

11 THE PRIVATE FINANCE INITIATIVE

- 11.1 The Private Finance Initiative (PFI) was initiated by the government in the early 1990s, and is an approach to funding construction that you should be aware of as a governor, even if it has not yet been used in your HEI. It constitutes part of the Public Private Partnership initiative described by the Treasury in the following terms:

"Public private partnerships (PPPs) are arrangements typified by joint working between the public and private sectors. In the broadest sense, PPPs can cover all types of collaboration across the interface between the public and private sectors to deliver policies, services and infrastructure. Where delivery of public services involves private sector investment in infrastructure, the most common form of PPP is the Private Finance Initiative.

"The Private Finance Initiative (PFI) is a small but important part of the government's strategy for delivering high quality public services. In assessing where PFI is appropriate, the government's approach is based on its commitment to efficiency, equity and accountability and on the Prime Minister's principles of public sector reform. PFI is only used where it can meet these requirements and deliver clear value for money without sacrificing the terms and conditions of staff.

"Where these conditions are met, PFI delivers a number of important benefits. By requiring the private sector to put its own capital at risk and to deliver clear levels of service to the public over the long term, PFI helps to deliver high quality public services and ensure that public assets are delivered on time and to budget"³⁹.

- 11.2 This description of the PFI was usefully provided by David Batty and Matt Weaver in the Guardian:

"Private consortiums, usually involving large construction firms, raise the capital finance to design and build a public sector project. They are also contracted to maintain the buildings while a public authority, such as a council or NHS trust, uses them. This means the private sector is responsible for providing cleaning, catering and security services. Once construction is complete, the public authority begins to pay back the private consortium for the cost of the buildings and their maintenance, plus interest. The contracts typically last for 30 years, after which time the buildings belong to the public authority"⁴⁰.

- 11.3 The crucial elements of PFI schemes are clear. They are intended to allow public bodies including HEIs to procure buildings or services without having to borrow the funds, to share or obviate the risk inherent in the undertaking, and to obtain services where the competence or cost effectiveness of a private company may exceed the public body's. These are self evident attractions, but it is worth dwelling on the underlying premises.

³⁹ See www.hm-treasury.gov.uk/documents/public_private_partnerships/ppp_index.cfm

⁴⁰ See www.guardian.co.uk/society/2006/may/03/politics.theissuesexplained

- 11.4 Firstly, the income to the company is the means by which it services the debts incurred and secures profit. The issue, then, is does this approach offer better value than if an HEI were to finance the activity itself? Leaving aside running costs, financially the undertaking may make sense as a PFI if a company can borrow more cheaply than an HEI, or if it can secure more income from services than an HEI would be able to. Clearly, the financing should be scrutinised as part of business planning to see how the options compare. (Of course, there may be other financial reasons for preferring PFI, for instance if an HEI does not want to take a further loan on to its books.)
- 11.5 Secondly, risk is to be shared, with all parties minimising their risk by introducing limits on liability, penalty clauses for failures to meet targets, and so forth. If the transfer of risk from an HEI is to be a reality, the terms of the contract are critical, and will call for the most careful scrutiny.
- 11.6 Finally, there is the implication that companies will be able to provide services more cost efficiently than HEIs: while this may be true, it will be necessary to ensure that performance is acceptable, and that remedies for under-performance are available. An HEI may also need to come to a view on the acceptability of companies possibly increasing efficiency through worsening staff pay and conditions of service.
- 11.7 The Hefce website gives some details of PFI case studies in English HEIs⁴¹, and generally, they relate to the procurement of student residences. This is unsurprising: the attraction for an HEI and private partner are clear when there is an identifiable income stream that will be generated from an initiative, and with relatively free standing activity against which risk can be assessed. It has to be said, though, that it is striking that the examples do not relate to mission critical activity. The case studies given are useful in that they contain descriptions of problems encountered as well as successes.
- 11.8 The issues for governors in this initiative are extensive, and raise the questions about the balance to be struck between ensuring that the governing body is properly involved without usurping the roles of those who carry executive responsibility, and without causing undue delay.

Self-challenge questions

- What part if any does PFI play in your HEI's strategies?
- If your governing body were to consider PFI funding, has it sufficient expertise to robustly assess the process?
- Looking back on the last main project that your governing body approved, in retrospect what might have been the advantages and drawbacks if PFI funding had been sought?

⁴¹ See www.hefce.ac.uk/finance/procurement/pfu/