a plan for implementing and evaluating the project has been drawn up.

The Criteria Submission should be signed off, in the case of Trusts by the Trust Chief Executive and the Health Board General Manager; or, in the case of Health Boards, the Health Board General Manager.

ANNEX 2



£x is £1m for Trusts and £0.5m for Boards

£y is £4m for Trusts and £0.5m for Boards