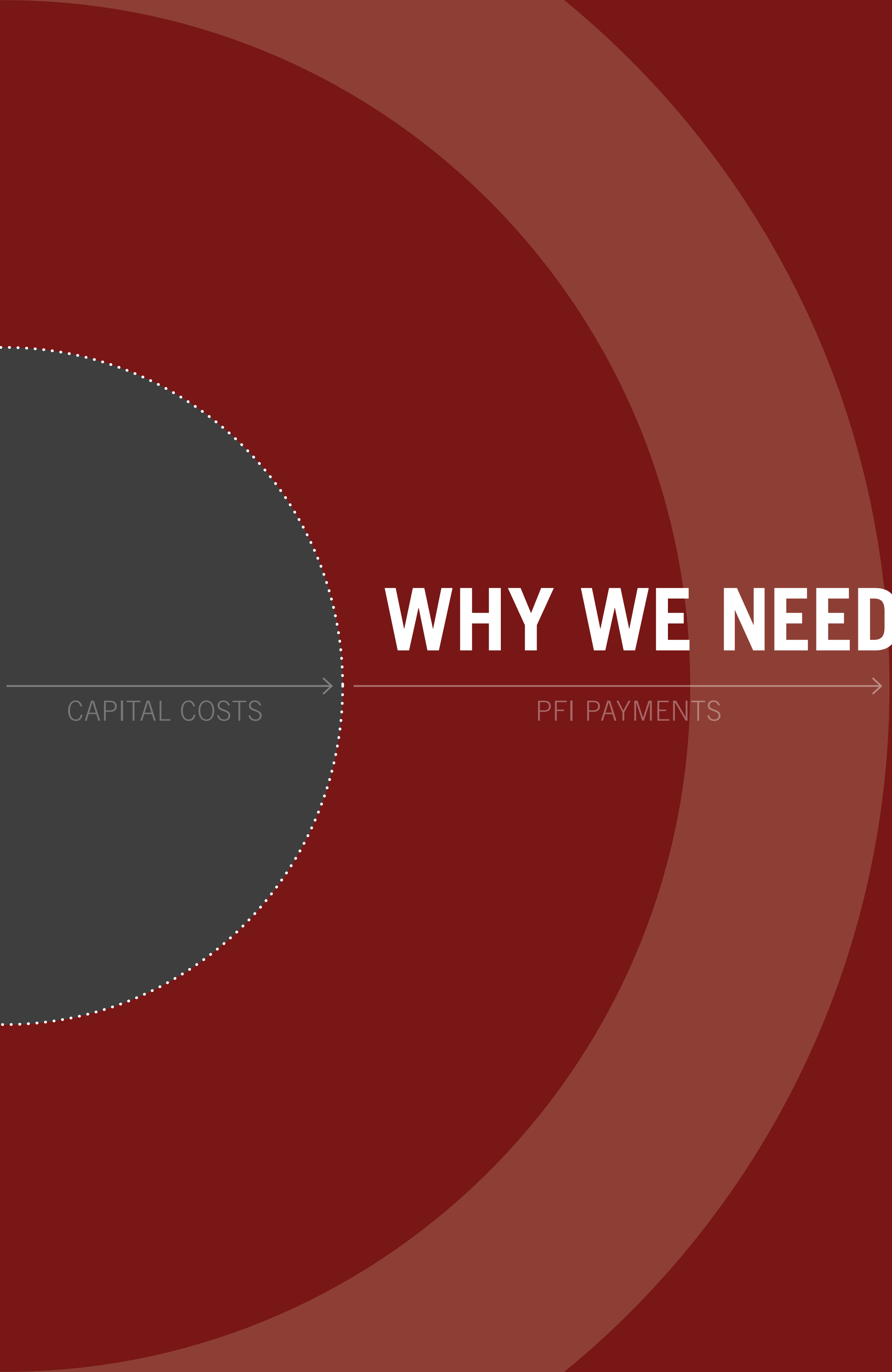

WHY WE NEED ACTION ON PFI IN THE NHS

ARGUMENTS FOR AN INCOMING GOVERNMENT

> It is not right for our generation to tie our children's and grandchildren's hands by saddling them with debts and service agreements 30 or 40 years into the future.

Margaret Hodge, Chair of the Public Accounts Committee, 2012

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What are the risks of non-action on PFI?

RISKS	EVIDENCE / EXAMPLES
More trusts will be forced into making large cuts in services and staffing by their unaffordable PFI deals. These hospitals will be the most exposed during periods of funding pressure as PFI costs rise year on year.	An end of year deficit of £60m at Bart's Health Trust in London has led to plans to cut nursing staff and wards. It spends 10% of its income on PFI. Two thirds of the NHS trusts in deficit have PFI debts. 15 trusts spent over 5% of their income on PFI. Five divert over 10% of their income to PFI (2013) Two thirds of **A&E closures** and proposed closures have been made at PFI hospitals. 25% of trusts believe they will not achieve foundation trust status due to debts (NAO 2011)
More PFI hospitals will need long-term government assistance to remain "viable". The link between PFI and debt has been proven. It is inevitable that more trusts will be sucked into a cycle of deficit.	16 PFI trusts ended the year in deficit, a further two were kept in surplus by government hand-outs. 6 out of 22 "at risk" PFI trusts, analysed by the Department of Health, were viewed as "unviable" in 2011. This number is likely to grow especially in periods where PFI repayments grow faster than income. Currently the government has committed a pot £1.5bn for 7 trusts with the worst PFI debts but this sum is likely to rise. The National Audit Office and Audit Commission reported a higher incidence of deficits amongst bodies with PFI schemes than those without.
PFI debt will lead to further controversial reconfiguration plans, affecting other hospitals and will distort health planning.	South London Healthcare trust accumulated debts of £150 million. Its PFI arrangements were blamed by ministers and the trust has since been dissolved. Part of the solution involved downgrading other nearby hospitals including the A&E and maternity services at Lewisham. High profile public campaigns involving legal action to stop local NHS changes have been successful in Lewisham, Liverpool and Gloucestershire.
More NHS funding will be drained off in excessive PFI profits and tax avoidance, at a time when "hard choices" are being proposed to the public due to NHS funding pressure.	85% of PFI hospitals are now owned by international investment companies, after opportunities for large, low risk profits created a market in PFI. These investment funds have bought equity in PFI contracts and offer investors returns 30% higher than the stock market. 60% of PFI hospitals are owned by investment funds working out of tax havens.
Further NHS trusts will take on PFI commitments that are unaffordable.	Peterborough and Stamford NHS trust used 'hopelessly inaccurate' projections to sign an **unaffordable contract**, National Audit office concluded. The DoH found that 6 out of 22 at risk schemes they examined were "unviable".
Loss of control of hospital buildings and land.	The government claims that all PFI land and assets revert to the public sector after the deal ends but in the case of at least five large PFI deals this is not the case. Despite collectively making £2.7bn in PFI payments and the debt being paid off, these five hospitals will not own the land or buildings as their leases will still be held by the private sector.
Loss of international financial credibility.	"PFIs are storing up costs for future generations," says Angus Hanton, co-founder of The Intergenerational Foundation. "And such build-ups clearly put Britain's AAA credit rating at risk by adding over a quarter to the country's £1 trillion national debt."

Political risks of not acting on PFI

RISKS	EVIDENCE / EXAMPLES
A future Labour government could be blamed for the negative impacts of PFI as they continue to affect hospitals and their patients. The plight of struggling hospitals will continue to attract media coverage. PFI started under John Major's government, but was vastly expanded under Labour and without further action it could be that Labour that takes the blame.	The Conservatives have already attempted to attribute the problems of PFI to Labour. "We've been working to expose the mess Labour left us with, and the truth is that some hospitals have been landed with PFI deals they simply cannot afford. Like the economy, Labour has brought some parts of the NHS to the brink of financial collapse." – Andrew Lansley The Daily Mail: "The **government blames** much of the debt on botched PFI deals which were encouraged by the Labour government." Responding to critical reports by the Treasury and Public Accounts Committees the government has rebranded future PFI schemes (PF2). A government review is attempting to find savings of £1.5bn across all PFI schemes in all sectors. But so far has only achieved £61m in NHS schemes, a drop in the ocean (0.09%) of the overall scale of PFI payments and does very little to address the poor value of PFI.
As PFI costs rise the next government will have to prop up PFI schemes to an even greater extent. This could be viewed as unacceptable waste at a time of heightened sensitivity around public spending.	The government has created a £1.5bn fund to pay the PFI costs of seven "unviable" schemes. 22 were examined as part of this review and as PFI costs rise it is inevitable that more trusts will struggle to afford payments.
PFI debt worsens the financial position of the NHS, adding weight to the argument that the funding model of the NHS is unsustainable and that the public should be charged directly for more services.	"All else has failed, **we have to liberalise the NHS**" – Spectator "**Cap on number of GP visits** being considered by Tories" – The Independent "**Paying £10 to see your GP** will help raise billions for the NHS" – The Express
Public awareness about the problems of PFI is increasing, non action will guarantee future criticism.	65% think the "NHS is under threat from private companies" YouGov poll: "**Nationalize energy and rail** companies say public." "The public's attitude has **hardened against private providers** running healthcare services, a poll has found."
Unpopular reconfiguration driven by PFI debt will fuel public criticism and will be a spur for public campaigns.	Legal action initiated by local people in Gloucestershire, South London and Liverpool has been successful in stopping or delaying NHS changes.

What are the benefits of taking action on PFI?

BENEFITS	EVIDENCE / EXAMPLES
Taking action on PFI will create considerable savings, releasing pressure on 100 NHS hospitals.	Renegotiation, refinancing and buy-out are all options which have produced substantial savings where they have been tried. However each deal will have to be considered separately to find the best way to achieve savings.
It will provide an opportunity to develop new forms of procurement which will provide more services for the sums invested.	The National Audit Office has confirmed that the cost of debt finance has increased since the credit crisis by 20 per cent to 33 per cent and now recommends that, "in the current climate, the use of private finance may not be as suitable for as many projects as it has been in the past. An analysis produced for the Treasury committee showed that "paying off a PFI debt of £1bn may cost the same as paying off government debt of £1.7bn. This would mean that a 70 per cent increase in investment could be achieved for the same long term cost if government funding were used instead of private finance."
Action on PFI is a key part of the plan to repeal the market, save the NHS and promote its long term security.	By reflecting the full liability of PFI in the nation's finances, the government could remove the incentive to pursue it. Clearly this would help to generate more effective and better value forms of public procurement. Market competition threatens the income of hospitals and under the tariff system PFI hospitals are underfunded. Better planning will result. Hospitals could gain more flexibility in changing services. Reconfiguaration of services could be led by patient need and not the management of PFI debt.
Taking action will prevent further hospitals from falling into debt crisis and prevent Lewisham-style controversy around local cuts.	The plight of struggling hospitals attracts public concern and wide media interest. The long list of media coverage on the Save Lewisham hospital campaign website confirms this. "Jeremy Hunt's decision to downgrade A&E services at Lewisham Hospital 'unlawful', rules court" - Evening Standard
Gain votes in marginal constituencies as failing hospitals with PFIs are in a number of these.	New research has revealed that 21 struggling NHS trusts will be located in marginal constituencies at the next election following a review of constituency boundaries. Seven are already on the government's PFI "at risk" list.
Visible action to reduce corporate exploitation of public contracts and tax avoidance are both popular with the public and could help to generate public funds.	"**Fury at corporate tax avoidance** leads to call for a global response" – Guardian "Two out of three (66 per cent) Britons now believe tax avoidance to be morally wrong" Poll Digest – Christian Aid **Tax Avoidance Poll** "Tackling tax avoidance is the key to **solving public debt** problems"

Why action must be taken on PFI

1. Securing the future of the NHS

Devising a plan to adequately fund the NHS will be one of the greatest challenges for the next government. Discussions around a projected funding gap of £30bn are intensifying as the implications are being realised. This new crisis comes despite the current efforts of the NHS to find £20bn worth of savings. Further **productivity gains** will be even harder to find. It is therefore crucial to take advantage of potential savings that could be made by addressing the excessive cost of PFI.

At present we will spend around £80bn of public money on hospitals that cost £12bn to build. So far £14.5bn has been paid over. Given that many of these deals have been criticised for their poor value then there is a strong case for making more effort to reduce the future costs. This could help to release the pressure on our hospitals. In real terms taking action on PFI could prevent large service cuts, stop PFI debts from distorting local planning and lessen the call on taxpayers for extra funding.

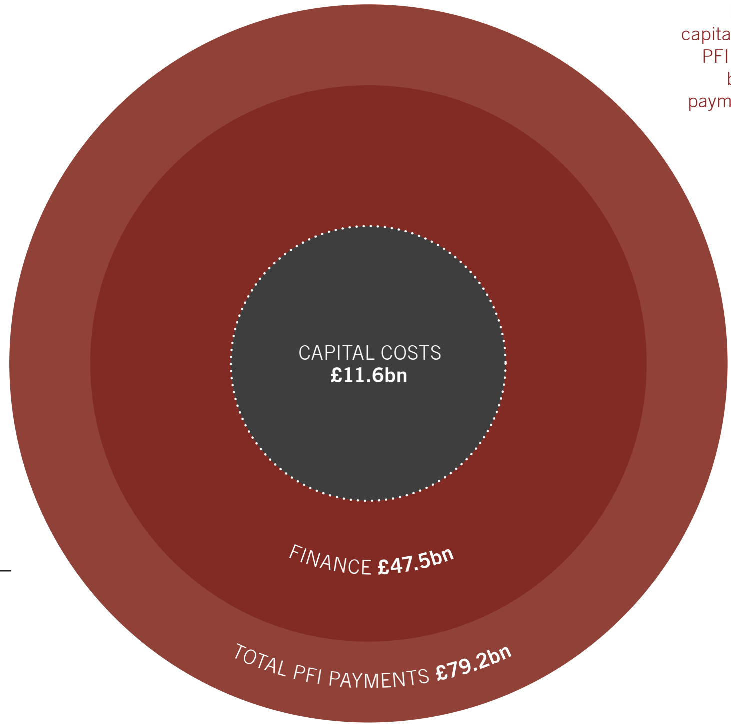


Figure 1: The original capital costs of all the NHS PFI projects are dwarfed by the estimated total payments over the lifetime of the deals

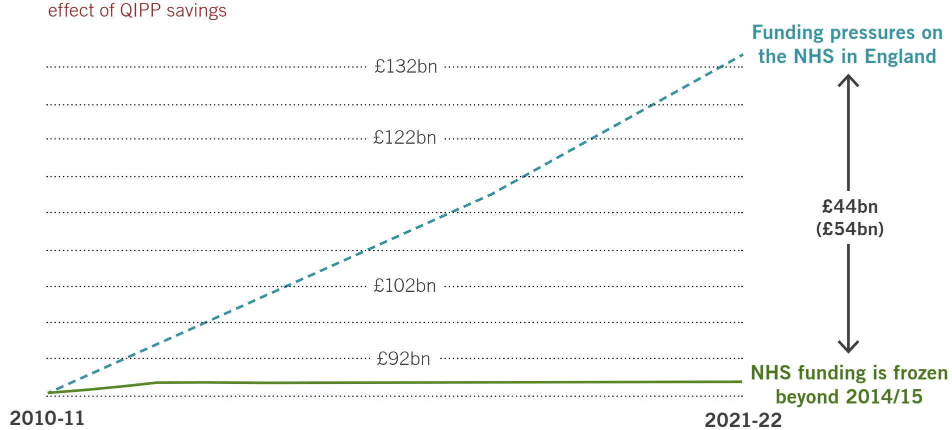
“If we were simply to carry on as the Labour party did in government, we would be seeing hundreds of millions of pounds every year being taken from what could provide improving services for patients in order to pay for PFI projects that roll forward for decades.”

Andrew Lansley, speaking on BBC Radio 4’s Today programme

The situation is urgent. Tim Kelsey, NHS England’s information director and a former Cabinet Office adviser on data, said the health service faced a £30bn funding gap by 2020. In an interview with Health Service Journal he said, “We are about to run out of cash in a very serious fashion.” The full position was outlined in a report by the Nuffield trust – ‘A decade of austerity?’[1]

In a wider sense, the failure of PFI is affecting the survival of the NHS. Its drive towards debt helps those who argue that the funding model of the NHS is broken and that we should all take more personal responsibility for paying for our healthcare. Like the impact of the market structures, PFI has been stitched into the NHS and now undermines some of its core advantages. Addressing PFI and the market in the NHS will ultimately make our NHS more sustainable.

Figure 2: The funding gap by 2021/22, assuming English NHS funding rises as set out in the 2010 Spending Review to 2014/15 and is frozen in real terms after, and without the effect of QIPP savings



1. www.nuffieldtrust.org.uk/sites/files/nuffield/121203_a_decade_of_austerity_full_report_1.pdf

Why action must be taken on PFI

2. PFI traps hospitals into a cycle of financial decline

As public finances tighten PFI hospitals are the most exposed. They are locked into rising spending on PFI at a time when their income is uncertain. The link between PFI and debt is already proven – in 2013/14 two thirds of the trusts that finished the year with deficits had PFI deals. Back in 2006 both the National Audit Office and the Audit Commission reported a higher incidence of deficits amongst bodies with PFI schemes than those without.[2] Without more stringent action more PFI hospitals will be pulled into debt and possible financial failure.

The government has already committed £1.5bn to bail out seven trusts with PFI payments that they can't meet. This came after a government review of a list of 22 at risk PFI trusts . There are identifiable reasons why the financial situation will get worse for these and other PFI trusts.[3]

1. PFI payments increase year on year, often by more than inflation as highlighted by Jim Cuthbert.[4] Meanwhile trust income is less secure and currently subject to pressure from competition and demands for large efficiency savings.

2. Under the current market arrangements PFI hospitals have to work harder to achieve financial success as they are unfairly funded through the NHS tariff system [Figure 3].

Figure 3: A selection of trusts whose PFI payments have been a rising percentage of their overall revenue. PFI hospitals have to work harder under Payment by Results. Trusts receive most of their income through a standard tariff for treatments, which includes an element for capital costs based on 5.8% of trust income. However, the capital costs of trusts with PFI schemes average 8.3%, with the result that they are under-funded.

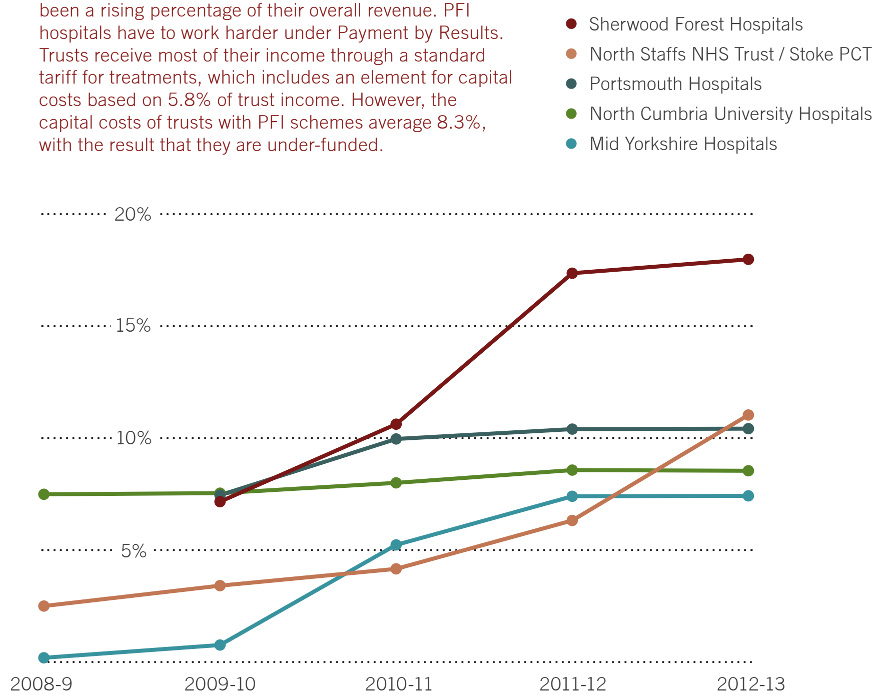
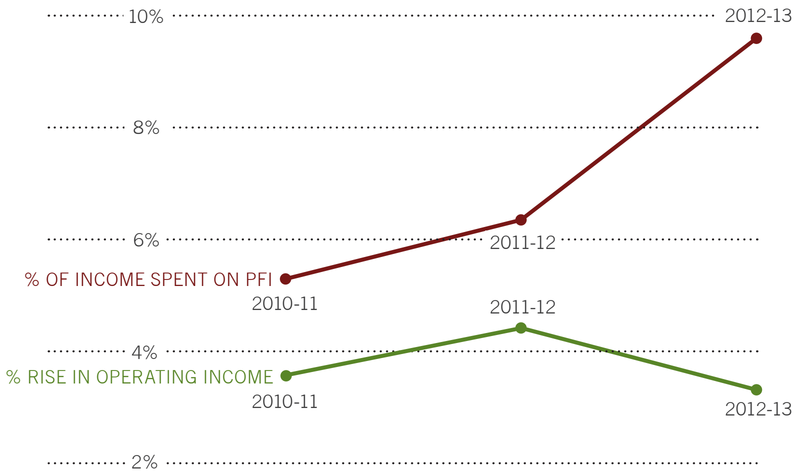


Figure 4: Hospital income is not rising as fast as PFI costs.



2. National Audit Office and Audit Commission (2006) Financial Management in the NHS: NHS (England) Accounts 2004–05, London: www.nao.org.uk/publications

3. http://www.bbc.co.uk/news/health-15010279

4. http://www.cuthbert1.pwp.blueyonder.co.uk/papers%202/c_invest-JimandMargaret Cuthbertsubmission1.pdf

Why action must be taken on PFI

3. PFI savings can be made

POOR VALUE?

The evidence about the value of PFI provides a powerful justification for taking action. The Treasury Committee concluded in their 2011 report that, “the price of finance is significantly higher with a PFI.” It was described by researcher Jim Cuthbert as “a one hospital for the price of two policy”,[5] reflecting the findings that PFI finance charges are 1.5-2 times greater than those for public borrowing.

PFI is also partly funded by equity. This involves a return for equity holders and adds an additional cost on top of the loans. The overall cost of capital (weighted average) across similar PFIs is now in excess of 8.5%. This compares to the current long-term government gilt rate of just over 4%.[6]

The supporters of PFI still say that it provides good value as it transfers risk from the pubic sector. However the Treasury select committee concluded that PFI was no more efficient than other forms of borrowing and it was “illusory” that it shielded the taxpayer from risk.

> **“It is a bit like taking out a pretty big mortgage in the expectation your income is going to rise, but the NHS is facing a period where that is not going to happen. Money is being squeezed and the size of the repayments will make it harder for some to make the savings it needs to. I don’t see why the NHS can’t go back to its lenders to renegotiate the deals, just as we would with our own mortgages.”**
>
> John Appleby, Chief Economist at The King’s Fund health think-tank

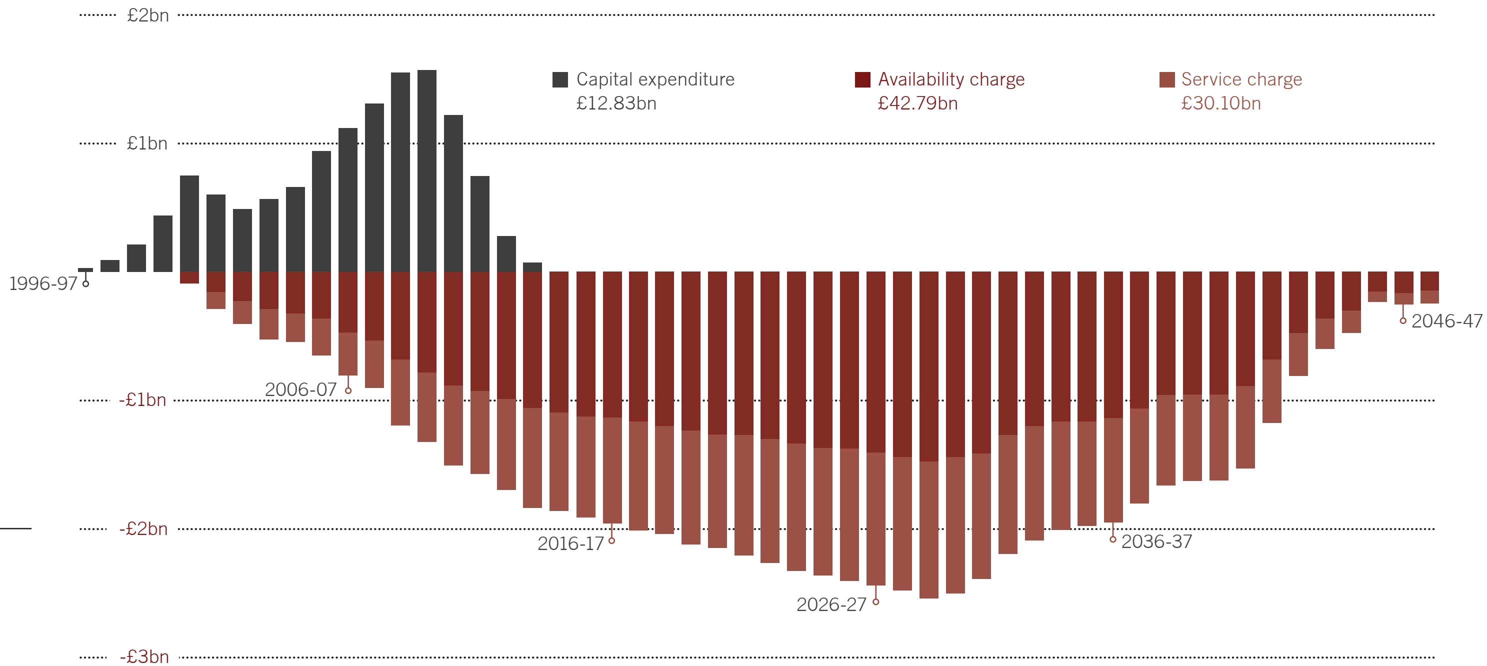


Figure 5: Capital expenditure and unitary payments for signed NHS PFI contracts. These payments include an availability charge and a service charge. The availability charge covers interest and principal payments on the PFI debt and an accumulation of cash reserves to meet life-cycle costs (e.g., maintenance and upgrade costs). The service charge covers facilities management (e.g., cleaning, IT, security).

5. http://www.socialpolicy.ed.ac.uk/__data/assets/pdf_file/0008/64358/AAA_PFI-PPP_Booklet_12-08.pdf

6. http://www.publications.parliament.uk/pa/cm201012/cmselect/cmtreasy/1146/114606.htm#n44

Why action must be taken on PFI

TIME FOR A NEW APPROACH

So far the government has achieved only minimal PFI savings of £61 million, which is just 0.09% of the total unitary charge remaining on PFI in the NHS – a drop in the ocean.

With many NHS trusts in dire financial circumstances, it is time to look at other measures to save money in the long-term and recoup a proportion of the excessive profits made by the private companies involved. The options under discussion include the following:

- Renegotiating the PFI contracts to reduce the annual payments either to be closer to that which would have been paid if public money had been used or at least to some 'fairer' level. Whether such negotiations should cover retrospective changes to the deals or not should be considered
- Buy out of the PFI contract either through the use of reserves or through borrowing from a different, much cheaper, source;
- A tax on the profits made by companies that sell their PFI shareholding;
- Closure of the loophole that allows companies not domiciled in the UK to hold share holdings in PFI contracts leading to increased tax payment.

0.09%

A DROP IN THE OCEAN

So far the government has achieved £61 million of PFI savings, which is just 0.09% of the total unitary charge remaining on NHS PFI

RENEGOTIATE PFI DEALS

In 2010 management consultants McKinsey & Company noted that a reduction of 0.02%-0.03% in interest charges paid to the contractors by NHS hospitals could save £200 million a year. Research by Cuthbert shows that there is wider scope to make savings. PFI payments are indexed[7] and increase annually, often above inflation. Meanwhile the outstanding loan is decreasing, creating rising profits for PFI companies.

Most of the risk in PFI is within the construction phase. In nearly all PFI schemes the original PFI partners including the construction companies have sold on their equity to other investors, who are still taking large profits but did not bear any of the major risk. Andy Friend, ex CEO of major PFI builder John Laing, stated in his evidence to the Treasury committee, "that once the construction stage had been completed and the operational stage had started there was a case for allowing the public sector to refinance the debt. This has been done in some cases."[8]

Public opinion could be harnessed to help bring companies into negotiation. There is growing public realisation that the original deals were unfair, with excessive profits being made, but not much tax paid due to the use of offshore companies. The reality that PFI schemes are draining large sums of public money away from services that are struggling for funding, provides a justification for seeking to renegotiate deals down to a fair value.

"£200m a year could be saved"

McKinsey & Company

EXAMPLES OF REFINANCING AND PUBLIC BUYOUTS

In August 2012 Northumbria Healthcare reported that it had been given in-principle approval buy out for two PFI schemes using a £120 million loan from the local authority. The trust estimated that it will save around £4.7 million per year on the combined cost of its two PFI schemes, which each have more than eighteen years left to run, according to Treasury data.

In February 2011, Esk and Wear Valleys Mental Health Foundation Trust paid off its PFI contract for the rebuilding of West Park Hospital in Darlington. The 30 year contract meant the Foundation Trust would eventually have paid £32.15 million for the hospital; by buying out of the deal the Trust paid just £18 million to release itself from the contract, saving the trust £2 million a year or around £14 million over the lifetime of the contract.

7. http://www.cuthbert1.pwp.blueyonder.co.uk/papers%202/c_invest-JimandMargaret Cuthbertsubmission1.pdf

8. http://www.publications.parliament.uk/pa/cm201012/cmselect/cmtreasy/1146/1146.pdf

Why action must be taken on PFI

4. Alternatives to PFI will create more services

With tight times for the public finances ahead we urgently need to replace PFI with procurement methods that offer far better value.

PFI COSTS HAVE RISEN AGAIN

The National Audit Office has stated that the cost of debt finance has increased since the credit crisis by 20 per cent to 33 per cent and now recommends that, "in the current climate, the use of private finance may not be as suitable for as many projects as it has been in the past." The Treasury Committee enquiry reported that, "all witnesses agreed that the differential between government debt and private project finance was significant and that it had increased since the financial crisis."

"Paying off a PFI debt of £1bn may cost the same as paying off government debt of £1.7bn."

House of Commons Treasury Committee Report on PFI, 2011

The NAO also called on the Treasury and departments to identify alternative methods for delivering infrastructure and related facilities services, building on the lessons learnt from PFI, to maximise value for money for government.

"PFI IS A POLICY OF ONE HOSPITAL FOR THE PRICE OF TWO"

Dr Jim Cuthbert

BETTER VALUE AVAILABLE FROM PUBIC BORROWING

An analysis produced for the Treasury Committee showed that, "paying off a PFI debt of £1bn may cost the same as paying off government debt of £1.7bn. This would mean that a 70 percent increase in investment could be achieved for the same long term cost if government funding were used instead of private finance."

"PFI is less likely to be value for money unless there are substantial and credible savings to off higher financing costs."

National Audit Office

According to the conclusion of the Treasury Committee's report, "Replacing some PFI with direct public sector investment would not necessarily result in a higher financial liability for the Exchequer. It would mean that the debt was more transparent [...] An increase in government debt to replace PFI investment should also not necessarily make it any harder to meet the fiscal mandate. Continuing to use an inefficient funding system such as PFI is likely in many cases to increase the overall burden on taxpayers for the provision of public sector capital projects. If, rather than using PFI, the lower financing costs of government are utilised, we have seen evidence that investment can be increased significantly for the same long term funding costs."[9]

9. Treasury Committee, Private Finance Initiative, 17th report of 2010-12, HC 1146, August 2011, para 89

Why action must be taken on PFI

5. PFI causes service cuts and distorts planning

The burden of meeting PFI costs and the push to use PFI above other forms of funding has had a serious impact on the level of services.

A study of the first wave of PFI hospitals found that bed numbers were reduced by an average of 30% in the new hospitals. Research by the Telegraph found that the majority of proposals to close A&E units occurred at PFI hospitals.

30%
of cuts in bed numbers occurred in the first wave of PFI hospitals

TWO THIRDS
of A&E closures and proposed closures come from PFI hospitals

NHS trusts in London and in the Midlands are amongst those who have made cuts in staffing and closed units to help meet PFI obligations. Queen Alexandra Hospital in Portsmouth cut 700 jobs and closed 100 beds while "seeking to manage annual hospital running costs of £40million." The British Medical Association's consultants' committee has said that PFI debts are "distorting clinical priorities" and impacting the treatment given to patients.

"We now have indexed payments for the next 35 years which at a time of growing concern over NHS budgets can only be a millstone. It isn't just that our scheme was expensive. Its very existence distorts whatever else needs to happen in this part of London and beyond."

Peter Dixon, Chairman of University College Hospital, 2009 writing in the Guardian

The perilous financial state of a PFI hospital can also impact upon neighbouring units. South London Healthcare Trust accumulated debts of £150 million. PFI was blamed by ministers and the trust has since been dissolved. Part of the solution involved downgrading other nearby hospitals including the A&E and maternity services at Lewisham. This was subsequently resisted after a strong public campaign but proves how neighbouring hospitals can be sucked into process of coping with PFI debt. A key argument against this plan was that both clinicians and the public felt that it was based on financial factors not the best interests of patients.

"Each wave of PFI has been associated with trust mergers, leading to 30% reductions in beds; staff lay-offs; and closures of hospitals, accident and emergency departments and an untold number of community services – all because of lack of affordability."

Allison Pollock, Professor of Public Health Research and Policy, Queen Mary, University of London

Why action must be taken on PFI

6. PFI creates excessive profits at taxpayer's expense

Huge profits are being made by the private companies investing in PFI. Firstly by the building companies and the initial lenders and then by investment companies who have brought shares in the schemes because of the large, low risk returns. 85% of PFI hospitals are now owned by international investment companies, who control the Special Vehicle companies that run each PFI scheme. They offer investors returns 30% higher than the stock market.

"Tax revenue is being lost through the use of off-shore arrangements by PFI investors."

Public Accounts Committee Report 2011

After publishing their 2011 report in to PFI, Margaret Hodge Chair of the Public Accounts Committee commented, "We have even seen evidence of excess profits being priced into projects from the start [...] The Treasury review must find a private finance funding model that allows flexible delivery of public services and ends the era of investors receiving eye-wateringly high rewards while taking ever decreasing risks."

PF2 is essentially a rebranding of PFI. It does nothing to address profiteering from equity sales in PFI."

Dexter Whitfield, author of *The PPP Wealth Machine*

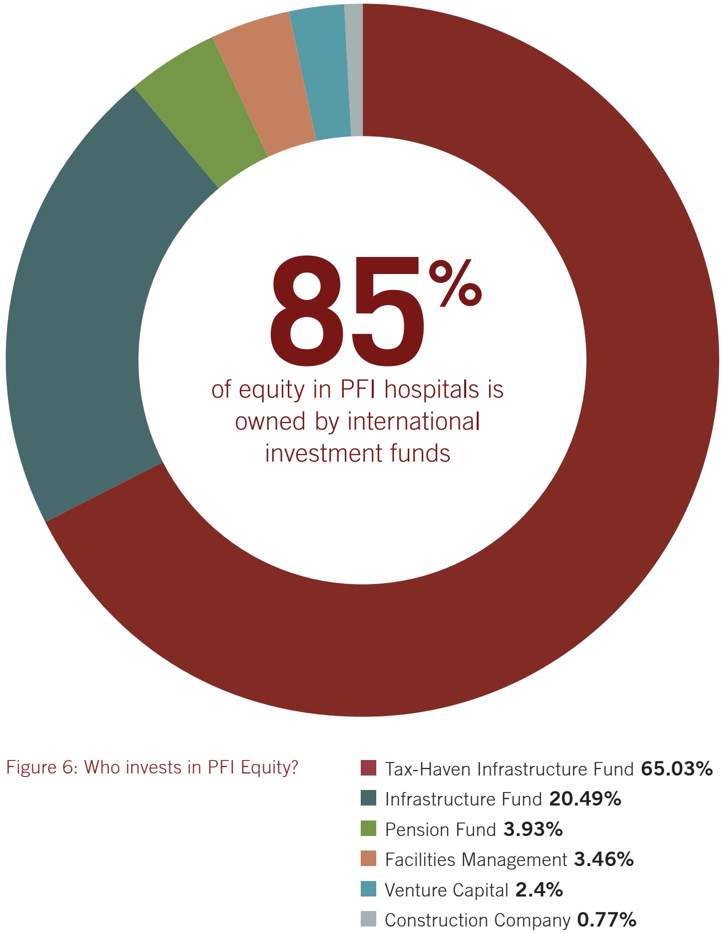


Figure 6: Who invests in PFI Equity?

Why action must be taken on PFI

7. PFI is a failing policy with a declining public reputation

After damning public reports in 2011 from the Treasury Committee and the Public Accounts Committee, George Osborne called PFI "discredited." Ministers blamed Labour and put the policy on hold. A year later PF2 was launched – a new version of PFI with what the Financial Times described as "minor changes", leaving many of its fundamental flaws in tact.

"The new system is likely to still transfer all the problems with the old PFI such as the lack of real risk transfer, large private profits and a lack of transparency," said Margaret Hodge, chairman of the Public Accounts Committee.

With public finances under pressure politicians from all sides are calling for better value. Former Tory health secretary Stephen Dorrell said that private companies making high profits should take a "haircut" when things go wrong. And yet PS2 and the accompanying review has so far failed to disturb the large scale profit making from PFI, achieving only a 0.09% reduction in PFI costs for the NHS.

PUBLIC MOOD CHANGING

Surveys show that there is growing public concern with corporate involvement in the NHS. "Two out of three Britons now believe tax avoidance to be morally wrong," according to a survey carried out for Christian Aid; and 65% think the "NHS is under threat from private companies."

In response to the impact of privatisation, growing numbers of people also now want to reverse the policy: "Nationalise energy and rail companies, say public," a YouGov poll reported recently.

Despite the "significantly higher cost of finance", the Committee said it had not found "evidence of savings and benefits in other areas of PFI projects".Instead, they found that the "design innovation was worse in PFI projects and we have seen reports which found out that building quality was of a lower standard in PFI buildings."

The Daily Telegraph reporting the Treasury Committee Enquiry

LOSS OF CONTROL OF RESOURCES

The government claims that all PFI land and assets revert to the public sector after the deal ends but in the case of at least five large PFI deals this is not the case. Despite collectively making £2.7bn in PFI payments and the debt being paid off, these five hospitals will not own the land or buildings as their leases will still be held by the private sector.

The DoH said five out of the 43 large deals it has signed to date have leases, which confers ownership of the hospitals' land and assets, that go beyond the length of the PFI contract. These five hospitals are:

Queen Elizabeth Hospital in Greenwich, south-east London [£93m]

Darent Valley scheme in Dartford, Kent [£177m]

Cumberland Infirmary in Carlisle [£87m]

Hereford County Hospital [£64m]

University Hospital in Durham [£96m]

65%

of people think the NHS is "under threat from private companies"