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The PFI Legacy: Lessons for UK Infrastructure

February 2025

Executive Summary

In the run up to the 2025 Spending Review, there will be a focus on the infrastructure needed to deliver on Government's Missions and on how this should be funded, including the role that private finance can play. We do not expect to see a direct return of the Private Finance Initiative (PFI) in its original form, but private funding should have a role to play in unlocking the infrastructure the UK needs and new funding models can and should learn lessons from PFI.

PFI played a key role in infrastructure funding in the UK for c. 20 years (around 700 projects with a capital value of c. £60 billion). PFI projects will continue to operate for another 20 plus years. This creates a rich evidence base to inform future funding programmes.

Six key lessons from PFI for Government, to help the public and private sectors work together to close the infrastructure funding gap:

1. Be clear in business cases – is the funding model unlocking infrastructure which could otherwise not be funded? Consider affordability alongside value for money
2. Set out acceptable and unacceptable funding models and remain consistent over time – this helps the private sector build a pipeline with certainty
3. Consider ring-fencing funding for condition and asset maintenance across the public sector asset base
4. Use long-term contracts when demand is highly predictable or where changes in use can be accommodated without significant adaptation of the asset
5. Consider models for disaggregating services from assets and procuring FM across multiple assets
6. Manage contracts and retain risks proactively and efficiently throughout the contract life (before, during and after)

This can drive additional investment, improve outcomes, manage risk and accelerate delivery.

Challenge and Context

The Challenge

The Spending Review in June 2025 will include an Infrastructure Strategy. We anticipate that this will set out the infrastructure needed to support delivery of Government's Missions and priorities and will indicate how this infrastructure will be funded.

The Infrastructure and Projects Authority (IPA) has previously estimated that over £700 billion will be needed across all UK infrastructure sectors over the next decade.

The 2024 Budget introduced a new stability rule to prevent borrowing for day-to-day spending and an investment rule based on net financial debt (taking account of liabilities and assets), which has unlocked c. £100 billion of public investment over the next five years. In parallel, the government has challenged the private sector, in particular pension funds, to increase investment in UK infrastructure.

We have previously recommended that Government should take a portfolio approach, optimising private investment in the sectors where it is most suited, allowing it to focus public investment in sectors where it is harder to attract private funding, often social infrastructure (e.g. schools, hospitals, prisons) where there is no traditional third-party revenue stream. The challenge for the Spending Review may well be that there is insufficient public funding available to meet the scale of infrastructure needed, in which case models to leverage private finance may be required in these sectors.

The Context

The Private Finance Initiative (PFI), a form of public-private partnership, played a significant role in attracting private investment into UK infrastructure (including social infrastructure) from the mid-1990s. In a PFI, the private sector funds, builds and operates an asset through a Special Purpose Vehicle (SPV) made up of funders and delivery partners. The public sector makes an availability payment (unitary charge), typically over a period of 20–30 years, reflecting the scale of investment and risk transfer. This payment creates a revenue stream for the private sector, covering its costs, including the cost to build the asset and financing costs.

In 2018, Government announced that PFI would not be used for new UK infrastructure projects, citing concerns about inflexibility and complexity. In its 2018 report, the National Audit Office (NAO) concluded that there was a lack of data available on the benefits of PFI. The number of new PFI projects had been declining for some time, from a high of 68 in 2004 to just one in 2018, after Government reduced its use of the model in 2008.

The 2018 announcement did not apply to the devolved administrations and each of the Scottish and Welsh Governments has introduced a next generation funding model, learning from PFI.

As the government develops its Infrastructure Strategy, there is a question as to whether some form of PFI-type model would be required to address the social infrastructure funding gap. We set out here some of the positive and negative features of PFI and lessons that can be taken forward into any new funding models.

Positive Features

By returning to the original intent of the Private Finance Initiative and considering the experience of PFI projects on the ground, there are many positive features from PFI.

Public infrastructure would not have been built at all

When many of these projects were approved, the choice was between PFI and no asset. No alternative public sector capital funding was made available.

The most explicit example of this was in housing where Ministers stressed that there was "no fourth way" (i.e. no additional public funding to achieve the Decent Homes Standard).

This additional infrastructure created positive benefits for users and created wider benefits to the economy.

Construction cost risk transfer has taken place

In 2003 and 2008 surveys, the NAO noted that PFI projects were reported to be delivered within budget more often than non-PFI projects (noting that certainty does not necessarily mean lower price).

There is evidence of significant cost overruns being borne by the private sector, e.g. at the National Physical Laboratory, John Laing plc lost c. £67 million on the construction project, and its sub-contractors at least £12 million. With the collapse of Carillion, the private sector bore losses of c. £600m across two hospitals.

Asset maintenance is baked into contracts and cannot be delayed for budget reasons

The NAO highlighted the dual benefits of the provider having an obligation to maintain the asset and the transparency of pricing, which means that the public sector knows in advance how much it will be paying. This this means asset replacement costs do not arise unexpectedly in any one year and should not be delayed in the event of budgetary constraints. NAO has recently reported on the poor condition of the non-PFI estate.

However, there are multiple examples of PFI SPVs not meeting maintenance obligations, leading to dispute.

Where assets / services are designed to be flexible, arrangements have been resilient

A review of the community health LIFT PPP programme showed positive benefits. The programme delivered 300 health centres, replacing outdated facilities with modern, flexible spaces. The initial design of the space has allowed it to adapt to different user requirements, without need for contract change.

MoD's Heavy Equipment Transporter PFI explicitly enables flexibility by providing Sponsored Reserves (during frontline operations these personnel are called up and serve alongside regular Army personnel).

PFI offered a bankable pipeline attracting funders and contractors

As PFI grew and became increasingly standardised, it became a recognised and understood investment opportunity for globally mobile capital.

High and stable demand was important to attract interest from large construction companies. In health, 92 projects were delivered in the nine years from 2002. To deliver new programmes at scale now, the supply chain would need to be rebuilt. In 2023, the New Hospitals Programme proposed 40 hospitals, with only four of the UK's main contractors voicing interest.

Successful contract management requires appropriate resourcing and mutual understanding

Authorities with well-resourced, proactive and robust approaches to contract management are held in high regard by the private sector and are seen as a blueprint for success.

Successful contract management is associated with appropriately resourced teams in the public and private sectors who have deliberately spent time to understand each other's motivations and incentives and understand where objectives do, or do not, overlap. For the public sector, this means understanding each part of the SPV.

Limitations

On the ground experience of managing these long-term, complex projects has identified a number of lessons.

It's not free – there is a long-term revenue payment

At its simplest, through PFI the Government is buying services rather than assets: shifting the budgetary impact from capital to revenue.

This gives short-term capital budgetary flexibility but creates a long-term financial commitment. As the existing PFI schemes mature and move to expiry, a peak annual unitary charge payment of £10 billion is forecast, with payments continuing to 2052.

Risk of total failure still ultimately sits with public sector

Although risks are transferred to the private sector under the contract, there are examples of Government being called upon when the contractor fails, e.g. Metronet / London Underground, where Government had guaranteed the debt. Also, in the case of the completion of two Carillion hospitals where Government stepped in to ensure service delivery.

Should Government step in, the Carillion experience shows the importance of taking immediate action to enforce its rights to avoid further adverse consequences.

Dealing with disparity of condition across multiple assets is complex

An example of running two disparate models side by side can be found on hospital sites which include a mixture of PFI and non-PFI assets. Typically, PFI buildings will be in better condition than non-PFI buildings. Maintenance budgets cannot be moved across the buildings and the disparity grows. The NAO highlighted an NHS trust where PFI payments represented over 20% of turnover. This presents challenges for NHS teams focused on patient experience and risk management across the site.

Operational inflexibility

Departments reported to NAO in 2017 that operational inflexibility was a drawback of PFI. Changes in long-term PFI contracts can be expensive with lenders and investors charging administration and management fees.

This is a challenge resulting from the payment mechanisms used in PFI contracts, rather than with the model. Recalibration of payment mechanisms could have addressed this. PF2, introduced in 2012 but little used, included a variation mechanism that aimed to reduce the cost and complexity of variations.

The squeezed FM

There is generally limited margin on FM within the contract. If issues arise, FM can quickly become loss-making and incentives to collaborate fall away.

As PFIs mature, the original equity holder may have sold out. In the final years, handback issues become critical and fall to remaining partners. If a liability for final handback had been placed on the original equity holder, this would help manage risk and reward with the SPV.

In addition, the FM delivering on site services becomes the face of the SPV and focal point for any challenge.

The public sector needs to play its part effectively and mange contracts proactively

The public sector needs to manage its responsibilities effectively and make timely decisions. E.g. Ferrovial's £48m losses on the M8 were in part due to failures to reach timely agreement across parties.

Public authority contract management has at times been insufficient given the complexity. Contracts are self-reporting, but this has on occasion been interpreted to mean self-managing, with insufficient authority focus on performance management.

Lessons Learned

Both positive and negative lessons can be taken forward in any PFI successor and more widely in infrastructure funding and delivery.

On the previous two pages we have highlighted some themes which should feed into any new funding model design.

These should help to unlock more infrastructure delivery and help the public sector get better value.

We have identified six lessons from PFI to be taken forward:

1. **Transparency in business case**: If the driver for using a model is to provide infrastructure that would not otherwise be affordable this should be explicit in the business case. The business case should capture the benefits of the additional infrastructure delivery and wider supply chain benefits. Value for money assessment should take account of realism of delivery of options.

2. **Strategic funding**: Government needs to be clear about acceptable and unacceptable funding models, which alongside playbooks, standardisation and the pipeline of projects expected in the Infrastructure Strategy, can help the private sector to build business with certainty.

3. **Ring-fence asset maintenance**: Consider ring-fencing funding for condition and asset maintenance across the public sector asset base, rather than allowing it to compete with other revenue budgets. PFI has hard-wired maintenance activity and funding into individual projects but the disparity in condition between PFI and non-PFI assets has negative consequences for non-PFI asset service users.

4. **Long-term perspective**: Focus long-term operating contracts on those assets where demand is highly predictable or where changes in use can be accommodated without significant adaptation (e.g. the flexibility of LIFT health centres) and draw on the PF2 experience of including an affordable approach to variation in the initial contract.

5. **Disaggregation of services**: Rather than link service provision to an individual asset, opportunities to procure services in a different way should be considered, with the potential to change the role of the FM provider and gain greater VFM. This could include procuring FM across a number of assets (e.g. the Schools Funding Programme).

6. **Robust contract management**: Management of long-term, complex contracts needs to be resourced appropriately, and the public and private sectors need to work together to establish objectives, identify incentives and understand one another's red lines.

Get in Touch

Deloitte has extensive expertise in supporting Public Infrastructure

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- debt & capital advisory, infrastructure financing and procurement advisory for both public and private/bid side; and
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Infrastructure plays a pivotal role in shaping tomorrow and strengthening our economy today, but not without challenges. Construction projects have grown larger, riskier, and more complex. Powered by collaboration, innovation and transformation, we find solutions to the most pressing issues facing our clients and communities. From green infrastructure to sustainability, smart technologies to a lifecycle approach – we drive ambitious outcomes, minimise risk and accelerate delivery.

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Appendix A – References

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