

Grant Thornton and the National Audit Office (NAO) Private Finance Initiative (PFI)

Private Finance Initiative (PFI) expiry roundtable discussion

Grant Thornton hosted a virtual roundtable event on the 21 January 2021 to discuss key issues in relation to the large number of PFI expiries due to occur over the next 5-10 years. This was as an important opportunity to share knowledge in this space, across a range of stakeholders. We were fortunate to draw on a breadth of skills and perspectives on the topic, with speakers including the NAO, a former Public Private Partnership (PPP)/PFI lawyer now focused on contract workflow software, a PFI operator, a PFI funder as well as Grant Thornton experts.

There were also a broad range of attendees, covering Local Government (providing insights on schools, housing, waste and transport PFIs), Health, Central Government including Justice, a mix of Grant Thornton audit and advisory clients and experts in the area covering contract management, commercial, legal and financial expertise.

NAO introduction and comments:

Colleagues from the National Audit Office provided an insight into the high-level themes from their report 'Managing PFI assets and services as contracts end'. The discussion was framed around the following four headings;

- Understanding the contract
- Knowing the asset
- · Skills and capabilities
- Tools and relationships

Following scene setting of the four components above, the roundtable explored three questions as set out below with key observations noted.

Question 1

Based on the experience of your PFI, which areas do you feel could be improved to drive better value for money:

- Strong contract management team in-house; one authority
 noted the use of an experienced solicitor managing the contract
 team and that this enabled them to challenge contractors on
 contract management issues to drive better outcomes.
- Collaboration with contractors; making changes to arrangements can be expensive – eg in a schools contract to add an extension proved to be very costly with legal fees, mark ups etc.
- Having in-house experience and knowledge of the contracts is key; often people have moved on within the public sector and loss of corporate memory makes it difficult to retain knowledge and experience of contract. At smaller Councils with fewer PFIs this can be challenging and they may be more reliant on external consultants.
- Knowledge sharing; We see instances of the same contract
 working successfully in one place, but unsuccessfully
 elsewhere. Good practice and working habits need to be
 shared, including what does not work well. There are some
 large investors with a lot of projects who can share knowledge
 to enhance value for money across the piece.
- Sensible approach to lifecycle and the size of the lifecycle pot; potentially better options exist on the treatment of the lifecycle pot and how these funds could be used.
- Lenders are looking to become more involved; Lenders have a role to play in policing the lifecycle, the distribution of surpluses and the behaviours of the parties.
- Good stakeholder management; an example was noted that a periodic (monthly, quarterly, annual) event attended by all parties can be very helpful in supporting a collaborative approach.

Ouestion 2

What preparations do you believe need to be considered for expiry and handback?

- Changing requirements of assets and in the sector should be at the forefront – eg changing schooling requirements, changing requirements in terms of waste and recycling and recognising where operations need to be adapted to respond to the needs of the end user.
- Adherence to Treasury Code of Conduct to be promoted further to encourage collaborative behaviour.
- Resource is required, including to allow for regular interaction with not just the SPV, but also service users, FM sub-contractors, parent company investors, debt funders, sponsoring departments, etc.
- Procurement if you want to run a procurement competition on expiry, this needs to be started well in advance. This can present challenges in terms of access to data from the contracts to help shape future requirements. The best approaches here have been collaboration and transparency, explaining the reasons for the data requirements and the benefit in providing to the timelines and the completion of arrangements post-expiry.

Ouestion 3

What does success look like for your service post - PFI and what types of arrangement do you believe will be suitable?

- Important to prepare a business case. Organisations should consider HM Treasury better business case approach and associated training, alongside certified PPP professional training developed by the World Bank Group and others, to build capability.
- Simplistically, the PFI brings together design, build, finance, operate and maintain. Some of those, only the private sector can deliver, hence the need for a follow-on procurement competition.
- Expectation that arrangements post-PFI will be cheaper.
 However, this is too simplistic, some may be more expensive.
 Early development of the business case allows all to
 participate in stakeholder conversations on the post PFI
 arrangements/costs.
- The comparative cost of follow-on arrangements does depend on how the deal was structured (eg equity vs debt profile).
- Discussed the need to properly examine what sort of expiry options may work in the future - shorter term contractual arrangements for greater flexibility?
- Public sector could enhance understanding of how private sector will price risk. Different scenario of risk transfer on exit. Opportunity to do something different which may drive savings but recognising this may be limited.

- With most Local Authorities having declared climate emergencies, targeting Net Zero in the 2030s and wider Government targeting 2050, work is needed on energy efficiency, including building retrofit. There are good 'win:win' opportunities here for PFIs and it would demonstrate how the public body and private sector supply chain might work collaboratively.
- Importantly, getting all parties round the table to discuss direction is important. Aligning the strategic view and sharing of joint risk registers can be a strong means of facilitating this, providing the opportunity to have an open dialogue.

From the questions and conversations, the group noted the following key themes and messages to take forward:

- Successful preparation for a smooth and effective PFI expiry relies upon transparent relationships and access to information to make informed decisions.
- Commencing preparation early for PFI exit is critical the NAO reflect the Infrastructure and Project Authority's recommend that preparations commence 7 years out from expiry.
- Many of the expiry and post-PFI options can be used to incentivise behaviour across the private sector partner supply chain and with the public bodies.
- Sharing best practice tools and experience to build in-house experience is important for public bodies to maximise their value from the PFI contract.
- The condition of the asset and handback provisions in the PFI contracts are often unclear from the contract. Attendees noted that it would be beneficial to have a standardised approach to condition surveys, as all parties can lose significant time in disputes over the condition of an asset at handback. Confronting any ambiguity over these clauses at an early stage may help prevent costly disputes.
- Requirements from PFI are now very different from 25
 years ago; PFIs need to be flexible when making changes to
 contracts. Waste PFI contracts were highlighted as an area
 this has been issue, with increased recycling rates over the
 past 20-25 years.
- Going forward, delivery of assets and services may be better supported through a suite of agreements with greater flexibility, different terms, and the ability to take advantage of developments around digital innovation in various aspects of PFI reviews, asset maintenance and operational monitoring of agreement.
- The expected use of assets could have changed over the last 12 months office space, to be re-considered.
- There is the opportunity to provide input on PFI Select Committee consultation – potentially commenting on the capacity and capabilities needed in public services for PFI expiry delivery.

Next steps

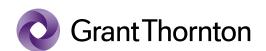
Grant Thornton has a well-developed PFI contract management, amendment, operational efficiency, expiry and follow-on approach. Please contact **Mark Williams** or **Wayne Butcher** if you would like to discuss this topic further, or have any questions or comments about this event.



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