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The actual evaluation of school PFI bids for value for money in the UK public sector

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Abstract

Much of the literature on value for money (VFM) evaluation of private finance initiative (PFI) contracts has concentrated on the financial methodology of constructing the public sector comparator (PSC) and its limitations. In contrast, this paper focuses on examining how 'PFI bids' are actually evaluated for VFM in the case of three secondary school PFI contracts. It is a unique study which presents the Northern Ireland school PFI decision-making processes, within the broader UK context. It is based on the full business cases of three PFI schools and interviews with key actors involved in the PFI processes. This study shows that the methodology used to evaluate and benchmark the design, facilities management, financial and contractual aspects of PFI bids for VFM is subjective and problematic-changes in the assumptions used may easily shift the balance in favour of conventional procurement and/or competing private sector service providers. It further highlights the importance of risk transfer; how non-financial factors are taken into consideration; and the public sector's reliance on consulting firms and 'accounting measures' in the PFI decision-making processes.

Keywords: Private finance initiative; Public private partnerships; New public management; Value for money; Schools; Northern Ireland; UK

1. Introduction

The private finance initiative (PFI), introduced in 1992 by the UK Conservative government, involves a contractual agreement for the provision of infrastructure

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related public services by a private sector consortium, in return for a stream of payments payable by the public sector. In 1997, it was adopted by the successive Labour government as part of the broader public private partnerships (PPP) reform agenda to modernise public services (Broadbent and Laughlin, 2005). The government posits that PFI offers better value for money (VFM) than conventional procurement, achieved through 'optimal' risk-sharing between the public sector and the private sector, and innovative design and delivery of public services by the private sector (HM Treasury, 1997, 2006). VFM, as illustrated later in the paper, is demonstrated through the 'accounting quantification' and comparison of the costs and benefits of the conventional public sector procurement option with the PFI option. Government departments mostly rely on HM Treasury guidance (for example, HM Treasury, 2003) and consulting firms to legitimise their preferred procurement option and demonstrate VFM.

Since its introduction, the PFI policy has been subject to many theoretical and empirical debates. Most studies have explored the PFI decision-making processes and have raised concerns over accountability and VFM (see for instance, Broadbent et al., 2003, in press; Broadbent and Laughlin, 1999; Edwards et al., 2004; Edwards and Shaoul, 2003a, 2003b; Heald, 2003; Pollock et al., 2002; Shaoul, 2002, 2003, 2004, 2005). For example, Heald (2003) explored the implications of risk transfer on VFM and the accounting treatment of PFI contracts on the public sector's balance sheet. From a distribution of economic wealth perspective, Shaoul (2005) critically examined the financial methodology used to appraise PFI projects in the case of hospitals. Recently, researchers have started to explore post project evaluation of PFI contracts to assess VFM and accountability in the underlying processes (see for example, Broadbent et al., 2004; Edwards et al., 2004; Ismail and Pendlebury, 2006).

To date, much of the literature on VFM evaluation of PFI contracts has concentrated on the public sector comparator (PSC) and its limitations. In contrast, this paper focuses on examining how school 'PFI bids' are evaluated for VFM after the initial decision to proceed with PFI has been made. It is a unique study of the Northern Ireland's experience of school PFI contracts, within the broader UK context. It is important to understand the methodology and the criteria used to evaluate PFI bids for VFM because it is in these processes that performance expectation regarding the delivery of PFI services are formed and transformed into binding legal agreements. The financial and non-financial criteria used to benchmark PFI bids for VFM may need to be followed by the respective government departments to monitor the progress of the PFI contract over its term of 25 years or more (Broadbent et al., 2003).

This paper is organised into six further sections as follows. The next section provides a brief review of prior studies on VFM evaluation of PFI contracts to highlight the gap in the literature that this paper has attempted to address. The third section explains the research methodology used for collecting empirical data. The fourth section explains the PFI decision-making processes in the context of secondary schools in Northern Ireland. The fifth section discusses the risk-adjusted PSC used by the public sector to appraise PFI contracts for VFM. The penultimate section illustrates the methodology and criteria used to evaluate PFI bids for VFM. The final section discusses the empirical findings and concludes the paper.