Enron auditors gave key thumbs up to PFI

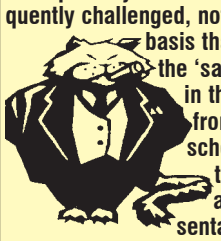
Andersen Consulting (now Accenture) separated in the UK from parent company Arthur Andersen in 2000. But prior to that, the company – now embroiled in the investigations into the collapse of US energy corporation Enron, had already established a position as a trusted advisor to the British government.

One of its reports, commissioned by the Treasury and published in January 2000 by the Office of Government Commerce, has played a key role in the Labour government's promotion of the Private Finance Initiative.

In collaboration with the consultancy arm of the London School of Economics ('Enterprise LSE') Andersen consultants wrote a report *Value for Money Drivers in the Private Finance Initiative*, which has been repeatedly cited by ministers seeking to back up their claims that PFI does in fact represent good value.

However Andersen's were hardly impartial or objective observers, since they were already involved in consultancy work on 32 PFI schemes covering hospitals, schools, roads and the controversial PPP project on the London Underground. The total value of the PFI/PPP deals in which Andersen has been involved exceeds £10.1 billion, and the company – like other private sector accountants, business consultants and lawyers – clearly stood to benefit from PFI continuing as government policy.

The validity of their key finding – that the budgeted costs of 29 actual PFI projects appeared to show an average saving of 17% over the projected costs of the schemes had they been publicly funded – has been frequently challenged, not least on the basis that 50% of all the 'savings' reported in the study came from just one scheme, making the 17% "average" unrepresentative.



In fact the report does not compare actual costs, but *projected* costs, contrasting a hypothetical public sector comparator (PSC) with the planned cost of the privately-funded project.

But an equally serious flaw in the argument is that 60% of the claimed 'savings' are based on the highly contentious notion that "risk" is transferred from the public to the private sector. Most of this claimed "saving" is undefined.

Despite these and other obvious flaws, the Andersen Report has been widely touted by Labour ministers, including Health Minister John Hutton and Treasury Secretary Andrew Smith, desperate to show evidence that PFI is a good deal for taxpayers. As Lib Dem spokesman Matthew Taylor pointed out in the Commons on June 21 last year:

"The Government always quote the Arthur Andersen report because it is the only one to support their position. The survey was based on expected savings, rather than delivered savings."

With fresh questions being asked over the competence and independence of the Arthur Andersen organisation, perhaps ministers may be wondering whether they too should have been putting at least one of its documents in the shredder.

1962 and all that, 40 years on

Which is the biggest ever hospital plan?

Oxford's John Radcliffe Hospital: one of the class of 1962

Labour ministers have repeatedly defended their policy of seeking to build hospitals using the controversial Private Finance Initiative by claiming that PFI has enabled them to embark upon the "biggest ever programme of hospital building in the NHS". But does their claim stand up to scrutiny? JOHN LISTER has been looking back at previous policies.

ALAN MILBURN's NHS Plan calls for a total of 100 new hospitals between 2000 and 2010.[1] On the face of it, this would appear to be bigger – and indeed the sums of money involved in such an investment programme are obviously larger – than the previous major programme of hospital modernisation, the 1962 Hospital Plan for England and Wales, almost exactly 40 years ago.

1948: Nye Bevan lays a foundation stone for a new health centre: but capital investment was minimal in the early years of the NHS

That scheme, eventually approved by the then Conservative government on the urgings of then Health Minister Enoch Powell, spelled out proposals for 90 new hospitals and another 134 major redevelopment programmes.

The 280-page Plan also listed a further 356 schemes costing over £100,000 each (equivalent to almost £500,000 today) and also acknowledged the need for many more smaller schemes "which represent a large volume of modernisation and upgrading". [2]

The Hospital Plan initially costed its programme at £707 million – the equivalent of £2.85 billion today. But this was almost three quarters of the entire NHS budget of that year (£971m) – so it might be argued a similar proportional share of spending today would amount to a £30 billion-plus investment in new hospitals, far bigger than Milburn's plan.

£500m was to be to be spent between 1962 and 1971 – an average of £50m a year, more than double the going rate at the time. Indeed the Conservative election manifesto had included a commitment to double the NHS capital programme, while Labour in opposition had called for spending of £50m a year. [3]

The Hospital Plan recognised that such a massive leap in public investment would represent a major change of policy, after years in which NHS capital to modernise the aged building stock nationalised in 1948 had been in desperately short supply.

In 1962 the government was spending just over half the current share of national wealth on the NHS, just 3.4% of GDP – compared with just over 6% today.

Within this limited pot of cash, NHS capital budgets in turn consistently accounted for less than 3% each year (though allocations had increased slightly, peaking at £24m in 1960-61). This was well below the level of around 5% that had been recommended back in 1956 by the Tory government's own Guillebaud Committee.

As a result, there was not enough capital to enable any substantial modernisation or even systematic repairs to buildings which were often unsuitable for modern medicine: 70% of hospitals taken over by the NHS in 1948 had fewer than 100 beds, and 20% of the building stock was found to be over 100 years old in 1962.

The situation called for a major change of policy: but perhaps surprisingly given Enoch Powell's right wing leanings, the entire 1962 investment programme was to be funded by the government from general taxation – and the completed hospitals would also be assets wholly owned by the NHS. There was no serious discussion of seeking the finance from elsewhere: the only debate within the Tory cabinet was over how much or how little should be invested in the modernisation of the NHS.

The Hospital Plan pioneered the concept of the District General Hospital of 600-800 beds covering a catchment population of around 150,000 as the key building block for acute (short stay) hospital services.

It involved a 6% reduction in numbers of acute hospital beds, but (reflecting the medical model of the time) a 35% increase in numbers of maternity beds. 1,250 hospitals – most of them small or very small – would close in the process.

Nation-wide

It also took an important step towards setting up a nation-wide plan and a coherent policy. It laid down norms for minimum levels of bed provision per head of population for each specialist service, and addressed the issue of staffing levels, both within the NHS as it then was, and within the Local Authority Health and Welfare Services (many of which are now council social services).

The Hospital Plan recognised that the schemes would take time to get up and running, and "assumed" spending of £200m in the first five years rising to £300m in the following five years. It accepted that "the sums which will eventually become available may be somewhat more or less, dependent on the state of the economy." In fact the costs were much higher than expected: but a change had been made.

By 1968 large schemes (carrying out building work costing over £1m a year) accounted for more than half of the NHS capital programme: there were 66 of these schemes – 6 of which were projects planned to cost over £10m. Capital expenditure that year was almost 10 percent of current NHS spending, and it continued to rise to a peak of 12.8% in 1973-4, before being cut back again to 9.9% in 1974-5.

Costings were distorted by high levels of inflation in the increasingly turbulent economic situation: but the new Royal Free Hospital with its tower block was completed in 1973 at what today seems an incredibly modest cost of £20m.

Only six new hospitals had been built between 1955 and 1965: but between 1966 and 1975 another 71 were started – and some completed, changing the shape of health care for a generation.

The 1970s saw a change in the economic climate, and a retreat by successive governments from investment, not only in the NHS, but throughout the public sector.

Government net capital spending plunged from a peak of £28.8 billion in 1974-5 to just £12.5 billion in 1979-80, and fell again to a nadir of just £1.9 billion in 1988-89. Only in one year during the 1980s (1983-84) did public sector capital investment reach £10 billion. And though it rose again briefly to double figures (with a peak of £14.2 billion in 1992-93), it fell back again sharply in the second half of the 1990s. (Figures are all at 1999-2000 prices)[4]

This cut in government spending was accelerated in the 1990s by the introduction of the Private Finance Initiative from 1992, which was accompanied in the case of the NHS by a steady reduction in government capital allocations. The 1995 budget projected successive cuts in NHS capital spending – by 17% in 1996-97, another 5% in 1997-98, and 6.5% the following year: PFI investment was supposed to increase year by year, from £47m in 1995-96 to

£300m in 1998-99. [5]

But PFI – and NHS land sales, which had become a regular feature of the Tory government's asset-stripping approach to the NHS – weren't the only ways in which governments found ways to claim to be investing generously in the NHS, while injecting comparatively little new capital.

During the mid 1990s the establishment of NHS Trusts within the Tory "internal market" reforms brought with it the introduction of capital charges to be levied on each Trust's land and property assets. This meant that a growing percentage of the NHS budget each year was generated internally from these "capital refunds".

Beginning at 1.2% of NHS total spending in 1993-94, these capital refunds steadily increased in scale as new Trusts were formed and more began paying charges on a greater share of their assets. By 1998-99 capital refunds amounted to a hefty 8% of the NHS budget. [6]

Less capital

So despite the appearance of allocating large sums for investment in new hospitals and other NHS facilities, and despite the apparent upturn in allocations since Labour took office in 19977, in practice the government has been injecting even less public capital for major hospital projects in real terms than the miserly amounts available in 1961.

Indeed in the two years 1997-98 and 1998-9, the injection of Treasury capital for Hospital and Community Health Services (HCHS) was more than outweighed by the cash generated from land sales and the refund to the government of capital charges paid by NHS Trusts on their assets.

Far from pumping in desperately-needed capital, the government effectively pocketed a surplus from existing NHS assets in these two years – of £139m in 1997-8 and £348m in 1998-9. [8]

The real figures are also disguised by the inclusion of PFI money under the general heading of "health capital investment" – of which it now makes up around a quarter of the claimed total [9]. However the extent to which PFI can be seen as "NHS investment" at all is not clear, given that the assets to be constructed will not belong to the NHS.

Instead the (inflated) cost of paying for the hospital projects financed through PFI will be met from NHS revenue budgets over the next 25-30 years. The "investment" is not a public sector capital asset, but a long-term public sector revenue liability.

Despite the claims by the DoH that PFI is simply "one of the weapons in our armoury of procurement tools", the pool of NHS capital is inadequate to offer Trusts a real choice of whether or not to seek private finance. This squeeze, tighter than ever since 1992, has meant that PFI has become seen by NHS managers as "the only game in town".

Only six major NHS-funded schemes, totalling less than £300m, have been given the go-ahead since 1997. This followed a long lean spell for NHS investment under the Tories: from 1980 to 1997, only seven publicly-funded schemes costing more than £25m were completed. [10]

By contrast, the Labour government has so far given the go-ahead to 38 PFI-funded NHS schemes totalling almost £4 billion, and aims to increase this to £7 billion by 2010.

A massive 85% of all new capital investment in the NHS is now coming from the private sector.[11]

Up go the girders: and with PFI, up go the profits for each new hospital – replacing NHS assets with private

Critics have argued that any short term benefits of PFI are outweighed by the long term costs. By 2007 the annual cost to the NHS of PFI payments involved in leasing these privately-owned, profit-making hospitals, and buying ancillary services from private contractors, will be in the region of £2.1 billion[12] – almost exactly the value of the entire NHS total gross capital expenditure last year.

Unlike the current capital charges, the payments to PFI consortia represent a net flow of cash and capital OUT OF the NHS and into the coffers of banks, building firms and their shareholders.

Together with capital charges, the total bill for leasing hospital premises from PFI consortia and capital charges levies by the government on Trust assets will add up to £4.5 billion a year. [13] This will become a first charge on the revenue of NHS Trusts – and thus squeeze the remaining budgets to finance patient care.

The PFI-funded £228m replacement for the Norfolk & Norwich Hospital is on a greenfield site on the edge of the city, and will cost £33.5m a year for 30 years.

In the longer run it is possible to see the process of renewal of NHS buildings through PFI leading towards a situation like that in social care, where the estimated value of assets involved is £13.3 billion, £10 billion of which are owned by the "independent sector".[14]

Of course such a process has a long way to go: the current estimated net book value of Health Authorities and Trusts is around £23 billion, with primary care assets valued at £2.2 billion. The estimated cost of replacement is over £75 billion.

But with NHS PFI projects likely to total £7 billion by 2007, inroads are being made, while existing NHS assets are still being sold off, (estate worth an estimated £1.58 billion has been identified as "surplus") while little new public investment is being injected to health care facilities and buildings.

The Department of Health's Investment Strategy points out that "One of the legacies of the under investment throughout the nineties is the sharp increases in backlog maintenance levels over the latter half of the 1990s. Between 1995-96 and 1998-99 backlog maintenance increased by around 40%. In 1998-99 it was £3.4 billion."

But this scale of backlog maintenance and the lack of NHS capital funding are used as the most potent arguments by Trusts seeking to justify embarking on costly and controversial new-build PFI schemes rather than refurbishing and redeveloping existing NHS assets.

The NHS has also fallen way behind European health services in levels of investment at every level – in medical staff, in hospital beds, and in modern diagnostic equipment.

The Investment Plan admits that the UK currently has just 7 CT scanners per million population compared with 20 in Germany and Italy and 15 in the Netherlands. And our hospitals have just 4 MRI scanners per million population, compared to Germany's 10 6 in Italy and 8 in the Netherlands. [15]

But the Strategy does not point out that our NHS also has fewer acute hospital beds per head of population than any OECD country other than Turkey. Only Turkey, Korea and Mexico have fewer physicians per head, and we are sixth from the bottom in numbers of practising nurses per head. [16]

A policy of investment for the future would focus on building, modernising and refurbishing a network of hospitals that would enhance the existing NHS asset base, rather than turning the country's most popular public service from a cash-strapped landlord into a cash-starved tenant in property rented from the private sector.

If PFI is allowed to remain the "only game in town" for the financing of the remaining hospital programme, Labour will not only fall short of the radicalism and public service commitment shown by Enoch Powell and the Tories in 1962, it will have substantially reduced and privatised the legacy of assets passed down from Nye Bevan in the formation of the NHS in 1948.

1 The NHS Plan, July 2000
2 Ministry of Health (1962) A Hospital Plan for England and Wales. HMSO.
3 Webster, C The Health Servics since the war, (1996) Vol 2 p99
4 HM Treasury, Budget 2001, Chapter C, Table C24)
5 "NHS's 1.6 per cent budget boost", DoH Press Release, Nov 28 1995.
6 The Government's Expenditure Plans 1998-1999, Fig 2.7.
7 Health Minister John Denham, Commons written answer, February 2 2000.
8 Gaffney D. Pollock A.M. Price D. and Shaoul J. "NHS capital expenditure and the Private Finance Initiative – expansion or contraction?" BMJ 1999 319; 48-51 (July 3).
9 The Government's Expenditure Plans 2000-01, Chapter 4, Fig 4.1.
10 Gaffney et al 1999
11 The Economics of the Private Finance Initiative in the NHS, by former Treasury advisor Jon Sussex, Office of Health Economics, April 2001
12 Will primary care trusts lead to US-style health care? Allyson Pollock, BMJ 322, 21 April 2001.
13 Ibid.
14 Departmental Investment Strategy, department of Health Nov 2000.
15 Departmental Investment Strategy, department of Health Nov 2000, p 14
16 OECD 'Health At A Glance', 2001.

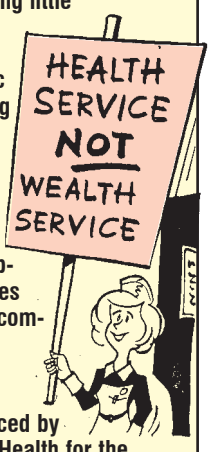
Publicly-funded NHS schemes: on budget and on time!

MINISTERS have claimed that financing new hospitals and NHS facilities using the controversial Private Finance Initiative represents value for money, despite costing more than publicly-funded alternatives – partly because, as they claim, PFI delivers projects "on time and to budget".

The implicit claim, (as stated in the PricewaterhouseCoopers report recently cited by Prime Minister Tony Blair) is that:

"traditional public sector procurement still suffers from delay, cost overrun and compromise on initially planned requirements."

Yet the government has gone over so enthusiastically to PFI as the means of funding 85% of NHS capital investment, that few public sector projects of any size have been agreed in the last five years, giving little base on which to assess the efficiency of the public sector in monitoring capital schemes.



Alan Milburn recently told the Commons Health Committee that only four major publicly funded schemes were under way – compared with 64 PFI schemes "on the stocks".

Yet figures produced by the Department of Health for the Health Committee reveal that of 24 publicly-funded NHS projects ranging in cost between £9.4m and £62m under way in 2001-02, with a total value of £510m, only two were expected to exceed budget … by a total of just £2.3m (less than a quarter of one percent of the total investment), and only five schemes are expecting a delay of 1month or more.

More significant, according to DoH forecasts, two NHS-funded schemes, in Blackpool and Bury, are expecting to come in BELOW the projected cost – something that NO PFI scheme will ever do.

The price of PFI: Kidderminster Hospital axed to pay for new Worcester hospital