SAVE LEWISHAM HOSPITAL CAMPAIGN CONFERENCE AND DISCUSSION
NHS in Crisis

Why is our NHS under threat and what can we do to defend it?
Goldsmiths College Saturday 5 December 2015, 10.30am - 4pm

PRIVATE FINANACE INITIATIVE (PFI): ISSUES AND WAY FORWARD

Jane Mandlik

Background

The purpose of this paper is to expand on the ideas put forward in a letter published in The Guardian on 31st August 2015 (App. 1) and to form the text for the PFI item at the SLHC Event on 5th December 2015

Introduction

When Labour came into power in 1997, PFI was already in operation having been first introduced by the Major government.

Gordon Brown was faced with the problem of financing the re-building of a crumbling public infrastructure but also the political imperative not to increase the National Debt. He enthusiastically embraced PFI encouraged by the then current view that the higher efficiency of the private sector versus the public sector would more than compensate for the higher cost of private finance as opposed to government borrowing rates.

Typical PFI Model

A small group of private investors form a company, often referred to as a SPV (Special Purpose Vehicle), to bid for a PFI project. If successful they go on to borrow money to finance the early stages of the project, i.e. acquiring the land, rationalising the estate, designing the new buildings and producing the construction documentation. They then sell bonds to raise funds to cover the cost of construction. In many cases the company successfully negotiates a further contract to service the facility for the full term of the PFI contract, i.e. to provide a hard and soft maintenance service.

A very tangled web is spun and there are opportunities at every stage for the original company to cream off profits:

- They charge for the administration of the company/SPV
- They are often partners in the design and build company and therefore take a share of the profits at the construction phase
- They borrow money and sell bonds at high rates of interest giving access to their cronies in the finance world to easy money
- They are either partners in the maintenance companies or they make a profit out of contracting out these services

- In some cases the original company retains ownership of buildings, leases etc. at the end of the contract and thereby benefit from any capital gains
- The original company may be registered overseas and therefore does not pay UK taxes on profits
- Original loans are refinanced to take advantage of current lower interest rates and the proven low risks associated with PFI projects
- Shares are sold on.

Unsustainable PFIs

Very soon it became apparent that some trusts were finding it difficult to meet their PFI payments. The PFI loans were in some cases out of kilter with the trusts' incomes and were not sustainable. A Nuffield Trust report on Health Spending in 2011/12 identified a number of NHS trusts that were spending more than 5% of total revenue on servicing PFI payments. In 2012 the Department of Health (DoH) announced that it would provide a £1.5bn pot to subsidise these trusts. The South London Healthcare Trust (SLHT), with a PFI commitment of £63.8m in 2011/12[1]- 16% of total revenue- was included and subsidies were specified towards the annual costs of the PFI contracts for two sites, the Queen Elizabeth Hospital (QEH) and the Princess Royal University Hospital (PRUH). When the SLHT was dissolved and the QEH merged with Lewisham Healthcare NHS Trust to form Lewisham and Greenwich NHS Trust, the subsidy agreement for QEH was transferred to the new trust. There is however still some uncertainty as to the terms of the subsidy in future years.

Recent Developments

Since the financial crash of 2008 and failed privatisation of sections of the NHS e.g. Hinchingbrooke, it is clear that the private sector cannot be relied upon to deliver best value for money or be trusted to operate essential services.

As reported in the BMJ (11th October 2014) Northumbria Healthcare NHS Foundation Trust has borrowed £114m from the local authority, Northumberland County Council, to terminate the PFI contract covering the building and maintenance of Hexham General Hospital. The Trust will save £3.5m per year for the remaining 19 years that the contract was due to run. The amount borrowed by that Trust is of the same order as the outstanding loan of the Lewisham and Greenwich NHS Trust, i.e. the PFI loan for QEH plus the loan for the Riverside Building at Lewisham Hospital (UHL). Therefore the paying off of the Hexham loan was of interest to the Save Lewisham Hospital Campaign.

In August the London Mayoral candidate, Sadiq Khan, announced that he would support a similar local authority loan option for the Capital's PFI Trusts. This was followed by a commitment to the proposal by Jeremy Corbyn, who has been since elected as Leader of the

[1] Figure from DoH reply November 2013 (ref:817027) to SLHT FOI request

Labour Party, (App.2). Support of the principal party of opposition is a major step forward in the resolution of the PFI problem and is to be welcomed.

Current Campaigning Positions

The efforts of many campaigners over recent years have ensured that the iniquities of PFI are now generally understood and it is now time to end this abuse. To date finding a resolution to PFI has proved to be contentious both within the Labour Party and among campaigners and no agreed way forward has been identified

Anti-PFI campaigners will only be too well aware that the Sadiq Khan proposal to pay back PFI loans is the very point over which there is vehement disagreement and is the issue that has prevented campaigns uniting in their fight against PFI.

For clarity, the principal arguments **against** paying back PFI loans are as follows:

- Paying back loans would increase National Debt thereby risking adjustment to credit rating of UK
- Any increase in National Debt could trigger increase in austerity measures
- Following delivery of Simon Stevens' 5 Year Forward View (5YFV) some PFI trusts may have been stripped of their A&E, Maternity and other non-profit making departments thus making them attractive for buyout by the private sector (particularly if there is land that could be sold off), but only if PFI loans have been paid back
- If contract re-negotiations are successful there should be no financial incentive to pay back the PFI loans
- It has been suggested that paying back debt could be a money laundering exercise. Without substantiating evidence this can only be viewed as a manifestation of the profound public mistrust of PFI and its ramifications, possibly a reason in itself to end the PFI regime.

Way Forward - Proposed Resolution

Against this background I wrote to the Guardian on 31st August outlining a proposal that would make it possible to move forward by avoiding the payoff of PFI loans but would still remove the unjust burden of PFI costs from NHS Trusts (App.1). This proposal is described in more detail below.

Annual PFI payments (sometimes called Unitary Charges) made by NHS trusts cover the interest payable on loans, pay back of capital, cost of management of PFI contract, major maintenance of facility and (where relevant) the cost of routine building maintenance and the provision of soft maintenance, i.e. catering, cleaning, security etc.

It is proposed that:

Phase 1: PFI Subsidies

- Each PFI trust should receive an annual subsidy equal to all PFI costs which are in excess of sovereign borrowing rates and market prices. This provides a level playing field where all trusts receive equivalent assistance and centralises the cost of legal and accounting expertise. It avoids duplication of effort while building up a centralised capability and expertise to ultimately resolve the PFI scandal in the best interests of the country.
- In WGA (Whole Government Accounting) terms this should be a revenue neutral exercise since these costs are already being paid from the public purse but via different budgets.
- Since some trusts are already being subsidised to enable them to meet PFI costs it is unlikely that any changes to legislation would be required to extend the subsidies to all PFI trusts and this could be enacted without much delay thereby relieving trusts of the annual burden of excessive PFI payments.

Phase 2: Re-negotiate PFI contracts

Grounds for Re-negotiation

- The government has a duty to address misuse of public funds
- Unjustified expenditure of public funds is incompatible with the Government's Austerity programme
- No risk – although the interest rates were based on risk of failing trusts defaulting on payments, in reality the government as a last resort covers the cost so there is no risk
- Efficiency argument disproved particularly since the 2008 crash and failed private sector projects
- Sympathy of Bond holders such as Pension Funds and other ethically aware investors
- Hospitals no longer fit for purpose and contracts make it difficult to adapt facilities to changes in delivery of service
- Current low interest rate levels
- Service contracts that are inflexible, difficult to monitor and do not reflect current market rates
- Poor conditions for workers employed by service contractors. There may be grounds for re-letting these contracts with terms and conditions drawn up jointly by local management and trades unions
- Failure to re-negotiate should render these firms no longer qualified to bid for future public sector work
- Contracts were drawn up hastily and should be subject to review
- Possible failure to comply with legislative tests e.g. prior to 1989 the Treasury had to apply the Ryrie Rules to public sector projects funded by private finance - these rules determined whether the use of private finance would deliver a cost saving for the taxpayer
- A re-negotiated contract may still be attractive as a safe investment in the current economic climate

Phase 3: Pay back PFI Loans

Following the re-negotiation process, the accountants and lawyers would be very familiar with the various contracts and their dangers and complications. So despite caveats highlighted above it may, after extensive research and testing, be considered expedient to pay back the loans for the following reasons.

- A significant concern and possibly the main argument supporting the paying back of PFI loans and the ending of PFI contracts is that as long as private profits are being made from the NHS by way of PFI and other privatisation packages the service will come within the TTIP remit.
- Some PFI contracts are now half way through their terms therefore the original loans have already been partially paid back and with adjustment for inflation the outstanding loans could possibly be added to the National Debt with minimum impact.
- More controversially the government could default on a percentage of the PFI debt on the basis that the contracts may not have delivered fully on the original terms and annual payments were excessive. Governments are generally reluctant to default on debts because it may risk their ability to raise money in the future.

Conclusion

The problem of PFI must be resolved as soon as possible. It is wasting significant amounts of public money and is causing profound damage to the NHS. Progress of the devolution agenda will make the achievement of a centralised PFI solution much more difficult as budget responsibility and decision making become more fragmented.

Subsidies could be introduced with minimum delay followed by re-negotiation of contracts. Simultaneously campaigners must put their energies into promoting the Reinstatement Bill (amended if necessary) to put an end to privatisation of the NHS and to protect the service from TTIP and other such agreements.

Recommendation

Advice should be sought as to feasibility of the above proposals as a means of resolving PFI issues. The approach is transparent, not post code dependent, efficient in use of expertise, may require only minimum legislative change and addresses many of the issues that have up to now prevented any meaningful progress in eliminating the abuse of public funds through unjustifiable PFI contracts.

Next Steps

Ask Shadow Health Secretary Heidi Alexander to refer paper to Shadow Treasury and Health teams.

Campaign for end of PFI in tandem with the Reinstatement Bill campaign.

Jane Mandlik, 26 November 2015

Appendix 1

Dear Letters Editor,
Ref: Corbyn hits out at PFI "mess" The Guardian Thursday 27/08/15

I fully support Sadiq Khan's proposal to relieve NHS Trusts of the burden of excessive PFI payments, however I do not agree that Local Authorities should raise funds to fully pay back PFI loans.

The PFI was a central government policy and should be resolved centrally to ensure a level playing field across the nation. Without delay the Government should arrange for subsidies to be given to all PFI NHS Trusts to cover elements of all PFI interest payments and associated maintenance contract charges which are in excess of market rates. The Government should also assist Trusts in re-negotiating all PFI contracts down to justifiable rates. Any PFI loans that may be paid back via Local Authority loans should include reductions to reflect the excessive and unfair payments that have been made during the life of the contract.

The private sector must learn that they can no longer make odious levels of profit out of the NHS.

Appendix 2

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