

Public Private Partnerships in the National Health Service: The Private Finance Initiative

Good Practice

Overview



This guidance has been endorsed by the Treasury Taskforce. Specific queries on it should be addressed to the NHS Private Finance Unit on 0113 254 6132. Wider queries on PFI policy should be addressed to the Treasury Taskforce Policy Helpdesk on 0171 270 5527.

Requests for copies of Treasury Taskforce publications should be addressed to the Treasury Public Enquiry Unit on 0171 270 4558/4860/4870.

This document

1. This overview of *Public Private Partnerships in the National Health Service: The Private Finance Initiative* is in two parts:
 - part one explains the nature, purpose and structure of the guidance;
 - part two summarises the operation of the Private Finance Initiative (PFI) in the NHS.

Part One

The guidance – *Public Private Partnerships in the National Health Service: The Private Finance Initiative (PFI in the NHS)*

2. The guidance (referred to from now on as *PFI in the NHS*) provides practical advice for NHS bodies involved in, or contemplating, PFI schemes. It is for NHS Trusts, commissioning Health Authorities (HAs) and Primary Care Groups (PCGs). It may also be useful to the private sector, and can be accessed via the internet at www.doh.gov.uk/pfi.htm
 3. *PFI in the NHS* is based on best practice and the experience of the first wave schemes. It has been developed in keeping with the White Paper *The New NHS: Modern, Dependable*. It highlights the main issues and procedures in PFI procurement, and indicates what is required at various points in the process.
 4. The guidance applies to both small and large schemes involving the provision of facilities and services.
 5. To ease the procurement process, the NHS Executive has produced a standard form contract, with which this guidance is consistent. Nonetheless, NHS bodies and private sector parties should seek their own legal advice before and during any PFI procurement. All efforts have been made to ensure the accuracy of this guidance, but it is not to be taken as a definitive statement of the law. Even if this guidance is followed, there is no guarantee that this will lead to Full Business Case approval by the NHS Executive. No liability for loss arising from following this guidance will be accepted.
- ### **Structure of *PFI in the NHS* guidance**
6. Figure 1 shows the guidance structure. Further sections may be added to the *PFI in the NHS* series later.

Figure 1: Structure of PFI in the NHS guidance

Section 1: <i>The Selection and Preparation of Schemes</i>	Section 2: <i>The PFI Procurement Process</i>
<ul style="list-style-type: none"> ● Introduction ● <i>Overview</i> of the pre-procurement process ● The Strategic Outline Case ● The Capital Prioritisation Advisory Group ● The Outline Business Case ● Affordability and value for money ● Roles and responsibilities of the public sector team ● Skills, training, and where to turn for help ● The selection and management of advisers ● Developing the scope of the project ● Planning permission ● Openness and public involvement ● Fair treatment of staff ● Milestones 	<ul style="list-style-type: none"> ● Introduction ● An overview of the PFI procurement process ● Advertising the project ● Prequalification ● The Invitation To Negotiate ● Evaluation and selection ● The Full Business Case ● Finalising the deal
Section 3: <i>Technical Issues</i>	Section 4: <i>Commercial Issues</i>
<ul style="list-style-type: none"> ● Introduction ● Risk analysis ● The Public Sector Comparator ● The accounting treatment of schemes ● Payment mechanisms ● Indexation ● Benchmarking/market testing of services ● Land and buildings in PFI schemes ● IT and equipment in schemes ● Methods of financing PFI schemes ● Financial models of schemes ● Design quality ● Establishment orders 	<ul style="list-style-type: none"> ● Introduction ● The project agreement ● Key commercial terms

7. Since best practice will continue to evolve this guidance will be updated in the light of experience, or if new models of public private partnership develop.

PFI in the NHS and other NHS guidance

8. This guidance supersedes the *Private Finance Guide* published within the *Capital Investment Manual (CIM)* framework in 1994, and *HSG(95)15 (Private Finance and Capital Investment Projects)* issued in March 1995. *HSG(95)48 (Information Management and Technology Procurement and Private Finance)* remains current.

9. The principles set out in *Commercial Issues* are reflected in the standard form contract which must be used for major PFI schemes and which is available from the NHS Executive Private Finance Unit. A version of the standard contract for smaller schemes will be provided in due course.

Other non-NHS guidance

10. As well as guidance from the NHS Executive, there is a growing body of guidance, advice and case studies available on PFI across all sectors. The Treasury Taskforce are compiling a library of documentation which may be accessed by contacting Olga Morris, Private Finance Policy Team, Treasury Taskforce, on 0171 270 5447. Treasury guidance is cross-referenced in *PFI in the NHS*, and a full bibliography is at Appendix 1 of this *Overview*.

11. After examining several PFI schemes, the National Audit Office (NAO) have now produced a report on their general approach to the audit of PFI deals (*Examining the value for money of deals under the Private Finance Initiative*, July 1999). The report is intended not only for auditors of PFI schemes but for all those in both the public and the private sector who are involved in taking forward a PFI scheme.

Further advice

12. As well as using the guidance, it will often be helpful to talk to others who are tackling similar projects. The NHS Executive facilitates networking for NHS Trusts working on major PFI schemes, and assists any NHS body with practical questions about PFI. For specific queries about PFI procurements, NHS bodies should in the first instance contact their Regional Office. The current list of contacts is at Appendix 2. The changes to the boundaries of NHS Executive Regional Offices came into effect fully from 1 April 1999; a map showing the new Regional Office names and boundaries is at Appendix 3.

13. A glossary of terms used is at Appendix 4.

Further information

The New NHS: Modern, Dependable, CM3852, The Stationery Office, 1998

Examining the value for money of deals under the Private Finance Initiative.
The Stationery Office, 1999

Part Two

The Private Finance Initiative in the NHS

14. PFI is one model of Public Private Partnerships in the NHS; other forms may develop over time. PFI is a key policy for improving the quality and cost-effectiveness of public services. It enlists the skills and expertise of the private sector in providing public services and facilities. It is not simply about the financing of capital investments, but about exploiting the full range of private sector management, commercial and creative skills.

PFI schemes

15. PFI schemes involve creating partnerships between the public and private sectors. In the health sector, the NHS will continue to be responsible for providing high quality clinical care to patients. But, where capital investment is required, there will increasingly be a role for a private sector partner in the provision of facilities. PFI is about building long term and mutually beneficial partnerships between public and private sector partners.

16. Major PFI schemes are typically DBFO (design, build, finance and operate). This means that the private sector partner is responsible for:

- designing the facilities (based on the requirements specified by the NHS);
- building the facilities (to time and at a fixed cost);
- financing the capital cost (with the return to be recovered through continuing to make the facilities available and meeting the NHS's requirements);
- operating the facilities (providing facilities management and other support services).

Risks in each of these areas will be assumed by the PFI partner, if best placed to bear them, in such a way that overall the risks associated with procuring new assets and services for the NHS will be reduced. Moreover, because the PFI partner's capital is at risk, they will have strong incentives to continue to perform well throughout the life of the contract.

17. NHS Trusts will continue to be the employer of clinical staff. PFI in health is about ensuring that the facilities in which they work are as modern, efficient and cost effective as possible by placing responsibility for their provision to specialist managers who are expert at providing them. The NHS can then concentrate upon the provision of health care.

18. The essence of PFI is that the NHS defines its needs in terms of "outputs", ie the nature and level of the service required, and invites private sector bidders to present their solutions to meet these service needs. This allows the private sector to make the fullest possible use of its experience and skills in order to bring innovative solutions to the needs of the health service.

19. Typically, for a large scheme, the private sector partner will be a consortium whose members may include a construction company and a facilities management provider, amongst others. The private sector partner obtains finance for the project, constructs the hospital, and provides services to the NHS Trust as specified in the contract agreed between the NHS Trust and the private partner. The terms of the contract set out the range of services to be provided and the performance standards required of the consortium. No payments are made by the NHS until services are provided to the agreed standard. Thereafter, the standard must be maintained to ensure full payment.

20. Figure 2 illustrates the contractual relationship between an NHS Trust, consortium and financiers for a typical large PFI scheme which is bank financed.

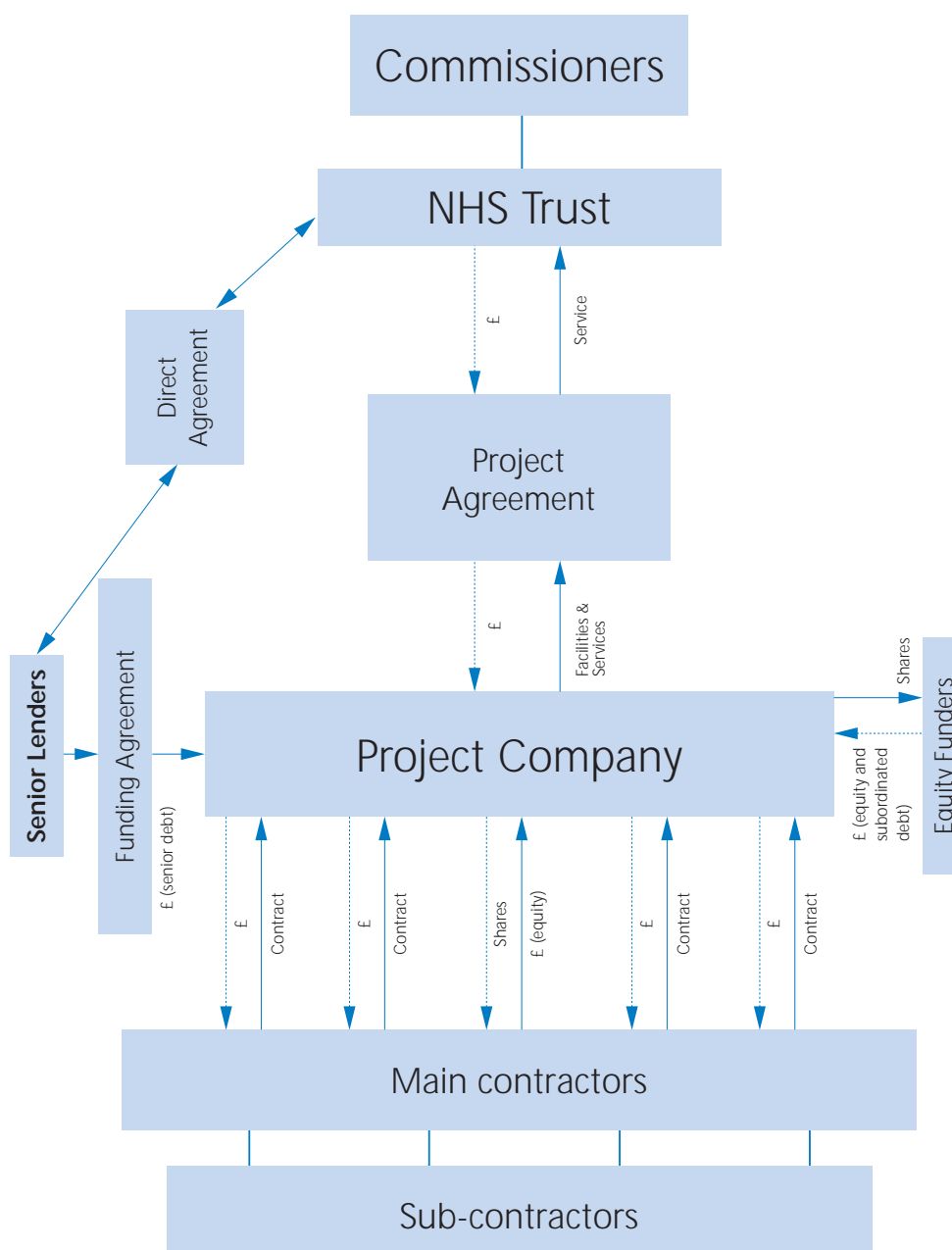
Fundamental requirements for a PFI scheme

21. Any PFI scheme must demonstrate value for money (VFM) for expenditure by the public sector. This can be achieved if the private sector assumes risks which would otherwise have been borne by the public sector where they are more cost effectively managed by the private sector, and by efficiency savings.

22. Best VFM is the optimum combination of whole life costs and benefits. There are three separate VFM decisions to be taken:

- whether to proceed with the project at all;
- whether to proceed using PFI;
- which private sector partner to select.

Figure 2: Contractual relationships under PFI



PFI Procurements in the NHS

23. PFI is governed by the same principles and procedures that have been established to ensure that all investment in the NHS is soundly based. The NHS capital procurement process set out in the *Capital Investment Manual (CIM)* comprises four stages:

- Stage 1: establish the strategic context and make the case for change. In future, the Health Improvement Programme will be the means by which the need for change is identified;
- Stage 2: identify the preferred option and prepare an Outline Business Case;
- Stage 3: assess and plan the preferred option in detail, and prepare a Full Business Case;
- Stage 4: manage the project through implementation and evaluation to ensure that the outputs are delivered.

24. The NHS PFI process reflects these four stages. In order to ensure that the number of major schemes (with a capital value over £25m) progressing through the system is realistic, and thereby to increase their chances of success, proposals for major schemes are prioritised nationally on the basis of health service need. Only prioritised schemes may proceed to procurement.

25. The NHS PFI process is as follows:

- establish the strategic context, assess the options and, for major schemes, make the case for change in a Strategic Outline Case and get approval;
- identify and develop a preferred option through an investment appraisal, make the case in an Outline Business Case, and get approval;
- prepare for procurement by turning the approved option into a detailed specification of outputs, outcomes and desired allocation of risks;
- advertise the project in the Official Journal of the European Communities (OJEC), identify potential providers and the best privately financed solution;
- select a preferred bidder with whom negotiations can be completed, involving stakeholders (eg staff and trade unions) in the assessment of proposals;
- complete the definitive investment appraisal and Full Business Case to obtain approval;
- finalise, award and implement the contract; and
- evaluate and monitor the project.

26. The phases of the NHS PFI process are illustrated in Figure 3, alongside the procurement process set out in HM Treasury's Step by Step Guide to the Procurement Process. The formal procurement process from advertising in OJEC to financial close is shown in Figure 4.

Figure 3: Reconciliation of PFI in the NHS and Treasury's Step by Step guide

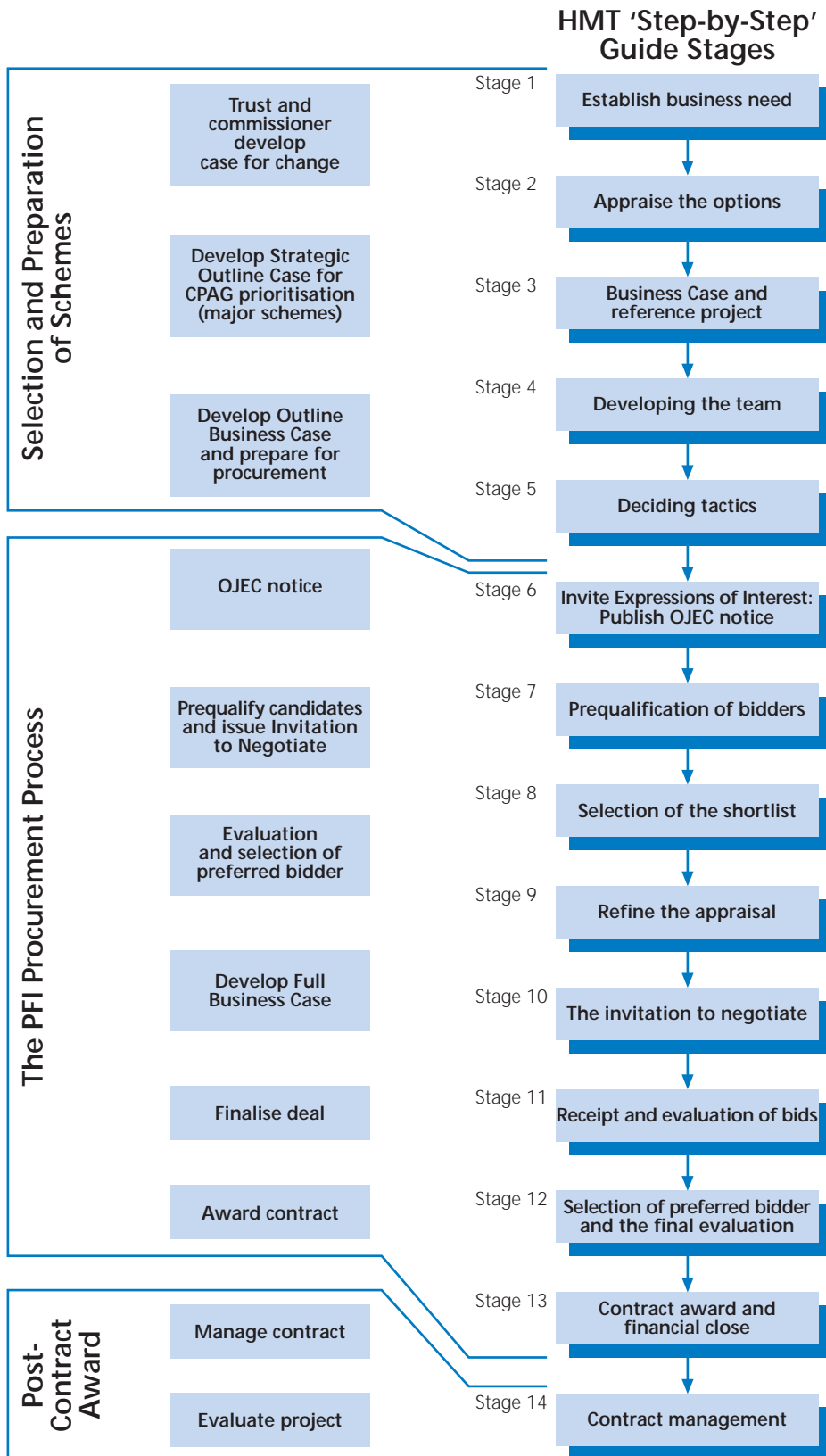
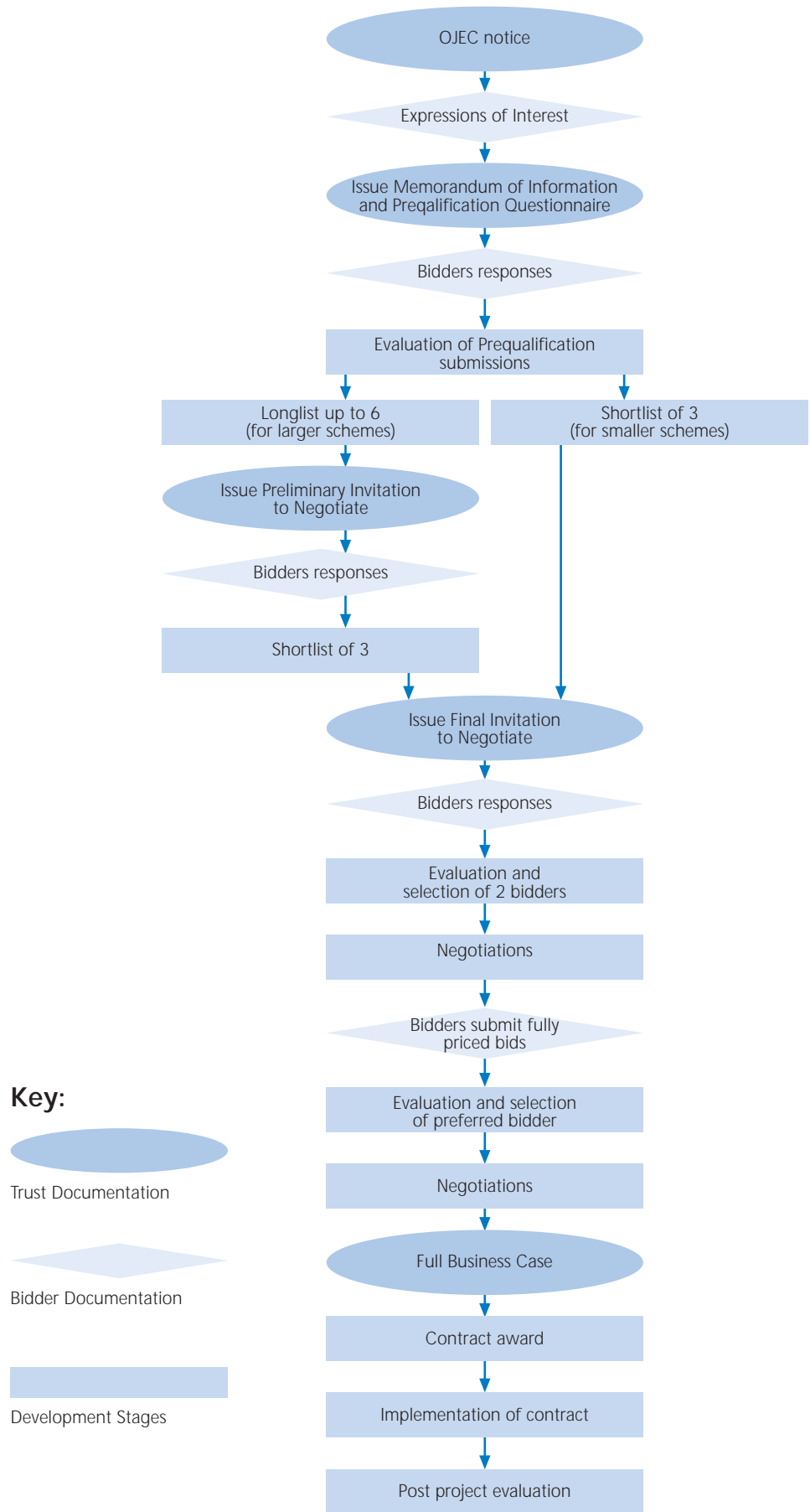


Figure 4: Formal procurement process from OJEC to financial close



Appendix 1: Bibliography of Treasury Taskforce Guidance

GENERAL

Partnerships for Prosperity (Treasury Taskforce, November 1997)

A Step-by-Step Guide to the PFI Procurement Process (Treasury Taskforce, revised April 1998)

Standardisation of PFI Contracts (Treasury Taskforce, July 1999)

Staff Transfers from Central Government: A Fair Deal for Staff Pensions (HM Treasury, June 1999)

POLICY STATEMENTS

Policy Statement No. 1: *PFI and Public Expenditure Allocations* (Treasury Taskforce, October 1997)

Policy Statement No. 2: *Public Sector Comparators and Value for Money* (Treasury Taskforce, March 1998)

Policy Statement No. 3: *PFI and Public Expenditure Allocations for Non-Departmental Public Bodies* (Treasury Taskforce, August 1998)

Policy Statement No. 4: *Disclosure of Information and Consultation with Staff and other Interested Parties* (Treasury Taskforce, October 1998)

TECHNICAL NOTES

PFI Technical Note No. 1: *How to Account for PFI Transactions* (Treasury Taskforce, September 1997)

PFI Technical Note No. 1 (Revised): *How to Account for PFI Transactions* (Treasury Taskforce, June 1999)

PFI Technical Note No. 2: *How to follow EC Procurement Procedure and Advertise in the OJEC* (Treasury Taskforce, May 1998)

PFI Technical Note No. 3: *How to Appoint and Manage Advisers* (Treasury Taskforce, September 1998)

PFI Technical Note No. 4: *How to Appoint and Work with a Preferred Bidder* (Treasury Taskforce, July 1999)

PFI Technical Note No. 5: *How to Construct a Public Sector Comparator* (Treasury Taskforce, October 1999)

Copies of the above publications are available from the Public Enquiries Unit, HM Treasury, Parliament Street, London, SW1P 3AG (Tel: 0171 270 4558/4860/4870)

HM Treasury guidance is also available on the Treasury Taskforce website direct at <http://www.treasury-projects-taskforce.gov.uk> or through the Treasury's website <http://www.hm-treasury.gov.uk>, under the section headed "Guidance"

Appendix 2: NHS Executive and Territorial PFI contacts

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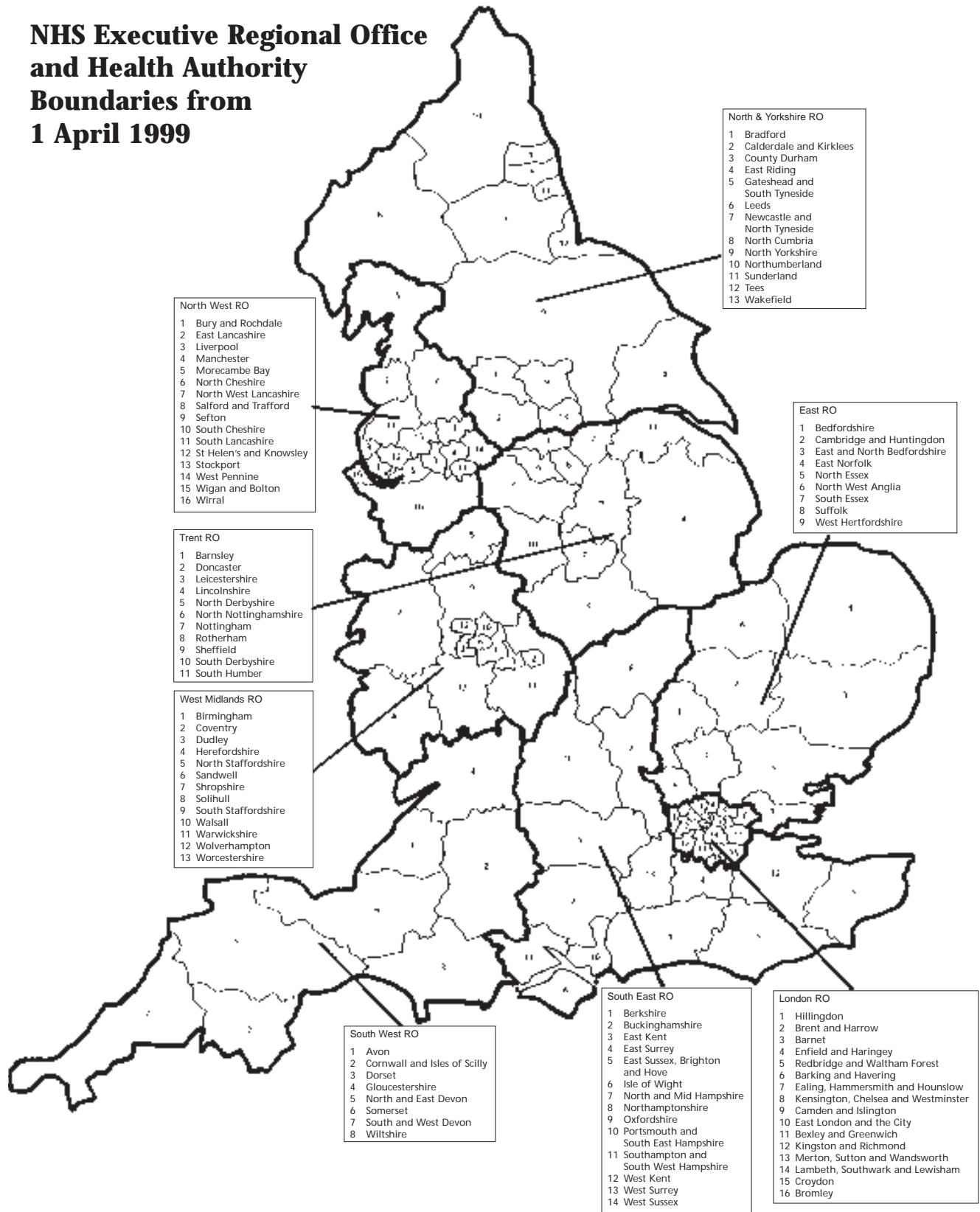
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Appendix 3: NHS Executive Regional Offices

NHS Executive Regional Office and Health Authority Boundaries from 1 April 1999



Appendix 4: Glossary of terms

ASB	Accounting Standards Board
CDM	Construction Design and Management Regulations
CHC	Community Health Council
CIM	Capital Investment Manual
CPAG	Capital Prioritisation Advisory Group
DBFO	Design Build Finance and Operate
DV	District Valuer
EAC	Equivalent Annual Cost
EFDA	Externally Financed Development Agreement
EL	NHS Executive “Executive Letter”
FBC	Full Business Case
FRS	Financial Reporting Standard
GAD	Government Actuary’s Department
GDP	Gross Domestic Product
HA	Health Authority
HAZ	Health Action Zone
HImP	Health Improvement Programme
HSC	Health Service Circular (guidance note)
HSG	Health Service Guideline
I&E	Income and Expenditure
IBD	Interest Bearing Debt
IM&T	Information Management and Technology
IRR	Internal Rate of Return
ITN	Invitation to Negotiate
ITT	Invitation to Tender
LIBOR	London Interbank Offer Rate

NBV	Net Book Value
NHS	National Health Service
NPC	Net Present Cost
NPV	Net Present Value
OBC	Outline Business Case
OJEC	Official Journal of the European Communities
OMV	Open Market Value
PCG	Primary Care Group
PDC	Public Dividend Capital
PFI	Private Finance Initiative
PFU	Private Finance Unit (NHS Executive HQ)
PIN	Prior Information Notice
PITN	Preliminary Invitation to Negotiate
PPP	Public Private Partnerships
PSC	Public Sector Comparator
RPI	Retail Price Index
RPI-X	RPI excluding mortgage interest payments
SLA	Service Level Agreement
SOC	Strategic Outline Case
SPV	Special Purpose Vehicle (ie project company)
SSAP	Statement of Standard Accounting Practice
TSC	Technical Sub-Committee (to CPAG)
TTF	Treasury Task Force
TUPE	Transfer of Undertakings (Protection of Employment) Regulations 1981
VAT	Value Added Tax
VFM	Value for Money