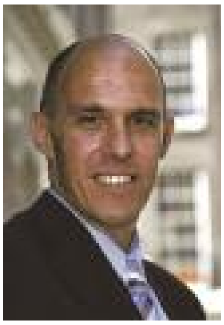
Why PFIs go wrong - and how to make them work



Millions of pounds of public money are wasted because contractors are charging unjustifiably high fees to amend active PFIs (Private Finance Initiatives), according to the National Audit Office. Public authorities often get 'poor value for money' when they request additions to ongoing PFI projects from private sector consortia, such as to build and operate schools and hospitals, the NAO report concluded.

The problem is attributable to a failure in leadership, says **David Archer** of **Socia**, (pictured above) who trains boardroom decision-makers in setting up and running partnerships – public-private, joint venture and supply chain. In his experience, partners at the most senior level in PFIs fail to understand the special requirements for operating these ventures on a collaborative, rather than the combative basis to which they default so often.

A recent Ipsos MORI survey, commissioned by Socia, found that senior decision-makers with partnering experience in both the public and private sectors believe that these relationships can transform the UK's ability to meet commercial and social goals, but they say that the relevant leadership capabilities are lacking.

Almost nine out of ten of the directors questioned acknowledge that more careful set-up and planning would have helped them avoid later operational problems for partnerships. The traditional focus on contracts and governance issues is not where the major gains are to be made, they say. Partners confirm the need to focus on 'partnering skills' and particularly on training in relationship management and collaborative leadership.

Contracting for PFI failure

David Archer says that many PFIs are doomed from the start because the objectives and methods of working of public authorities and contractors are incompatible at the most senior level, and the issue is ignored or assumed to be simply irreconcilable.

To reduce the perceived uncertainties in the relationship, public authorities often try to define it within a highly prescriptive and inflexible contract. This means that the agreement, which can run for up to 25 or 30 years, cannot accommodate the unforeseen changes that inevitably impact on projects – whether from variations in user demand, cost inflation or the positive opportunities arising from new technology, for example.

The private sector exacts a high price to discount the costs arising from future risks associated with PFI contracts. Future payments across all PFI projects up until 2031-32 amounts to £91 billion in today's money, according to the NAO: and this is before any amendments.

More than £180m of taxpayers' money was spent on changes to many of the 500 PFI deals in 2006. The audit office report found that most private sector PFI operators charged 'unjustified' extra management fees, often as high as 10 per cent, in addition to the charges made by the service providers for changes that were requested.

A further problem was that public authorities were frequently not equipped to manage PFI projects and had little idea how much changes should cost. For example, the cost of adding a single electrical socket varied from around £30 to more than £302 in projects, with an average that was higher than the benchmark prices published by the Royal Institution of Chartered Surveyors.

"Under the media spotlight, problems in PFIs escalate to a crisis point where the contract breaks down. A management consultancy is brought in, which reacts by rewriting the terms for an even tighter, more inflexible contract. The project fails again and the result is more delays and massive expense overrun." Says David Archer.

Socia identified the opportunity for a different approach to public-private partnerships in the 1990s during its work in advising oil and gas companies on how to deal with risk and uncertainty when partnering with national governments, contractors and the range of other parties that are engaged in big exploration projects.

This new approach pre-empts problems, according to David Archer, by ensuring transparency in the relationship and alignment of 'purpose and processes' at the outset of the project, at the most senior level.

Socia works with public and private sector leaders using a range of analytical tools to determine and disclose what each party really wants and will need from the partnership, and how future problems will be resolved and changes accommodated, and by whom. It is the foundation for a more collaborative relationship: it also ensures that the unworkable clauses that are so often written defensively into the contract by legal teams can be excised at the start, rather than when they finally collapse.

Collaboration makes PFIs work

Commenting on the recent NAO report, Edward Leigh, the chairman of the Commons' public accounts committee, said that public sector managers should be more 'street-wise' when dealing with savvy private sector contractors:

"The public sector has allowed itself to be taken for a ride. It is depressing that, for one in five PFI projects, the public authorities trim the projects at the initial plan stage to save money, only to risk being stung later by the private sector contractors when things are put back into the project."

David Archer says the interests of public authorities and contractors are reconcilable: "No relationship can work when it is predicated on ignorance and suspicion. You have to understand and acknowledge the points of difference on key operational and performance issues at the start and throughout the life of the project – then you can reconcile these variances when and where it really matters. These things are not instinctive to most leaders, but with the right training and support PFIs can not only build new public infrastructure, but collaborative partnerships between the public and private sector can produce long term operational cost savings as well."

Here are some of the steps PFI partners can take to assist a collaborative approach, according to David Archer:

1. Be open about your objectives.
2. Ensure the contract incentivises all parties to invest in solving joint performance problems.
3. Be clear about where the boundaries of responsibility lie.
4. Agree a dispute resolution process.
5. Maximise communications.
6. Be challenging about your own business processes.
7. Staff needs a role model of collaborative leadership – from the top.

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