

## **PFI SCHEMES – A TYPICAL STRUCTURE**

The Private Finance Initiative (“PFI”) has been part of the government’s procurement strategy since 1992, yet many in the construction industry remain uncertain of how such schemes are structured and how they can get involved. The aim of this article is to outline the typical structure of such schemes and identify how organisations in the construction industry can become involved in this large market.

In general PFI schemes have capital values over £15 million, albeit that a very small number have been for sums less than this. Since 1992 there have been over 300 schemes started with a combined capital value over £38 billion.

So how do these schemes come about and who can get involved?

The schemes are initiated by the public sector, typically for the provision of hospitals and health schemes, schools, transport projects, fire and police stations, prisons and waste and water projects. The scheme usually involves the private sector providing, say, a building, either new or refurbished, which will be maintained by the private sector for a specified period, typically 20 or 25 years. The public sector pays for the project by means of a unitary charge, e.g. a set rate per bed per year for a hospital.

The public sector body (usually known as the Authority) lets a single contract to a company who will provide the finance, design, construction and maintenance of the scheme. This company is often referred to as the Project Co, which itself is a Special (or Single) Purpose Vehicle (“SPV”) set up specifically for this scheme. Such SPV’s are usually set up and owned by one of the larger construction groups who work in this area of the market. It is the SPV that then enters into a series of contracts to facilitate the finance, design, construction and maintenance of the scheme. The group that owns the SPV usually acts as guarantor for its performance to the Authority and possibly the funders but not to the contractors and sub-contractors who get involved in either the construction or the maintenance.

Finance is generally obtained from the banking sector who in return for providing the necessary funds will inevitably attempt to influence the level of risk passed down the contractual chain so as to limit the risk carried by the SPV thereby seeking to ensure the likelihood of the funds being repaid. Any other comment in respect of finance arrangements is outside the scope of this article.

Typically, the SPV will then enter into two contracts, one with a Construction Contractor for the design and construction of the project and a second with a Facilities Management Contractor for the maintenance of the scheme after practical completion of the construction (but excluding defects liability). It is not



unusual for both the Construction Contractor and the Facilities Management Contractor to be part of the construction group that owns the SPV.

To summarise at this point, the Authority enters into a single contract with the SPV (Project Co). The SPV then enters into three contracts, for (i) finance, (ii) design and construction, and (iii) maintenance.

It is primarily from the second of these three contracts, i.e. the design and construction of the scheme that other organisations in the construction industry can obtain work as sub-consultants, sub-contractors or suppliers, either direct to the Construction Contractor or to one of the sub-consultants, sub-contractors or suppliers. The diversity of the supply chain from this point on knows no bounds.

Consultants, contractors, sub-contractors and suppliers who provide services to PFI schemes should be aware that there are no standard forms of contract in use in this sector of the market. Due to the diverse nature of the arrangements entered into the contracts tend to be bespoke and tuned to the requirements of every scheme. As stated above this is often influenced by the funders' perception of the risk involved in each scheme and its approach to the terms of the funding in relation to the contracts let by the SPV. The Construction Contractor and the Facilities Management Contractor may then seek to pass this risk down the supply chain albeit that they do accept some of the risk if they consider the financial incentive sufficient or that the supply chain is incapable of carrying such risk at an economic price. It is not unknown for standard contracts such as DOM/2 to be used as the basis for these sub-contracts but be aware of the amendments which effectively turn such sub-contracts into bespoke documents.

What appears to have emerged as a common theme is that organisations entering into sub-contracts or sub-consultancy agreements in relation to PFI schemes need to be aware of the level of risk they are being asked to take. To this end professional advice in assessing the risk prior to a contract being entered into usually proves to be worthwhile.

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