



HM TREASURY

1 Horse Guards Road London SW1A 2HQ

Tel: 020 7270 4640

Fax: 020 7451 7607

jeremy.pocklington@hm-treasury.x.gsi.gov.uk

www.hm-treasury.gov.uk

To Departmental Private Finance
Units

21 March 2007

Revision to Standardisation of PFI Contracts (SoPC)

I am pleased to announce that HM Treasury has now published SoPC Version 4 ("SoPC4") on its public website.

Following the commitments made in 'PFI: strengthening long-term partnerships' ("SLTP") in March 2006, HM Treasury has been developing its policy in several areas and has sought to provide further guidance on areas of key importance to Authorities. SoPC4 delivers on these commitments and includes further guidance on, among other areas:

- Price and Payment Mechanisms (Section 7);
- Changes in Service (Section 13);
- Price Variations (Section 15);
- Change of Ownership (Section 18);
- Authority Break Points (Section 21.5.4);
- Information Provisions (Section 26.2);
- Contractor Distress (Section 35);
- Bond Finance (Section 36); and
- Corporate Finance (Section 37).

Further details of the main changes made from SoPC Version 3 are set out in the accompanying summary paper 'Standardisation of PFI Contracts – An Outline of Principal Changes'. As previously, two versions of SoPC have been made available on the HM Treasury public website; a clean copy of Version 4 and a marked-up copy showing changes made from Version 3. These changes include amendments made in the Addendum to SoPC Version 3 and the additional chapter on insurance, both published in December 2005. It should be noted that the mark-up version is provided to assist practitioners, and whilst every effort has been made to ensure its accuracy, only the clean copy should be relied upon for compliance purposes.

The application of the revised guidance is mandatory for all PFI projects that are still in competitive procurement (i.e. where final bids have not yet been

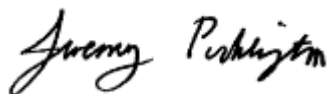


received or the competitive dialogue not yet been closed) on or after 1 May 2007. The guidance is therefore not mandatory for those PFI projects at preferred bidder or where final bids are received before 1 May 2007. However, adoption of the revised guidance and adherence to the principles contained therein is encouraged for those projects where its use is not mandatory.

The derogation and sector specific contract approvals process is set out in the Appendix hereto.

Authorities should note in particular the amendments to Section 13 (Change in Service) of SoPC4. Further guidance on variations has been provided, following the commitment made in SLTP. The required drafting in SoPC Version 3 relating to Change in Service, Small Works and Contractor Changes in Service at clauses 12.4, 12.5 and 12.6 is no longer required. Instead, Authorities must develop a project-specific Change Protocol that complies with the principles set out in Section 13 (Change in Service). These contractual principles constitute a "Core Area" for the purposes of the derogations process, and therefore each project to which SoPC4 applies must include a compliant Change Protocol. Sector specific contracts developed by Government Departments and/or 4ps should include a compliant Change Protocol. Once this is agreed with HM Treasury, Change Protocols compliant with that sector specific contract need not be individually approved.

If you wish to discuss these issues further please contact Partnerships UK ("PUK") Helpdesk (Tel: 020 7273 8384/8383, e-mail: helpdesk@partnershipsuk.org.uk).



Jeremy Pocklington
Head of Corporate and Private Finance

Appendix - Approval of sector specific contracts and submission of derogations from Standardisation of PFI Contracts Version 4 (“SoPC4”)

Application of SoPC4

1. SoPC4 applies to all PFI contracts in England. PFI is not suitable for projects with a capital value of less than £20 million, nor should it be used for IT projects.
2. SoPC4 may also be applied to PFI contracts in Wales, in which case the Welsh Assembly Government will determine the detail of such application.
3. PFI contracts in Scotland and Northern Ireland must comply with guidance relevant in those jurisdictions.
4. As set out above, all PFI projects still in competitive procurement (i.e. where final bids have not yet been received or the competitive dialogue not yet been closed) on or after 1 May 2007 must comply with SoPC4.

Definition of Compliance with SoPC 4

5. In order to comply with SoPC4, each PFI contract must include all required drafting, as referenced in paragraph 1.4.1 of SoPC4. In addition, there are a number of clear contractual principles (without specific contractual drafting) set out in SoPC4 which must be complied with. Together, the required drafting and mandatory contractual principles are referred to as the “Core Areas”.
6. If a project wishes to derogate from a Core Area, it must submit a derogation request to HM Treasury for approval. When assessing derogation requests, HM Treasury may request PUK to advise and manage the process.
7. Where permissible derogation language is provided in SoPC4, specific derogation approval is not required when using this language, subject to compliance with all relevant conditions.
8. Where SoPC4 sets out suggested drafting or approaches, individual procuring bodies and sponsoring departments will be responsible for assessing whether the approach taken in their contract is reasonable and compliant with the overall approach of SoPC4. HM Treasury will not require sight of these aspects of individual contracts.

Sector Specific Contracts

9. A number of departments have already developed sector specific contracts, which use SoPC Version 3 as a starting point, but reflect the inevitable differences between PFI procurement in different areas of economic activity. In addition there are a number of 4Ps procurement packs, which contain sections giving sector specific guidance on PFI contracts. Work should now

begin to ensure these contracts and sections reflect the principles laid out in SoPC4¹.

10. The process for agreeing the sector specific contracts will be:

- each Department will conform its sector specific documents to SoPC4 terms as far as possible;
- the Department will provide HM Treasury with a copy of such conformed document for approval, together with a report identifying where there is a sector specific necessity for its guidance to derogate from SoPC4 terms, and the rationale for each such derogation; and
- PUK, on behalf of HM Treasury, will undertake the assessment and agreement of the contract.

11. HM Treasury will contact individual Departments to discuss timetables for the update of all existing sector specific contracts.

12. Once sector specific contracts have been agreed with HM Treasury, Departments should ensure that PFI projects they sponsor fully comply with those documents. Derogations from the Core Areas in individual PFI contracts which have already been agreed in the relevant sector specific contract will not need to be sent again to HM Treasury for approval.

Derogations from SoPC4 prior to approval of Sector Specific Contracts

13. For the transitional period prior to the approval of sector specific contracts, HM Treasury expect Departments to ensure that, for all PFI projects which were still in competitive procurement on or after 1 May 2007, the PFI contracts comply with the Core Areas.

Individual contract derogations

14. HM Treasury believes that derogations from SoPC4 or approved sector specific contracts should only be made in exceptional circumstances on project-specific grounds. We would emphasise that it is essential that departmental Private Finance Units take an active role in ensuring that the policy on standardisation is implemented.

15. If sponsoring departments are aware that individual PFI projects (for which they have oversight) are seeking to derogate from the Core Areas they should, in the first instance, directly assess the specific derogations and work with the procuring authority in order to reduce these to a bare minimum before presenting a case to HM Treasury. Sponsoring departments should avoid approaching HM Treasury without having first convinced themselves through detailed assessment that there is an exceptional project specific need for any such derogation.

¹ Where a derogation from a Core Area of SoPC Version 3 has previously been approved on behalf of HM Treasury in a sector specific contract, and such Core Area has not been amended in SoPC4, there is no need to seek further approval for such derogation.

16. If HM Treasury is presented with extensive derogations reports it is likely to revert back to the department to challenge this position. It should also be borne in mind that the more extensive the derogations provided the longer it is likely to reach an agreed position. Such timing concerns should be taken into account in timetables for closing deals. While HM Treasury will make every effort to be responsive to the needs of procuring bodies and Departments, the last minute provision of extensive derogations will be likely to slow the procurement process.
17. Subject to the above, PFI procuring bodies should seek derogations approval once contractual drafting is settled. In the case of a procurement using the competitive dialogue procedure, as there can be no significant changes to the PFI contract following final tender, approval for any necessary derogations should be sought in respect of each bidder prior to conclusion of the dialogue.
18. As previously, where PFI procuring bodies seek advice directly from PUK on any exceptional need for derogations from SoPC 4, they should look to fund this work themselves.
19. HM Treasury would not normally expect to directly engage in contract discussions relating to derogations with private sector parties involved in PFI deals such as lenders and equity providers. HM Treasury's contact would usually be through the public sector bodies responsible for the contract. This is to ensure that there remains a clear line of communication and responsibility in such negotiations.

Consequences of non-compliance

20. Projects that are non-compliant with SoPC4 and have not had their derogations or sector specific contract approved by HM Treasury will not have their Final Business Cases approved. In the case of Local Authority PFI projects, SoPC4 compliance is a pre-requisite for approval of PFI projects at the Project Review Group.