taking the initiative

a framework for purchasing under the private finance initiative
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# Taking the Initiative

## Introduction

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For whom has this paper been written?

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Main features of the private finance initiative

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Appendix 1: Members of the advisory group
Introduction

Why has this paper been written?

1. The way in which public bodies procure the facilities that they need to deliver services has been changing rapidly in recent years. Examples of these changes include compulsory competitive tendering (CCT), contracting out and privatisation. In 1992 the government of the day launched a policy that was to become widely known as the private finance initiative (PFI). The Government’s aim was to ensure that the best possible services should be provided to the public, irrespective of which agency actually had operational responsibility for providing those services. For the same reason, the present Government is promoting PFI and other forms of joint working between the public and private sector, and is providing a range of financial incentives to encourage these policies.

Notwithstanding the provision made in the public expenditure plans recently announced, the resources likely to be available to some public bodies may mean that using a PFI procurement may be the only realistic way of financing improvements to services in the foreseeable future. In such cases, clearly important issues of value for money can arise.

2. Any large-scale procurement by whatever means must be controlled properly, and the use of PFI does not affect this basic principle. Whether PFI or a more conventional procurement process is pursued, a control framework is needed to ensure the proper use of resources and stewardship of funds. However, PFI has features that distinguish it from other forms of procurement – in particular, the purchase of a stream of services and the use of associated capital assets for long periods, often for several decades, and the substantial commitment to pay for these services. The amount of money and the length of the contract mean that these decisions need to be controlled even more carefully.

3. The intention of PFI is to bring, through competition, a range of private sector expertise and finance into the provision of public services. In order to achieve value for money, the higher costs incurred by private sector involvement – for example, in borrowing money – have to be more than outweighed by lower design, construction, management and operating costs. Whether PFI contracts generally offer value for money in terms of service delivery will become apparent only once the service is being provided; only then is it possible to compare costs and services with those of similar PFI contracts and with those procured by other means. There is no formula that can guarantee better value for money from a particular scheme; each scheme – irrespective of size and type – has to be properly evaluated and controlled to ensure its successful procurement and operation.
For whom has this paper been written?

4. This paper aims to help members and chief officers at local authorities (including police authorities), and board members at NHS bodies, to consider the strategic and control issues that they should address to ensure the proper control of a PFI procurement. The decisions facing councillors, chief officers and board members are onerous – for some public bodies a major PFI scheme will be the largest single procurement decision that has ever been contemplated. An effective framework will help these decision-makers to demonstrate their proper stewardship of public funds.

How should this paper be used?

5. This paper is designed primarily for organisations that are either considering the use of PFI or are in the early stages of preparing a scheme. The paper is aimed at stimulating consideration of how decisions about PFI schemes can be made on a properly informed basis. It focuses upon the procurement process up to the point of contract signature and also includes arrangements to enable the proper management of the contract during its operational period and mechanisms to protect public services.

6. The paper is designed to be helpful as an overview to councillors, chief officers and board members who are new to the process, as well as a source of information on the key control issues that need to be considered as a PFI procurement progresses. Checklists of questions that councillors, chief officers and board members may wish to consider are included at the end of each section and are gathered together in a centre pull-out section.

7. The paper does not provide comprehensive coverage of all aspects of PFI procurement – it focuses on the control framework. Nor is it written to provide guidance about the detailed project management of a scheme, although those involved at an operational level may find the issues covered here helpful when considering how they can best help councillors and board members to fulfil their role.

8. The paper uses case studies drawn from actual schemes to illustrate current practices in different public bodies. These practices should not be taken as the recommended, or only, approaches to particular issues and are not in any way endorsed by the Audit Commission as being universally appropriate.

9. Using the guidance in this paper will not guarantee the success of a particular scheme, but should highlight the key factors that need to be considered in the course of a PFI procurement.

10. PFI is one of several possible methods of procuring investment in assets and is often used following a wider review of the needs of an area and of existing assets. Two previous Audit Commission publications provide guidance on these issues: *Just Capital: Local Authority Management of Capital Projects* (1996), and *Rome Wasn't Built in a Day: A Management Handbook on Getting Value for Money from Capital Programmes and Construction Projects* (1997).
The research behind this paper

11. Information was gathered from some 26 schemes in sectors as diverse as prisons, universities and police, and views were sought from people in both the public and private sectors. In addition, visits were made to six local authorities and NHS bodies with PFI schemes, ranging from schools, roads, waste disposal, large district general hospitals and community health schemes. The results were reviewed by an advisory group for whose assistance the Audit Commission is grateful [APPENDIX 1]. Thanks are also due to those organisations which have provided examples of current practice. Responsibility for the contents of this paper, however, rests solely with the Audit Commission.

The structure of this paper

12. The first section sets out the main features of the PFI and how it both resembles and differs from more traditional means of procurement. Subsequent sections examine the relationship between a public body's planning process and PFI procurement; views from the private sector on the public sector's approach to PFI; a control framework for a PFI procurement including the types of decisions that councillors and board members should take, the issues of risks, value for money, affordability and the key features of a payment mechanism, and contract management arrangements. Attention is also given to the creation of a project team, the use of external advisers and the importance of clear ownership, leadership and communications in a properly managed procurement process. The final section brings together the main points for councillors and board members.
1. Main features of the private finance initiative

How PFI differs from conventional procurement routes

13. The main features of a PFI procurement include:

• the financing of assets by the private sector rather than by the public sector;
• the negotiation of details of a scheme with a preferred supplier;
• a commitment to purchase services for a long time;
• the purchase of both services and associated assets within a single contract;
• the relative newness of this form of procurement and the sometimes costly learning process involved; and
• an explicit focus on the risks inherent in the provision of services over many years and, through negotiation with the private sector, the transfer of appropriate risks, at a price, away from the public sector.

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EXHIBIT 1
The responsibility of the public sector in a traditional procurement compared to a PFI route

There are both differences and similarities between a procurement using traditional methods and using PFI.
14. However, while some financial and other risks can be transferred, the public sector remains accountable for securing the provision of public services should the initial contract break down. It still has to satisfy itself that arrangements are in place to provide services at the required time and to the agreed standards.

15. There are differences and similarities between conventional procurement and procurement under PFI [EXHIBIT 1]. It should also be recognised that the public sector enters into contracts with the private sector that fall between these two approaches.
16. The PFI schemes in local government and the NHS are beginning to cover a widening range of services [BOX A].

**BOX A**

**A selection of current PFI schemes in local government and the NHS**

PFI is being used for an increasing range of services

<table>
<thead>
<tr>
<th>Service</th>
<th>Outline of scheme</th>
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<td>Social services</td>
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<td>Economic development</td>
<td>Link road to development area</td>
</tr>
<tr>
<td>Libraries</td>
<td>New library</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>POLICE</strong></td>
<td></td>
</tr>
<tr>
<td>Premises</td>
<td>New headquarters building</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>NHS</strong></td>
<td></td>
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<td>Hospital</td>
<td>New district general hospital</td>
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<td>IT</td>
<td>Patient administration system</td>
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<tr>
<td>Clinical accommodation</td>
<td>Refurbishment of maternity and paediatric buildings</td>
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<tr>
<td>Clinical equipment</td>
<td>Provision, management and maintenance of theatre anaesthetic and monitoring equipment</td>
</tr>
<tr>
<td>Specialist facility</td>
<td>Provision, management and maintenance of a magnetic resonance image facility</td>
</tr>
</tbody>
</table>

*Source: Audit Commission*
17. There are several features about the nature of PFI procurement that should be carefully considered by councillors and board members before they take decisions about using it for a particular scheme. Among the most important is a clear recognition that PFI contractually commits the public sector body to paying for services for long periods of time. This could restrict the future flexibility of the body to determine the way that services are provided, unless careful attention is given to incorporating into the contracts provisions for making changes to the nature and cost of services provided. A second key issue is that capital expenditure under PFI is undertaken by the private sector and is paid for by the public sector as part of an annual charge, rather than by the public sector either meeting this expenditure directly or by borrowing and then repaying these loans over a period of years.

18. The clear disclosure and explanation of the contractual liabilities arising from PFI contracts in annual accounts and reports is another important issue that needs to be addressed.

19. It is also important to be aware that some schemes may be more attractive to the private sector than others – for example, because of their larger size. These schemes may not, however, be the highest priority for the public sector. Councillors and board members should be aware of the risk of this issue distorting their priorities.

20. A further feature of PFI schemes is that quite specific skills are required to successfully conclude a PFI contract that represents a good deal for the public. Because PFI contracts bundle so many elements together, the requirement for high quality skills at negotiating complex transactions to a settlement should not be underestimated, along with the acceptance that people with such skills are able to command high fees. While such skills can be bought in, it is also important for public bodies to pay attention to building up the abilities of their own staff, and acquiring the skills in-house for overseeing ongoing and future PFI procurements. A public body entering into a PFI procurement for the first time should be prepared to tackle a learning curve that is likely to involve a significant time commitment from chief officers and which may also involve buying in specialist advice.

Potential benefits of PFI

21. A PFI procurement may give a public body the opportunity to focus more upon what services are needed rather than how they will be provided. But it does not mean that ultimate responsibility for the existence of the service and its quality can be transferred. Rather, the public body must design systems for monitoring the service that is received, and ensure that a real link between service quality and payments to the supplier is included in the contract.
22. While not unique to it, PFI does highlight the potential to benefit from efficiently integrating the design of assets and their subsequent operation. In addition, a PFI procurement can mean that proper provision is made in the contract for maintaining assets through the entire contract period, and thus ensure that a backlog of capital maintenance does not accumulate. Equipment may also be replaced on a regular basis and so avoid the problem of obsolescence. All this is achieved only at a price. Bringing private sector commercial skills to the utilisation and management of the public sector estate is another possibility.

Legal and contractual aspects of PFI

23. The nature of the legal and contractual agreements involved in a PFI scheme can be complex. In addition, there are likely to be a range of other important relationships that could affect the progress of a PFI procurement [EXHIBIT 2]. Identifying and managing all these relationships is the cornerstone of a successful PFI procurement. Some of them will be common to other approaches to procuring services – for example, contracting out a service that was previously run in-house will involve negotiations with trades unions, just as a PFI deal will. Other relationships, such as that with the special purpose vehicle company, tend to be more unique to PFI.

EXHIBIT 2

Key relationships in a PFI scheme

The identification and management of the key relationships in a PFI procurement is important in achieving a successful deal.

Source: Audit Commission

The identification and management of the key relationships in a PFI procurement is important in achieving a successful deal.
24. Choosing to pursue a PFI procurement does not in any way diminish the public body’s responsibility to fulfil its statutory obligations, nor its duty to be fully accountable for its decisions. PFI puts the performance of these duties into a different context – in which there are different types of relationships to be managed, and where the financial consequences of decisions are more prominent than under a traditional procurement route.

25. Public bodies must also bear in mind that, although one of the Government’s intentions is to increase the use of PFI, there is a detailed vetting process of proposed schemes before approval is given to go ahead. The approval process for PFI schemes has become more structured under the present Government. In the NHS, outline business cases and full business cases must now be approved by either the regional office or headquarters of the NHS Executive, depending on the size and nature of the scheme. A local authority wishing to receive revenue support grant (RSG) towards PFI charges has to obtain approval from the Treasury’s PFI project review group before the formal procurement process can begin.

Deciding on PFI

26. Experience from early schemes shows that any organisation that is considering using a PFI procurement has to have a clear view about:

- what it is trying to achieve;
- why it is minded to use PFI as opposed to any other means of procurement;
- the nature of the relationship between its existing corporate planning process and PFI; and
- whether PFI provides an opportunity to address some long-standing problems.

27. The key starting point for any public body is that PFI is a means of procurement that should always follow a comprehensive planning process. The relationship between the planning process in a public body and PFI procurement is explored further in the next section.

QUESTIONS

- Is there an understanding of PFI and how it differs from other forms of procurement?
- Has the range of relationships likely to be involved in a PFI scheme been identified and plans made to manage these?
2. Planning and PFI procurement

The importance of planning

28. The most important point to keep in mind is that procurement should always follow planning. *Just Capital* and *Rome Wasn't Built in a Day* both highlight in detail good practices for the planning and management of capital programmes and construction project. Many of these good practices also apply to a PFI procurement. These reports commented on the risk inherent in PFI of particular schemes being promoted because they are more likely to appeal to the private sector. Schemes might also be pursued because some subsidy from central government is available, rather than because they are the highest priority for the organisation. Given that a PFI contract may commit the public sector to decades of payments for services, the decision-making process must be very clear and rational. Otherwise there is a risk that the PFI procurement process, rather than the organisation’s planning process, will determine the nature of the services to be delivered.

What PFI can offer

29. However, public bodies can use PFI in different ways, ranging from the procurement of services requiring investment in a single asset that would not be possible within existing funding regimes, to creating a means of meeting the aims of the wider organisation by unlocking the value in existing assets and allowing these resources to be redirected to priority areas.

...procurement should always follow planning.
30. In some cases, PFI may be used as a convenient and cost-effective way of dealing with isolated problems such as rebuilding and running a single school's rundown buildings [CASE STUDY 1]. In other cases, the assets and services involved may be of fundamental importance, both in terms of their cost and significance to the public – for example, the provision and running of an entire hospital exclusive of medical and nursing services. In such cases the body will need to undertake a complete review of its strategy to determine what is needed and how it should be procured. Often this review can be done jointly with other organisations – for example, in the case of a hospital, it should involve both the NHS and social services.

CASE STUDY 1: Lancashire County Council – Fleetwood High School

Background

The local education authority covers an area of predominantly rural communities, small towns and about six large urban centres. Fleetwood High School has been operating from two sites, all in old buildings, since its creation by a series of mergers in the early 1980s. The school is well supported and is likely to face an increasing pupil roll. There have been proposals, first mooted over 10 years ago, to redevelop the largest site and stop using the other one.

Financial factors

Without any new development, the council will have to spend some £5 million simply to keep the buildings on the two sites in a useable condition. It does not have such resources available. The backlog maintenance looks set to grow.

Proposal

The intention is to invite bids from the private sector to:

• demolish the present buildings on the main site;
• design, build, finance and operate a secondary school on the main site;
• explore the potential for selling the other site; and
• consider the potential for joint education and community use of the new facilities.
31. There may be other triggers for using PFI. An organisation may have considerable latent value in existing assets that are perhaps under-used or expensive. PFI may provide an opportunity to sell assets and/or change the use of them in order to release resources to improve services for the public or to reduce costs [CASE STUDIES 2 AND 3]. Just Capital recommended that public sector organisations should periodically review their assets in this way but, again, PFI deals are only one of several ways to release under-used assets.

CASE STUDY 2: Glasgow City Council: secondary schools

Background
The Council covers a densely populated urban area with some wards containing areas designated as socially and economically disadvantaged. Because of population changes over a number of decades, some 40 per cent of all secondary school places are surplus to capacity. Demographic trends show that the number of secondary schools could be reduced from the current 38 to around 30.

Financial factors
The present school estate has a growing backlog of maintenance running into tens of millions of pounds, with no real prospect of capital being available to tackle this and other required spending. There may be potential to release some of the value tied up in the current under-used estate in order to develop services more in line with the needs of the city.

Other factors
The Council has divided the city into a number of distinct community areas for the purpose of social and economic development. The aim is to link the rationalisation of secondary school places to the needs of each community area, the idea being that a community's sense of well-being and potential is heavily dependent on the provision of good quality educational facilities.

Proposals
The intention is to follow extensive consultation with interested parties with the invitation to the private sector to submit bids to:

- provide the city with a reduced number of secondary schools and a wide range of services such as caretaking, security, cleaning, catering and maintenance;
- build some new schools, adapt others to make them larger and renovate yet others to bring the entire estate up to proper standards; and
- identify surplus sites for disposal or alternative use.
Background

The city covers inner-city areas and part of the suburban hinterland. For many years the priority to replace an ageing primary school in a socially deprived part of the city has been hindered by the lack of capital. The Victorian school is in a dilapidated state and will need substantial expenditure simply to keep it operational.

Other factors

One of the aims of the local health authority has been to improve the provision of community health services. For some time the City Council and Health Authority have been discussing the prospects of some form of joint development in this part of the city.

Proposals

The City Council invited bids from the private sector to:

• provide a fully serviced primary school on an adjoining site;
• demolish the existing buildings and replace these with playing fields and new housing/commercial development; and
• discuss with the Health Authority how to meet the need for community health facilities on one part of the site, thus bringing a contribution from the Health Authority to the scheme.

Current position

Negotiations are taking place with a preferred partner and a draft legal agreement is being considered.
32. The results of forward planning and reviewing services and assets should then be brought together before a decision is made as to the outputs required and whether to use PFI or other means of procurement [EXHIBIT 3].

QUESTIONS

- Is the relationship clear between the planning process and the procurement options?
- Is there an understanding about the way that a PFI procurement can be used to tackle single-service, cross-service and cross-organisation issues?
- Is PFI an integral part of the body’s procurement policy?

EXHIBIT 3
Planning and procurement

The decision to use PFI to procure services should be made only as part of an overall planning process.

Source: Audit Commission
3. Working with the private sector

33. There is a lot of experience in public bodies of working with the private sector. Using a PFI procurement extends the concept of joint working on to a larger scale and to achieve this successfully, each side needs to appreciate the concerns of the other. In order to secure value for money, a public body needs to understand what is likely to attract private sector interest to a scheme and then seek to use a competitive process to obtain the best possible offer from potential suppliers.

Understanding the costs involved

34. The aim of the public sector is to secure the consistent and continued delivery of services of an appropriate quality at the lowest possible price. The aim of a PFI supplier is to have a profitable contract. For the public sector to achieve its aims it needs to be a tough, well-informed negotiator. But in any contract there should be a desire to build a solid working relationship based upon mutual trust, where both sides recognise common interests and are prepared to work together to resolve problems. While the public body must always prioritise the public’s interests, it can assist the PFI procurement process and help to avoid delays and any consequent costs by trying to understand the concerns of the private sector.

35. Once a public body decides to take the PFI procurement route, it has to appreciate that this is likely to be a costly process – for itself and for its potential private sector partners. So it is important that the public body is clear about its main requirements and that PFI is a realistic option before it engages in discussions that will cost it and the private sector time and money. But, equally, the private sector has to accept that some preliminary discussions may well prove abortive just as not all contracts tendered for will be won.

The private sector agenda

36. To help to deliver successful schemes, the private sector sees the following as important issues for public bodies to address:

- being able to afford the PFI charge;
- showing demonstrable commitment to the PFI process;
- producing a clear and settled service requirement at an early stage;
- having a realistic approach to risk allocation;
- possessing the legal powers to enter into the contract;
- having a person with sufficient authority, knowledge and commitment to drive the PFI process along in the public body; and
- timely decision-taking.
37. One of the most frequent comments from bidders is that they are asked to tender for a service that is ill-defined and subject to significant change as the procurement proceeds. While the bidder should be able to produce innovative solutions, the public body does need to be clear about the services that it requires. Failure to do so can mean repeated attempts to clarify the brief with bidders wasting money costing out their interpretation of what they think is being requested. It is also likely to be the case that when a bidder is faced with uncertainty, this will be reflected in a higher price. Such uncertainties will have to be resolved as the procurement proceeds and inevitably lead to delay, or in some cases the abandonment of the scheme.

Allocating risk

38. An integral part of the service requirement is the desired allocation of risk between the parties. Each side will seek to minimise its risks. One private sector criticism is that public bodies have an unrealistic attitude about the risks that can affordably be transferred to the private sector. In the main, these complaints relate to attempts to get the private sector to accept demand- or volume-related risk, and they are not always valid. The public sector should be a tough negotiator and seek to transfer as much risk as it can to the private sector. However, it should be borne in mind that transferring risk can increase costs, and in some cases it may be more cost-effective to retain certain risks. Risk is likely to be affordably transferred only if the receiving party has a reasonable influence over the associated events, or if it is a common business risk, such as general taxation rates.

39. The need for timely decision-taking is in the interests of all parties – but, equally, expenditure of public money has to be subject to due process and this requirement must not be neglected. However, where a local authority requires the commitment of central government for additional RSG – or an NHS trust the support of its purchaser and the NHS Executive – to make a scheme affordable, it is important that the necessary preparatory work with the relevant central body is undertaken early in the process.

QUESTIONS

• Is there an understanding of the concerns of the private sector?
• Are there arrangements in place to deal with these concerns but always maintaining priority for the public body's interests?
4. Framework for a PFI procurement

Accountability

40. Anyone taking decisions that involve spending public money has a duty to act in a proper and honest way. Decisions have to be taken in a reasonable manner, according to 'Wednesbury principles' as set out by the courts in a case dating back to 1948. These principles require that only relevant factors should be considered when making a decision, and all irrelevant or extraneous factors ignored. Councillors and board members must be able to provide reasoned and cogent arguments for the course of action taken, backed up by proper records, in order to demonstrate how they have discharged their stewardship of public funds.

41. In principle, the factors influencing decisions about a PFI procurement will be the same as for any other decision. What can make decisions involving PFI schemes more onerous is the size and length of some of the contracts [EXHIBIT 4].

EXHIBIT 4
Scale of commitments in recently signed PFI deals

The financial commitments in PFI deals can be large and for long periods of time.

<table>
<thead>
<tr>
<th>Public body and service</th>
<th>Contract period (years)</th>
<th>Annual PFI fee</th>
<th>Break clause/option</th>
<th>Renegotiated fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dorset County Council</td>
<td>0 Years</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Serviced secondary school (except teaching staff)</td>
<td>15 Years</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Carlisle NHS Trust</td>
<td>30 Years</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>474 bed hospital</td>
<td>45 Years</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dartford &amp; Gravesham NHS Trust</td>
<td>60 Years</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>400 bed hospital</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Norfolk &amp; Norwich Trust</td>
<td>0 Years</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>800 bed hospital</td>
<td>15 Years</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>30 Years</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>45 Years</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>60 Years</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: The NHS schemes exclude medical, nursing, diagnostic, paramedic and management staff.

Sources: Dorset County Council; NHS Executive
42. It is essential that councillors and board members make arrangements to put in place an effective control framework and can demonstrate that they have done so. This framework should be based on well-informed decisions that, in turn, rely on the proper consideration of a range of factors [EXHIBIT 5].

**The control framework for PFI schemes**

43. While the level of detailed knowledge obtained by councillors and board members will vary depending on local circumstances, as decision-makers they should require assurance from officers that the key controls over a PFI procurement are in place and are operating properly. The rest of this section examines these key features in more detail.

*It is essential that councillors and board members make arrangements to put in place an effective control framework...*
44. The control framework surrounding a PFI procurement will differ between public bodies depending on the complexity of any particular scheme and the underlying control environment already in place. The Treasury has set out the steps that should be taken when first considering and then entering into a PFI contract. Different elements of the control framework will also apply more rigorously at different stages of a PFI procurement, although to some degree all the elements of the control framework should be considered at each stage [EXHIBIT 6].

EXHIBIT 6
Applying a control framework around a PFI procurement

The Treasury has set out the key stages of a PFI procurement in its publication, Step-by-step Guide to the PFI Procurement Process.

Key stages in a PFI procurement

Note: While almost all the features of the control framework will have some applicability at each stage in a PFI procurement, the bars indicate those that are likely to be particularly relevant at the stages indicated.

Source: Audit Commission
Awareness

45. The present PFI policy originated in 1992, but since then the experience of the private and public sectors as well as changes in government policy have led to some significant shifts in the nature of the schemes being proposed. For example, in the early years there was a feeling that the private sector would accept a payment mechanism linked explicitly to the use made of a facility – the so-called ‘demand or volume risk’. Experience to date has shown that in school or hospital schemes, where they have no control over teaching or medical staff and cannot influence directly the number of pupils or patients, private sector partners favour payment mechanisms linked to availability of the specified service to the required performance standard. In the case of road schemes, payments are usually based on traffic flows. However, public bodies should not feel bound by experience to date.
46. A public body considering PFI must seek to become an 'informed consumer' in the PFI procurement process. To do this it must understand PFI in sufficient depth that it can debate the relative merits of PFI against other forms of procurement, and so that it can discuss PFI options with potential advisers and PFI suppliers from a position of knowledge. A public body can take action to keep itself up to date about PFI developments [EXHIBIT 7].

A public body considering PFI must seek to become an 'informed consumer' in the PFI procurement process.

EXHIBIT 7
Steps to keep up to date with PFI developments

To become an informed ‘PFI consumer’, a public body needs to keep its knowledge up to date.

Source: Audit Commission
47. This knowledge needs to be brought to bear on specific schemes [CASE STUDY 4].

CASE STUDY 4: Being aware of PFI and exploring its potential for specific schemes

Example 1: Essex County Council – road scheme

Essex County Council was one of the first to consider using PFI for a road scheme. As a pioneer it decided, after acquiring a basic awareness of PFI, to hold a series of workshops to help councillors and officers to think through the process and to try and tease out the implications of using PFI for the scheme.

Attendees at the workshops included representatives from external financial and legal firms, a facilities management highways supplier, and construction companies as well as council staff. From these discussions developed an outline scheme which has now become a fully fledged PFI procurement.

Example 2: Dorset County Council – Colfox School

To try and gauge whether there would be any interest in a school scheme the Council, after doing a basic literature search, held a series of informal one-to-one discussions with a number of potential partners. The outcome of the discussions was to confirm that the scheme was possible and views from the private sector were taken into account when deciding on the details of the output specification.

Example 3: Glasgow City Council – secondary schools

To obtain a feel for whether a large-scale school rationalisation scheme would be possible, a general information-gathering exercise was followed by an ‘options workshop’, which was attended by people from a range of public and private sector organisations. A series of models was developed that showed possible structures and ways that the private sector could organise itself. A very high-level affordability exercise followed, and another workshop was held to evaluate the results. From this process the basic outline specification was developed.
Major decisions in a typical PFI scheme

At different stages in a PFI procurement, important decisions have to be made.

### Decision-making powers

**48.** At different stages in a typical PFI process major decisions will have to be made that commit the public body to a course of action, such as progressing to the next stage or incurring expenditure [EXHIBIT 8]. The legal powers of individuals to take the range of decisions likely to be required need to be considered at the outset. The first stage is to identify the type of decisions that are likely to be required, the people who should take such decisions and the legal power available.
49. It is for councillors and board members to decide, taking any advice deemed necessary, whether they have the legal powers to carry out their intentions and to do this by entering into a PFI scheme. Recent legislation in relation to both the NHS – NHS (Private Finance) Act 1997 – and local authorities – Local Government (Contracts) Act 1997 – has aimed to clarify the legal powers of these bodies. Within this statutory framework, the public body may need to review its own delegated decision-making arrangements, as set out in its standing orders or financial instructions, to make sure that the decisions it is expecting officers, working groups and subgroups to make are backed up by the necessary delegated powers. Where delegation is not deemed appropriate, arrangements will have to be made for councillors and board members to take decisions. It may also be necessary to convince the private sector that the decision-making arrangements are soundly based in legal terms.

50. As part of the PFI process, a timetable should identify and specify timescales for the decisions that councillors and board members are required to take. One option is to use the stages set out on page 23 [EXHIBIT 6] as a guide and then assess how the body’s formal delegation arrangements could cope with taking these decisions and what is the most appropriate forum – for example, full council or board or a subgroup or committee. The type of decisions that councillors and board members at different PFI schemes have been asked to take varies [CASE STUDY 5].

CASE STUDY 5: Decisions taken by members

Example 1: Isle of Wight Council – waste disposal scheme

For a waste disposal scheme the Council established a subcommittee of members from its main policy committee after taking the decision to proceed with a PFI procurement. The project management team of officers and advisers requested decisions from the subcommittee about:

- the output specification;
- the selection of a longlist, shortlist and preferred bidder; and
- the outcome of the negotiations with the preferred bidder and the decision to sign the PFI contract.

All the decisions of the subcommittee were reported in the normal way to the policy committee and then the Council.

Example 2: Carlisle Hospitals NHS Trust

For the replacement of the hospital, the Trust board was asked to decide on the:

- option appraisal and an outline business case;
- timetable for the scheme;
- output specification and design framework;
- selection of a longlist, shortlist and preferred bidder;
- full business case, including the contract terms; and
- decision to sign the contract.
Risks

51. The risk that the actual outcome of an event will be different from that either intended or planned is an everyday hazard. In the context of planning the events and the costs of a procurement process, it is perhaps not surprising that actual costs are often different from those planned. Since the survival of private sector organisations depends on minimising any adverse effects of unforeseen events on their profits, they have tended to have a better understanding than the public sector on how to deal with the concept of risk in a procurement process.

52. The first step for a public body is to identify the risks associated with a scheme that could cause the quality or costs of the service delivered to differ from those planned [EXHIBIT 9].

EXHIBIT 9
Examples of risks in a PFI scheme for a serviced building

There is a wide range of risks that have to be identified and costed in a PFI procurement; there can be several hundred risks that can all affect the cost and quality of service delivery.

 MAIN RISK

Planning  Design  Finance  Construction  Operating  Regulatory  Obsolescence  Supply

 SUB-RISK

Delays in completing design, design not fit for purpose
Impact of changes in interest rates and taxes
Costs over budget, time delays
Higher than expected maintenance, staffing and other running costs
Costs of meeting new statutory requirements
Outdated building or equipment and/or service delivery leading to higher costs

Essential public services cease to be available

Source: Audit Commission
53. Under a traditional procurement, the risk of increases in costs usually rests with the public body. One of the key features of PFI is the allocation of risks to the party best able to deal with them, thereby obtaining the required standard of service at the lowest cost. If a party that is not able to influence the outcome carries a risk, a higher charge is likely to be made to cover the increased uncertainty.

54. Having identified the risks inherent in a scheme, the public body has to consider the likelihood of these risks occurring, their probable financial effects and whether it wishes to seek to transfer the risks to the private sector. The negotiation process will determine whether risk transfer is achievable and the associated cost. The way in which a public body deals with the risks associated with a scheme is central to whether it obtains value for money from a PFI contract [CASE STUDY 6].

One of the key features of PFI is the allocation of risks to the party best able to deal with them...

### CASE STUDY 6: Stoke-on-Trent City Council's proposal to allocate risk

Risks are to be allocated between the Council and PFI supplier – the special purpose vehicle company (SPV) – for a scheme to refurbish and maintain the education estate.*

<table>
<thead>
<tr>
<th>Risk</th>
<th>City Council</th>
<th>Shared</th>
<th>SPV</th>
</tr>
</thead>
<tbody>
<tr>
<td>Detailed planning</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Health and safety</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Planning consent</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Design</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes required by legislation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes required by SPV</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes required by council</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes required by planning authority</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ground conditions</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Access to utility services</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Site conditions</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Construction</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost increases during design</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost increases during construction</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Health and safety compliance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Default by contractor</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Default by subcontractor</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Force majeure</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industrial action</td>
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<td></td>
<td></td>
</tr>
</tbody>
</table>
In its management paper, *Taking the Initiative*, the Audit Commission identified issues to help councillors, board members and chief officers take informed decisions about PFI procurement.

These questions have been drawn together in this pullout section to assist in the consideration of these issues, stimulate discussion in public bodies and to help identify priorities and who should take the lead in addressing them.
## QUESTIONS FOR COUNCILLORS AND BOARD MEMBERS

<table>
<thead>
<tr>
<th>Question</th>
<th>Yes/No</th>
<th>Priority/Lead Person</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Is there an understanding of PFI and how it differs from other forms of procurement?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Is the relationship clear between the planning process and the procurement options?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Is there an understanding of the concerns of the private sector?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Is there an understanding about the way that a PFI procurement can be used to tackle single service, cross-service and cross-organisation issues?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Is there an awareness of the main stages of a PFI procurement: option appraisal; scheme selection; output specification; European journal advert; longlist; shortlist; preferred bidder; contract negotiation, award and management?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Have the key stages for member involvement and decision been agreed?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Is there an effective framework in place to enable informed decisions to be taken?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8. Have the implications for staff and other stakeholders been communicated to them?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9. Are the financial implications understood of entering into a contractual commitment for many years ahead?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Question</td>
<td>Yes/No</td>
<td>Priority/Lead Person</td>
</tr>
<tr>
<td>-------------------------------------------------------------------------</td>
<td>--------</td>
<td>----------------------</td>
</tr>
<tr>
<td>10. Is there an understanding of how a decision to enter into a PFI contract will demonstrate that value for money in the use of resources will be achieved?</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**QUESTIONS FOR CHIEF OFFICERS**

1. Are there arrangements in place to keep up to date with PFI developments?  
2. Has the range of relationships likely to be involved in a PFI scheme been identified?  
3. Is there a process for planning how these relationships should be managed?  
4. Is PFI an integral part of the body's procurement policy?  
5. Is PFI suitable for single-service, cross-service or cross-organisation procurement?  
6. Are there arrangements in place to deal with the concerns of the private sector but that always maintain priority for the public body's interest?  
7. Are there rearrangements to demonstrate:  
   • affordability;  
   • the identification and costing of risk;  
   • value for money through competitive tension, use of public sector comparator, risk transfer, rates of return and non-financial factors; and  
   • cashflow effects?
<table>
<thead>
<tr>
<th>Question</th>
<th>Yes/No</th>
<th>Priority/Lead Person</th>
</tr>
</thead>
<tbody>
<tr>
<td>8. Is there a process for involving members?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9. For PFI schemes, are there processes in place to:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• set up project teams;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• examine the need for external advisers;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• control external advisers;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• develop ownership;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• provide leadership;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• set out the financial implications; and</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• confirm the vires of decisions?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10. Has the composition of the negotiating team been decided?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>11. Have the team's tactics been decided?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>12. Will the payment mechanism:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• reflect the actual risk transfer;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• ensure that payment reflects performance; and</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• in the case of a local authority, meet the contract structure test?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>13. Will future decisions take account of PFI commitments?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>14. Will PFI knowledge and experience be retained by the public body?</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### CASE STUDY 6 (com.)

<table>
<thead>
<tr>
<th>Risk</th>
<th>City Council</th>
<th>Shared</th>
<th>SPV</th>
</tr>
</thead>
<tbody>
<tr>
<td>Latent defects</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Claims from third parties</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Time delays</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Commissioning</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Failure of heating, electrical or water systems</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Facilities fit for purpose</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Time delays or cost overruns</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Operational</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Health and safety</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes required by council</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes required by SPV</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Higher than expected costs</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Failure to meet performance standards</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industrial action</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Numbers of pupils in a school</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### Notes:

1. The above allocation of risks represents a broad initial interpretation of the Council's position at the time of drafting the outline business case (OBC). As negotiations with bidders proceed, the details of each of their risk categories will be considered further.

2. The intention of the Council is to pass the responsibility for most of the risks associated with the provision of the service over to the SPV. The Council is seeking a degree of certainty about its expenditure levels, and to benefit from the private sector's expertise in managing risk, and to retain only those risks that cannot be influenced by the SPV.

*The Audit Commission neither endorses or criticises this particular risk allocation.*

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55. The contract management system must be able to monitor whether the financial impact of these risks is actually being met by the party that agreed to carry them. Where the public body agrees to retain or share a risk, it must make arrangements to minimise the likelihood of the risk having a financial impact.

### Value for money

56. Whether a PFI contract offers value for money in terms of service delivery will become apparent only once the service is being provided and the opportunity exists to compare costs and services with those of similar PFI contracts and those procured by other means. But every public body considering a PFI contract must be able to demonstrate that it has taken all reasonable steps to satisfy itself that the scheme offers value for money.

**Public bodies must be able to show that they have taken all reasonable steps to satisfy themselves that the scheme offers value for money.**
57. There are a range of factors that councillors and board members should normally consider before entering into a PFI contract [EXHIBIT 10].

58. Proper competition between bidders is important in producing the best possible offer from the private sector. The competitive process should extend from the respondents to the initial advert in the *Official Journal of the European Community*, through the receipt of initial expressions of interest, pre-qualification, return of invitations to tender, best and final offers and selection of preferred and reserve bidders. Unless the public body does its utmost to generate and maintain a competitive tension through the process, proving that any offer accepted is the best available will be extremely difficult.

EXHIBIT 10
Value-for-money issues to be considered before entering into a PFI contract

There are a number of issues that require careful consideration when assessing if a PFI scheme is likely to provide value for money.

*Source: Audit Commission*
59. What the private sector is willing to offer is only one element in the evaluation process. Another important aspect is what it would cost the public body itself to provide the services in question. This consideration involves producing a public sector comparator (PSC). The PSC should be prepared as soon as possible in the PFI process, and in any event should be completed by the time the invitation to tender is issued.

The main elements of a PSC are likely to be:
- the capital costs of construction;
- the cost of providing the specified services; and
- the cost of retaining the risks that would be transferred to the private sector under a PFI procurement.

The PSC should be prepared as soon as possible in the PFI process...
60. The cost of the risk that the public body would retain must be included in order to ensure a like-for-like comparison with the PFI bids, since bidders will be pricing in the cost of the risks that they are being asked to bear. It is therefore important to prepare an indication of risk allocation and send it to bidders as part of the tender documentation.

61. The costing of risk can be a complex process, sometimes involving hundreds of risks associated with any given scheme. The public body must estimate the financial impact and the probability of the underlying event occurring, and from this exercise create a risk register showing the costs of the risks to be included in the PSC [CASE STUDY 7]. There are also a number of statistical techniques that can test the robustness and sensitivity of the underlying estimates. While councillors and board members would not usually be involved in the detail of drawing up the PSC, they need to be able to understand and question the basis on which risks have been costed. PSCs can also help a body to make decisions about replacing and/or disposing of major assets [CASE STUDY 8, overleaf].

### CASE STUDY 7: Costing risks for a PSC for a large specialist education building

The institute occupies a city centre site, and wishes to enter into a PFI contract that involves the demolition of some existing buildings and the sale of the land, as well as the construction of new facilities and the refurbishment of others.

<table>
<thead>
<tr>
<th>Risks to be transferred under a PFI contract but retained under a traditional procurement</th>
<th>Cost £000</th>
<th>Probability %</th>
<th>PSC £000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Planning</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Failure to get planning permission by due date</td>
<td>200</td>
<td>10</td>
<td>20</td>
</tr>
<tr>
<td>Planners want changes to design</td>
<td>1,000</td>
<td>50</td>
<td>500</td>
</tr>
<tr>
<td>Town planning enquiry held</td>
<td>6,000</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Statutory approvals delayed</td>
<td>2,500</td>
<td>30</td>
<td>750</td>
</tr>
<tr>
<td>Planning gain required</td>
<td>200</td>
<td>80</td>
<td>160</td>
</tr>
<tr>
<td>Construction</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Archaeological finds</td>
<td>200</td>
<td>30</td>
<td>60</td>
</tr>
<tr>
<td>Asbestos found</td>
<td>100</td>
<td>20</td>
<td>20</td>
</tr>
<tr>
<td>Other contaminants found</td>
<td>50</td>
<td>30</td>
<td>15</td>
</tr>
<tr>
<td>Extra structural work on present buildings</td>
<td>100</td>
<td>15</td>
<td>15</td>
</tr>
<tr>
<td>Disputes with neighbours over noise and disruption</td>
<td>500</td>
<td>50</td>
<td>250</td>
</tr>
<tr>
<td>Design changes</td>
<td>4,000</td>
<td>10</td>
<td>400</td>
</tr>
</tbody>
</table>
**CASE STUDY 7 (cont.)**

<table>
<thead>
<tr>
<th>Risks to be transferred under a PFI contract but retained under a traditional procurement</th>
<th>Cost £000</th>
<th>Probability %</th>
<th>PSC £000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Financial</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Claims not covered by insurance</td>
<td>500</td>
<td>50</td>
<td>250</td>
</tr>
<tr>
<td>Construction industry inflation higher than estimated</td>
<td>8,000</td>
<td>50</td>
<td>4,000</td>
</tr>
<tr>
<td><strong>Property related</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Delay in selling vacant land</td>
<td>3,000</td>
<td>1</td>
<td>30</td>
</tr>
<tr>
<td>Delay in getting vacant possession</td>
<td>3,000</td>
<td>50</td>
<td>1500</td>
</tr>
</tbody>
</table>

Note: The source of the data on identifying the risks and then attaching costs and probabilities was a combination of the Institute's own financial systems and advice from external advisers.

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**The costing of risk can be a complex process...**

62. The base cost data for the capital and revenue elements should normally be available from the public body's own budgeting and costing systems. There may be instances, particularly regarding capital costs, where the public body has not built any similar assets in recent years. In such cases, guidance may be available from central government departments or from other public bodies that have built such assets more recently.
63. The choice of discount rate for the net present value (NPV) calculation is important. In the NHS, the Treasury indicates the discount rate to be used; in local government this advice is not mandatory. This is an important issue because a relatively small difference in the discount rate used can mean the difference between a PSC being either above or below that of a PFI bid. The decision about the discount rate chosen should be justified by officers and scrutinised by members.

64. The relative importance and weight to be given to non-quantifiable factors will depend on the individual scheme, but should not be overlooked. Where such factors have played a part in a decision, the reasoning followed by the decision-makers should be recorded carefully.
1. NPV is a term to show the total cost in today’s money of the income and expenditure streams over the future life of the contract.

2. The trust used the PSC to evaluate the preferred bid. Although a direct comparison of the figures was important, it was only one element in the procurement. The eventual decision was not taken solely on the basis of a spot comparison between the preferred bid and the PSC, but also took into account a range of other factors that the Trust deemed to be important. These included an assessment of the way in which the traditional procurement and the preferred bid dealt with:
   • safety and statutory requirements;
   • public confidence;
   • patient benefits;
   • improvement to the environment for patients and staff;
   • service supply; and
   • the management of the disruption during the development period.

65. The allocation of risks between the public body and the private sector will have a direct influence on whether the contract is likely to provide value for money. The public body should not accept risks that the private sector can manage more effectively as the latter will have the costs of its risks underwritten and its profits more assured. The allocation of risks will depend on the skill of the public body’s negotiating team, and will vary between schemes.

66. It follows that when evaluating a proposed deal, attention has to be given not only to the cost of the bid, but also to the underlying risk allocation. Perhaps as important is the effect of any changes in risk allocation during the negotiation stage. It is during this stage that the details of the scheme are finalised and agreement reached on sums to be paid, services to be received and the form of the contract.

67. Another indication of whether the proposed deal is likely to deliver value for money is the rate of return to the private sector, normally known as the ‘internal rate of return’ (IRR). The information needed to calculate the IRR should be available from the financial models provided by the bidders, and should normally be verified by the public body’s financial advisers. At one level the profitability of the PFI supplier, provided that it meets its obligations under the contract, is not of concern to the public sector body. However, it is worth having an indication as to whether the likely returns are excessive when compared to industry or economy norms.
68. Where, because of other financial constraints, a PFI procurement is the only way that a public body can procure the services that it wants, it may question whether a public sector company (PSC) should be created given that a publicly funded option is not available. However, a true value-for-money study requires comparison with all the options. If the cheaper option is not feasible, the decision-maker should be aware that a more expensive option has been selected.

**Affordability and financial awareness**

69. Affordability needs to be a constant theme throughout a PFI procurement, from the early stages of deciding on an appropriate procurement route [EXHIBIT 3, p18] through to the close of the deal and service provision. It is an issue that has to be revisited several times as the proposal becomes more detailed. The financial appraisal of any proposed scheme is important, but the scale of the commitments of large PFI schemes [EXHIBIT 4, p21], means that it is essential to have clear answers to some basic questions [EXHIBIT 11].
EXHIBIT 11
Key financial questions about PFI schemes’ affordability and viability

To help in assessing the affordability of a PFI scheme, a public body needs to consider some fairly basic questions.

70. The key issue of affordability must be considered at an early stage. Once the affordability constraint is established, it is likely to help to calculate (in fairly broad terms) what providing the desired service by a traditional procurement would cost the public body. Such a benchmark is sometimes called a ‘reference project’ and can be important in informing the discussions about whether it is worthwhile proceeding with a PFI option: if the costs of a traditional procurement are not patently beyond the body, PFI may be a realistic alternative. If a PFI procurement is then undertaken, the data gathered for the reference project may well be useful in the subsequent development of a PSC.

71. One of the features of PFI contracts is the long-term financial commitment by the public body to paying for the specified services. Not only is this commitment likely to limit the ability to switch resources in the future but, in the event of a need to cut spending, the PFI contract payment is likely to be protected from any cutbacks. The corollary is that non-PFI expenditure may have to carry proportionally deeper cuts.

Source: Audit Commission
72. The size of the liabilities accepted under a PFI contract may not be apparent to members or to the public. To overcome this risk, the details of the annual and the total commitment should be explained in a note to the annual financial statements that are approved by councillors and board members, and included in any summary made available to the public.

73. For many local authorities, the receipt of additional central government grant is essential if a scheme is to be affordable. The procedures for applying for such support are now well-established. At the moment, the receipt of the additional revenue support grant (RSG) is likely to be over a longer period than the PFI contract as the notional debt upon which the support is based is deemed to be repaid on a reducing balance basis. Also, once any allowance for inflation is made in the PFI payments and the associated RSG, there may be a mismatch between expenditure and receipt of RSG [CASE STUDY 9].

CASE STUDY 9: Stoke-on-Trent City Council – education estate scheme

The Council has embarked on a PFI procurement for the refurbishment and maintenance of almost all its education service buildings. The affordability of the scheme depends on financial support from central government. With the extra financial help the flow of funds to and from the city council for the scheme is likely to result in a mismatch between PFI payments and the receipt of associated RSG contribution to the capital element of the PFI charge (see below).
The implications are that:

- for the first ten years of the PFI scheme the council will receive more RSG than it pays out in PFI fees;
- for the next 20 years the situation is reversed, with the PFI fees being progressively higher than the RSG; and
- RSG, albeit on a reducing basis, will continue to be received for many years after the PFI contract has ended.

The Council has to be able to calculate the scale of the mismatch in the funding and take this into account when planning its finances, particularly its cash flow management. In addition, controls must be put in place to ensure that in the ten years of RSG 'surplus' other decisions are not taken that commit these resources in the mistaken belief that they are not already committed.

**Payment mechanism and contract management**

74. An integral part of a PFI agreement is the payments structure, and the management of the relationship between the public body and the private sector. The public body makes no payments until the specified service is received. The payment mechanisms being devised for PFI contracts link payments to availability of service, performance against predetermined standards and, in some cases, the level of usage or demand for the service [CASE STUDY 10, overleaf]. It is important to design a contract monitoring system that is simple enough to operate in a busy working environment, yet is capable of ensuring that significant financial penalties are imposed for substandard service.

75. To ensure that there is effective commercial pressure upon the PFI supplier to meet the required standards, the conditions set out in the contract must be tough but reasonable, and the deductions arising must be significant enough to prompt corrective action. In order to satisfy the current capital finance regulations, a local authority PFI scheme must have at least 20 per cent of the annual PFI payment demonstrably variable according to performance. This is known as the 'contract structure test'. There should always be the option of the contract being terminated, or of the financiers exercising step-in rights, on the grounds of persistent poor performance.

76. The performance monitoring and reporting procedures also need to form part of the contract. During the construction stage, there should be regular contact between the public body and the supplier to ensure that progress is according to plan. The project manager would normally be the main point of contact, and any reshaping of the existing organisation and arrangements for transferring staff and other assets would take effect as the new asset is completed.
Example 1: Dorset County Council – Colfox School
The Council negotiated a payment mechanism for the PFI contract based on elements of availability and performance.

Availability
The school is divided into zones according to the type of space – for example, classroom, hall and toilets – and each zone is given a weighting according to its importance to the school. The basic availability criterion is that no room or space shall be unavailable for more than a set number of days in any academic year. Each zone has a schedule of requirements that forms part of the service level agreement with the PFI supplier. Unavailability will be reported to the County Council in a regular facility management report, and will result in a deduction from the contract payment.

Performance
A series of performance standards for the required service covers all aspects of the building fabric and facilities management. Deductions from the contract payment will be made if the service falls short of either standards or the response times for remedial work.

In the event of successive failures to meet the required standards, a weighting is applied to the resultant deductions from payments that increases the penalty for continuing poor service. The option to terminate the contract is based on the number of penalty points accumulated.

The risk of changes in pupil numbers rests with the County Council, although the contract permits the Council to alter the accommodation requirements with resultant changes to the contract payment. The PFI supplier carries the risk of changes in the demand for school meals.

Example 2: Dartford and Gravesham NHS Trust – replacement hospital
The Trust agreed a PFI contract for the provision of a serviced hospital that included the following payment mechanism:

- the PFI supplier will provide estates and maintenance, portering, security, transport, catering, linen and laundry, domestics, window cleaning and pest control. For each service there is a service level agreement (SLA) backed up by a procedure manual that set out the quality of the services to be supplied;
- deductions will be made if a service fails to meet the agreed standards of performance, with a trigger point at 70 per cent, below which termination warnings and notices can be issued. If demand for services such as catering, linen and laundry, and waste disposal falls, then the performance-related payment will be reduced by amounts based on the unit cost of the service; and
- if an authorised member of staff declares any part of the hospital unavailable, then a schedule of penalty payments is applied.
77. The systems needed for ongoing monitoring will vary between schemes, but will essentially involve arrangements for staff of the public body receiving the services – such as teachers, medical and nursing staff – to report problems to a monitoring officer. This reporting structure will need to be supplemented by mechanisms to monitor aspects of performance such as cyclical maintenance, the performance of which would not immediately be evident to staff such as teachers. Methods of assessing the performance of a PFI supplier will differ depending on the nature of both the public body and the service being delivered [CASE STUDY 11].

78. The PFI supplier and the public body should share information about performance in order to minimise the data collection burden. For the purpose of monitoring and audit, there should also be a policy of open book accounting between the two sides.

**CASE STUDY 11: Assessing the performance of a PFI supplier**

**Example 1:** Dorset County Council’s PFI contract for the Colfox School scheme requires that representatives of the Council and the school review on a monthly basis the standard of the different services being received that relate to the following areas.

<table>
<thead>
<tr>
<th>Management</th>
<th>IT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Administration</td>
<td>Emergency resources</td>
</tr>
<tr>
<td>Cleaning</td>
<td>Provider's staff</td>
</tr>
<tr>
<td>Building maintenance</td>
<td>Security</td>
</tr>
<tr>
<td>Grounds maintenance</td>
<td>Health and safety</td>
</tr>
<tr>
<td>Catering</td>
<td>Energy and utilities</td>
</tr>
<tr>
<td>Caretaking</td>
<td>User satisfaction</td>
</tr>
<tr>
<td>Waste disposal</td>
<td>Quality</td>
</tr>
</tbody>
</table>

**Example 2:** Dartford and Gravesham NHS Trust will monitor the performance of each service (see Case Study 10) across the whole hospital in relation to the standards set out in the SLAs. Each month the Trust and supplier score each service and the outcome will affect 60 per cent of the expected monthly charge.

Each month there will also be a very detailed scrutiny of the performance of a service provided to a department chosen at random. The outcome will affect 40 per cent of the expected monthly charge.
The contract management process also needs to include arrangements for changing the way that services are delivered, both in terms of quantity and quality. It may also permit the benchmarking or periodic market-testing of specific services to see whether there should be any changes to the charges under the contract. Such procedures are particularly important in the context of long-term contracts, because they provide a degree of flexibility to cope with changing circumstances and introduce an element of responsiveness into what could otherwise be very rigid agreements [CASE STUDY 12].

The contract management process also needs to include arrangements for changing the way that services are delivered...

CASE STUDY 12: An NHS trust – change mechanism

The contract for a new district general hospital includes a timetable for the benchmarking and market-testing of the support services (such as catering, cleaning and maintenance). While any subsequent reduction in the cost of these services is passed on to the trust, any increases have to be met by the supplier.

The contract also specifies the notification period and decision-making procedures that both sides have to adhere to should they wish to change the level or nature of the facilities or services to be provided.

Project team

80. At the centre of a PFI procurement is the project team. One of the lessons from the early PFI schemes in the NHS and local government is the crucial role played by the project team leader. This individual would normally be a senior officer of the public body, but in smaller organisations the service can be bought in from outside. The remit for the project team leader is to manage the PFI procurement process through to a successful conclusion on time and within the resources available for the task and should be specified in terms of detailed responsibilities [CASE STUDY 13]. Councillors or board members will not always expect to be involved in the appointment of the project manager, but given the critical nature of the role they should at least satisfy themselves that the role and skills required have been properly defined.
CASE STUDY 13: Carlisle Hospitals NHS Trust – replacement hospital project

The overriding responsibility of the project team leader is to manage the PFI process through to a successful conclusion. This task involves:

- setting a timetable for the scheme;
- producing the project brief and plan;
- being the first point of contact for private sector and other outside bodies;
- appointing by competition and then managing the external advisers;
- ensuring that adequate communications exist between the project team and the rest of the Trust and between the team and external bodies;
- maintaining an overview of the scheme and monitoring progress against the timetable;
- ensuring that all work is planned and that resources are made available;
- providing regular reports to the Trust chief executive and board;
- reaching agreement with the private sector for the provision of a new hospital on a cost-effective basis and presenting this to the board;
- establishing performance monitoring systems and payment mechanisms that protect the Trust's interests, and presenting these to the board; and
- arranging a post-completion evaluation of the scheme.

At the centre of a PFI procurement plan is the project team.

81. Having determined the role of the project team leader, the next stage is to decide on the membership of the team. Again, this may not directly involve councillors or board members, but they should review and endorse (or otherwise) the approach proposed.

82. From the public body's view, care should be taken not to assume too readily that only external advisers can provide the skills needed for the PFI procurement process. The procurement will be time-consuming and complex, but the public sector often has many of the necessary skills available. External advisers can be expensive and should be used only in those areas where the organisation has identified a real gap in its own skills that cannot be bridged by staff training, use of free advice from organisations such as the 4Ps or departmental private finance units.

There will normally be three stages in appointing the project team:

- deciding upon the skills that are likely to be required;
- establishing whether these skills are available within the organisation and can be directed to the PFI scheme; and
- making arrangements to obtain these skills, either by making in-house staff available or buying in services from outside.
83. The range of skills required in project teams will depend on the nature of the scheme [CASE STUDY 14]. Again, this is not a once-and-for-all decision, and councillors and board members should satisfy themselves that the skill mix is right for each stage of the project.

84. Once the composition and mix between the internal and external advisers has been decided, the likely budget for the team should be prepared and submitted for approval in the normal way. One aspect that councillors and board members should ask to be included is the cost of the directly employed staff; while not wishing to create a cumbersome bureaucracy, officers should be required to keep basic records of the time spent on the scheme, to establish a reasonably accurate figure for the actual costs.

External advisers

85. Having established the need for external advisers, arrangements have to be made to procure these services. As with the purchase of any services, what is required must be specified as precisely as possible. The services available range from total scheme management and specialist legal and financial advice, through to support during the negotiations with the preferred bidder and technical advice on narrow aspects of a scheme. No matter what type of external advice is sought, the management and control of the scheme must always rest firmly with the public body.

CASE STUDY 14: Membership of PFI project teams

Example 1: Dorset County Council Colfox School scheme

The Council put together a team comprising the headteacher and staff from finance, education, building services, valuers, legal and other council departments (such as contract services) as and when the need arose. In addition, external support was bought in to provide specialist financial and legal advice, and use was made of free guidance from central government and the 4Ps.

Example 2: Carlisle Hospitals NHS Trust hospital replacement scheme

The Trust created a project board which was chaired by the chief executive and included the directors of medical services, site services, nursing, finance, human resources and clinical representatives. In addition, external support was bought in for financial and legal advice.

Example 3: Essex County Council’s new strategic road scheme

The Council set up a team of officers from the highways, legal and finance departments, supplemented by external financial, technical and legal advisers.
86. The usual way to appoint external advisers is by competition, and there must be very good reasons for the appointments to be made in any other way. This does not automatically mean that the cheapest should always be appointed, since other factors such as experience and specialist knowledge should be taken into account. The basis for both appointing and remunerating external advisers will vary according to the nature of the task being required [CASE STUDY 15].

87. Public bodies need to consider how they will evaluate the performance of advisers. Delivering a signed contract is a clear measure of success but will be achieved only after several preliminary stages have happened and many months have elapsed. Advisers' fees will be paid throughout the process and the appraisal of their performance must also be continuous. One way is to break the stages down into a series of tasks and, where feasible, to set clear timescales for completion. Assessments can then be made against these targets. There has to be both a willingness and the ability to question the advisers' views throughout to ensure that the interests of the body are paramount.

CASE STUDY 15: Appointment and remuneration of external advisers

Example 1: Staffordshire County Council – Sir Graham Balfour School
The Council invited six firms with experience of acting for public sector bodies on PFI schemes to submit tenders for the role of financial advisers. A range of criteria was used to assess the bids, including:
- the extent of experience on school schemes;
- knowledge of the private sector, including financiers;
- the degree to which the bid was structured to this particular scheme;
- the impression made by the team in its presentation and subsequent discussion; and
- references from other clients.

The fee structure was a day rate for the whole process, but was broken down into the main stages. Payment was linked to satisfactory progress. A cap on fees at each stage was also negotiated.

Example 2: Essex County Council – road scheme
Financial and legal advisers were appointed by competition. The financial adviser's fees are on a stage basis; any underspend against budget on one stage is carried over to the next, should it be required, within an overall limit. The legal adviser's fees are based on a daily rate.

Example 3: Glasgow City Council – secondary schools
For a large-scale school rationalisation scheme, financial advisers were appointed for a detailed feasibility study by competition on a fixed-fee basis.
Ownership

88. The importance of managing a series of relationships has already been referred to as central to a successful PFI procurement. Alongside this requirement is the need for the public sector body to be able to demonstrate a clear sense of ownership of the process to other parties involved. Potential partners need to act in good faith and have a degree of trust in one another.

89. Who needs to show ownership depends on the nature of the scheme. In the case of a school scheme, for example, a vital group will be the school governors, and local education authorities may need to invest time in explaining and exploring the implications of PFI with the school governing body. In some school schemes, the chair of the governors becomes an effective spokesperson and driving force behind the PFI scheme. Without the full support of key stakeholders it might be necessary to conduct a detailed appraisal of whether it is worthwhile proceeding with the scheme before any further expenses are incurred. A disunited governing body can easily cause concern among potential private sector partners and quickly lead to disillusionment with the PFI process. Private sector partners will certainly look for evidence of unity of purpose.

90. In a local authority context, councillors have to be prepared to show their commitment to a scheme, and a willingness to tackle problems that the PFI process may uncover. Such a sense of ownership and purpose can be demonstrated by a knowledge of PFI, formal adoption by the council or committee of the PFI process for a scheme and by membership of steering groups that have been set up to oversee a scheme.

91. In an NHS trust it is essential that the board is supportive of the PFI process, and in particular that the medical staff and trade unions are in agreement with the main aim of the PFI policy. The support of the main purchasers of healthcare is essential. Again, time and resources invested in seeking the views of key stakeholders and trying to secure their agreement will allow the trust to present a unified front to potential partners.
The key individuals involved will also have to demonstrate their commitment on behalf of their organisation [EXHIBIT 12]. One way of doing this is to take a lead in explaining the potential benefits of a scheme to all the communities affected by it [CASE STUDY 16].

CASE STUDY 16: Ownership of PFI schemes

Cardinal Heenan (Voluntary Aided) Roman Catholic High School, Leeds

The headteacher and the chairman of the governors instigated a series of interviews with local newspapers and radio to publicise the school’s intention to try and use the PFI to obtain a replacement school. As the scheme progressed through its various stages, more cultivation of the media reminded the community of the steps being taken.

EXHIBIT 12

Steps to demonstrate ownership of and commitment to a PFI scheme

Unity of purpose and the willingness to demonstrate a real commitment to a PFI scheme will be one of the features that the private sector will seek.

/formal resolution by:
• council or committee
• board
• school governors

/willingness to:
• meet potential bidders
• chair/speak at open days for bidders
• be a spokesperson to the media
• drive the process along

Source: Audit Commission
Leadership

93. For any major project that involves changing people's way of working, leadership and vision are required to make it a success. Experience shows that either a single person or a small number of people should be given responsibility for driving the PFI procurement and engaging key stakeholders. For some schemes, this role may be carried out by a councillor or board member, in others by an officer, and there might also be instances where it is carried out by more than one person. The aim should be to create a focal point for the PFI scheme in the organisation [EXHIBIT 13].

EXHIBIT 13
Personal characteristics for the leadership role in a PFI procurement

A demonstration of strong leadership by the public body is important in a PFI procurement.

Source: Audit Commission
94. The role of PFI leader may be combined with that of the project manager responsible for the day-to-day administration of the procurement process, but it does not have to be. In some schemes, the two roles are quite distinct and responsibilities are allocated accordingly. The main point is not who does what, but to recognise the importance of the leadership function, think through the demands of the task, allocate responsibility clearly and discuss openly any overlap with other roles. The demands upon chief officers and senior staff are likely to be significant, and arrangements may have to be made to ensure that other aspects of these individuals' work does not suffer.

Communications

95. The critical role of managing relationships was referred to in Section 1. In order to do this successfully, it is important to keep people informed about the progress of a scheme. There are likely to be a number of different 'audiences' that need to be kept informed [EXHIBIT 3, p18]. These can be divided broadly into those inside and those outside the organisation. Internally, the largest group and the one with the greatest concerns will be the staff whose employment may be affected directly by the PFI scheme and public bodies need to approach this issue carefully [CASE STUDY 17].

96. Externally, service users and the wider community can be targeted – in the case of a school scheme, for example, by a combination of newsletters to parents and direct briefing of the local media [CASE STUDY 18, overleaf]. Use can also be made of displays and exhibitions in hospitals and libraries and, where appropriate, these can also be moved between locations within the area.

CASE STUDY 17: Carlisle Hospitals NHS Trust – replacement hospital

Keeping staff informed

The Trust had over 300 staff who were likely to be subject to compulsory transfer to the successful bidder. The board stressed the importance of telling staff as much as possible as the scheme progressed.

Staff briefings on a cascade basis were held at least monthly, and more frequently when necessary. These briefings were backed up by more detailed discussions with staff and trades unions to discuss employment-related issues directly.

A newsletter was sent to all staff, initially quarterly, but in the latter stages on a monthly basis.
CASE STUDY 18: Dorset County Council – Colfox School

The following were consulted about the provision of the Colfox school scheme.
• Local MPs
• DfEE, DoE and Treasury
• Members of the Council
• School governors
• School staff
• Parents
• Other local schools
• Trades unions
• 4Ps
• External auditor

97. Effective communication with the private sector is essential. While there are the statutory requirements to advertise in the Official Journal of the European Community for schemes above a certain threshold, and established procedures for responding to requests for information from potential suppliers, there is scope for public bodies to be more proactive within the basic statutory framework. The intention is to show potential suppliers that the scheme has been prepared properly, and to demonstrate that a professional approach is being taken to the procurement process [EXHIBIT 14].

There are likely to be a number of different 'audiences' that need to be kept informed.

98. Both NHS and local government bodies involved in early schemes insisted on communicating with the financiers behind the bidder in order to try and reduce any delays arising from the review of the scheme by the financiers. The financiers' detailed review is often known as the 'due diligence process'. Financiers may well be new to the public sector and uncertain about its legal powers and decision-making processes. A high degree of caution may be fuelled by past legal decisions involving public bodies where banks suffered large losses. It is in the interests of all parties that schemes are not unduly delayed because of concerns about very basic issues; public bodies may be able to avoid this by insisting upon direct contact with financiers at an appropriate stage and making this a requirement during the negotiation process.
Direct communication with financiers is also important because an agreement between the public body and financiers – as well as that with the private sector suppliers – is a feature of most completed PFI contracts. It is important to establish rights and duties upon both sides about action to be taken and expenditure to be incurred should either the public body or the supplier default on the contract. The details of these 'step-in' and 'step-out' rights will be decided when the final contract is being negotiated. The public body should use the negotiation process to set up arrangements to ensure that services to the community are maintained should the initial contract break down, and early communications can help to identify potential problems.

It is important to establish rights and duties upon both sides...

EXHIBIT 14

Personal characteristics for the leadership role in a PFI procurement

A demonstration of strong leadership by the public body is important in a PFI procurement.

Source: Audit Commission
100. The Audit Commission has issued advice to external auditors about their responsibilities in relation to PFI procurements. It is important that public bodies keep their external auditor informed about PFI schemes. Auditors must maintain an independent position and not become part of the body's decision-making process. Within this constraint, auditors will seek to be as helpful as possible to public bodies. The Audit Commission has produced a number of technical releases (T/Rs) about different aspects of PFI for external auditors. These are also available to public bodies and cover the following:

- TR 24/96  
  Audit Approach to PFI schemes in the NHS;

- TR 36/96  
  Local Government PFI;

- TR 2/97  
  PFI: Provision of Accounting View;

- TR 15/97  
  Audit Approach to PFI in Local Government; and

- TR 40/97  
  HMT Interim Guidance on the Application of FRS5 to Accounting for PFI transactions.

It is important that public bodies keep their external auditor informed about PFI schemes.
QUESTIONS

- Are there arrangements in place to keep up to date with PFI developments?
- Is there an awareness of the main stages of a PFI procurement:
  - option appraisal;
  - scheme selection;
  - output specification;
  - European journal advert;
  - longlist;
  - shortlist;
  - preferred bidders; and
  - contract negotiation, award and management?
- Is there a process for involving members?
- Are there arrangements to demonstrate:
  - value for money through competitive tension, use of a public sector comparator, risk transfer, rates of return and non-financial factors;
  - affordability;
  - the identification and costing of risk; and
  - cashflow effect?
- Are there processes in place to:
  - set up project teams;
  - examine the need for external advisers;
  - control external advisers;
  - develop ownership;
  - provide leadership;
  - set out the financial implications; and
  - confirm the vires of decisions?
- Has the composition of the negotiating team been decided?
- Have the team's tactics been decided?
- Have the implications for staff and other stakeholders been identified and communicated to them?
- Will the payment mechanism:
  - reflect the actual risk transfer;
  - ensure that payment reflects performance; and
  - in the case of a local authority, meet the contract structure test?
- Will future decisions take account of PFI commitments?
- Will PFI knowledge and experience be retained by the public body?
5. Conclusions for councillors and board members

101. The responsibility upon members of public bodies (councillors in local authorities and both executive and non-executive members of NHS bodies) in undertaking a large PFI scheme is significant and at times onerous. The decisions that they take directly affect the quality of life of the local population, and can often involve large sums of public money. While members will, quite rightly, rely upon the advice and guidance of officers, the eventual decision will be one that they have to make and take responsibility for.

102. This paper has highlighted a range of issues about a control framework. Members need to be aware of all the issues covered in this paper, but will not necessarily have detailed involvement throughout. But issues that they should always consider in detail are:

- the basic features of a PFI procurement and the potential advantages and disadvantages for the public body. In particular, they need to understand that PFI is not a 'free option', but rather spreads costs over several years ahead;
- how PFI relates to the existing planning process and ensure that it should always follow, never drive, the way that planning is undertaken. PFI is a procurement tool only, not a planning tool;
- the key decision points in the PFI procurement process. As a minimum, members should make the decision to:
  - agree the business case;
  - pursue procurement by the PFI route;
  - engage external advisers;
  - issue information to respondents to formal advert;
  - select longlist from respondents;
  - select, after evaluation, a shortlist from the longlist;
  - issue 'invitation to tender' document to shortlist;
  - select the preferred bidder after evaluation from the shortlist; and
  - enter into agreement, after negotiations, for the provision of services, monitoring procedures, payment mechanisms, penalty clauses and step-in and step-out rights.
- the key stages for receiving reports; and
- the nature of the financial commitment of a PFI contract and the implication for future financial and policy planning. In particular, once entered into, a PFI contract can restrict future flexibility over services and discretion to redirect resources to other areas.
103. The above is the minimum requirement; members may wish to get involved in more detail depending upon their own interests and the extent to which they carry special responsibility for a scheme. It is also generally the case that members at NHS bodies, because of the size of major schemes, are more likely to become involved in more detail than their local authority counterparts. Nevertheless, it is important that those taking decisions about PFI schemes in all public bodies understand properly the issues involved.

104. The PFI has given public bodies an alternative way of meeting the needs of their communities. But PFI may not always be the best option and is certainly not an easy option. Those responsible for taking decisions need to do so with a clear appreciation of the consequences of their actions. The control framework outlined in this paper should help them to tackle this challenge.
Appendix 1: Members of the advisory group

David Cain  
Deloitte and Touche

Jeremy Colman  
National Audit Office

Peter Fanning  
Public Private Partnerships Programme Ltd

Derek Howell  
Leeds City Council

Sir Peter Kemp  
Audit Commissioner

Paul Kent  
Dorset County Council

Ben Prynn  
HM Treasury

David Revel  
NHS Executive

Malcolm Stamp  
Norfolk and Norwich NHS Trust

Tim Watkinson  
District Audit
The Audit Commission has produced a number of studies covering issues related to strategy and management in local government and the NHS. The following may be of interest to readers of this paper:

**Promising Beginnings**  
A Compendium of Initiatives to Improve Joint Working in Local Government
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Compendium, 1998, 80 pages, 1862401187, £25

**A Stitch in Time**  
Facing the Challenge of the Year 2000 Date Change
---

**Worth More Than Money**  
The Role of the Local Government Finance Director
---
Management Paper, 1998, 36 pages, 186240058X, £10

**A Learning Experience**  
Service Delivery Planning in Local Government
---
Occasional Paper, 1997, 28 pages, 1862400288, £10

**Kiwi Experience**  
VFM Messages from New Zealand
---
Occasional Paper, 1997, 36 pages, 186240013X, £8

**Representing the People**  
The Role of Councillors
---
Management Paper, 1997, 46 pages, 1862400113, £7

**Form follows Function**  
Changing Management Structures in the NHS and Local Government
---
Management Paper, 1996, 40 pages, 1862400008, £6.50

**Called to Account**  
The Role of Audit Committees in Local Government
---
Management Paper, 1996, 28 pages, 0118864505, £6

**Improving Value for Money in Local Government**  
A Compendium of Good Practice from Audit Commission Reports
---
Compendium, 1995, 62 pages, 0118864114, £8

**Taken on Board**  
Corporate Governance in the NHS: Developing the Role of Non-executive Directors
---
Management Paper, 1995, 29 pages, 0118864408, £6

**Less Dangerous Liaisons**  
Early Considerations for Making Mergers Work
---
Management Paper, 1995, 26 pages, 0118864033, £6

**Protecting the Public Purse 2**  
Ensuring Probity in the NHS
---
National Report, 1994, 76 pages, 0118864668, £10

**Protecting the Public Purse – Probity in the NHS**  
Combating Fraud and Corruption in Local Government
---
National Report, 1993, 40 pages, 0118861210, £9

**Protecting the Public Purse**  
Ensuring Probity in Local Government
---
Update Papers
Bulletin, 1997, 24 pages, 1862400571, £10
Bulletin, 1996, 20 pages, 1862400032, £6
Bulletin, 1995, 26 pages, 0118864289, £6
Bulletin, 1994, 46 pages, 0118861271, £5

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To order Audit Commission publications, please telephone 0800 502030, or write to Bookpoint Ltd, 39 Milton Park, Abingdon, Oxon OX14 4TD
Public services have traditionally been financed by either central or local taxes. The Private Finance Initiative (PFI) scheme offers a way to bring private sector money and skills into the provision of public services.

But the decision to enter into a PFI contract can commit a public body to paying out millions of pounds for decades ahead. Given the typically long-term consequences of PFI deals, it is therefore vital that those responsible for taking such decisions operate within a framework that provides them with the information that they need to demonstrate the proper stewardship of public funds.

The Audit Commission has written this paper to help local authority councillors, board members at NHS bodies and chief officers to identify the issues that should be addressed both when considering the PFI route and, once this option has been chosen, to ensure the proper control of the PFI procurement process.