REPORTING AND MONITORING: RECENT DEVELOPMENTS IN PFI CLAIMS

By Sean Wilken KC

Historically many of the claims arising from Private Finance Initiative ("PFI") projects have been about the state of or financing of the asset: how was it built, how was it maintained and who pays for what. These claims are slowly becoming ones about the state of and liability for the asset on handback. A recent trend, however, is claims which are not about the actual asset but what has been said and done about the performance of the PFI arrangement – claims which turn on the reporting and monitoring of performance. These claims have their own particular difficulties and pitfalls for all parties.

The starting point is that PFI contracts were intended to be self-reporting – the Project Company and the other entities in the supply chain – construction and Facilities Management contractors – were supposed to report their own failings to the public sector body notionally running the PFI. This was to be done in a series of monthly reports. The public sector body would then check the report and dispute it, if appropriate, by reference to the Dispute Resolution Procedure in the PFI arrangement. The reports were to cover the state of the asset – which should have been apparent. The reports were also to cover the day to day performance and then the reporting of performance by reference to either supposed Service Level Standards or Key Performance Indicators ("KPI"). Where the performance or reporting were deficient, Deductions from the amounts paid under the PFI would then notionally be levied by the public sector body.

This concept was novel to all of those involved. Historically, contractors have not been renowned for reporting their own defective performance. Further, when the asset left the public sector, those involved with the asset would, under the Transfer of Undertakings (Protection of Employees) Regulations, usually transfer with it. The result is that the public sector would be stripped of the staff and expertise required to monitor the performance and reporting under the PFI. Allied to that, many parties viewed the PFI as akin to a simple contract to manage the asset once built or renovated. Thus, the focus was on whether the asset had defects, was clean and properly maintained. The focus was not on the much softer service provision in relation to reporting and monitoring.

Recently, however and due in part to the changing economic climate in relation to PFI, public sector bodies have begun to realise that there may be a significant monetary advantage to them (by way of Deductions reducing the amounts otherwise payable) in focusing not only on current but also historic reporting and monitoring. This focus has revealed numerous quirks in the PFI arrangements which in turn can and do create difficulties for all those concerned.

In general terms,[1] there are three drafting issues and one operational issue that are commonly found. I take each of them in turn.

Structurally, the provisions relating to defects in the PFI asset are usually relatively easy to locate. Thus, where a defect renders an area of the asset unsafe or unusable, recourse is had to Unavailability which is usually defined and sits plainly within the Payment Mechanism ("PayMech") with the associated formulae for calculating Deductions. Those involved in PFI disputes are now relatively comfortable with these provisions which have been debated since the early 2000's. The provisions relating to monitoring and reporting are not so straightforward. As set out above, the PFI style of monitoring and reporting was new and this is reflected in the drafting. Often the requirements in relation to the requisite reports are grafted on or into elements of the payment procedure in the main body of the PFI contracts or as extra elements to the PayMech. The results are very often that the requisite reports are not defined or only have an ad hoc definition. Further, there are usually inconsistences and contradictions between the monitoring and reporting requirements and the rest of the PFI contracts. Opportunities for *Chartbrook*[2] type arguments based on errors in drafting abound.

This structural problem becomes more acute when one turns to the benchmarks against which performance, monitoring and reporting are to be judged. Often there are no provisions as to what is to be in any given report or how the format and contents of the report are to be agreed or then judged. Obviously, if there are no provisions, given the levying of Deductions is penal (in financial not legal terms, Deductions are very unlikely to be a penalty as a matter of law), an attempt to levy will inevitably be met by an uncertainty defence. Thus, it will be said, if the public sector body wishes to levy, the terms under which it seeks so to do must be sufficiently clear and certain. If they are not, then no Deduction can be made.

Further, when one is talking about benchmarking against a KPI, if KPIs are present at all, KPIs will usually be in the very detailed schedule that covers the entirety of the works and services to be provided under the PFI. The difficulties that then arise are often ones of omission – the contractual puzzle lacks pieces or the necessary links. There is a further problem, however, of demarcation. The works and services will be provided by a construction contractor and a Facilities Management contractor. Liability for and financing of those services may – but not always will – be passed through the Project Company. Where one is talking about construction versus management, demarcation may be less of a problem. Monitoring and reporting, however, can and do apply across all works and services provided by all the parties making demarcation a live issue – one that was rarely properly addressed in the contracts.

Thus, at the basic level of structure and drafting, there are difficulties that can render any claim problematic.

The second main area is the question of retrospectivity. Again with Unavailability, at least for the mid to later generations of PFI, it is reasonable to expect there to be caps on the ability to levy Deductions retrospectively for historic alleged failures. Thus, there are often provisions that Deductions for defects can only be levied for (n – 1) or (n – 2) – that is for one or two months before the month for which an invoice is being presented. There may also be financial caps imposing a financial limit on the amount of Deductions in any given period. Such explicit caps are often missing in the case of monitoring and reporting Deductions. This in turn has triggered some public sector bodies to issue claims for monitoring and reporting for the entire life of the project. Quite apart from questions of proof and limitation, this type of claim often fails to notice that there may be temporal caps in either the KPIs themselves or in the provisions that allow audits of past performance under the PFI arrangement.

The third main area is what the content of any given report is to be and who decides. As set out above, the contracts are often silent on the detail as to that which should be in any given monthly report. Thus, there is a debate as to whether it is the Project Company (and the associated contractors) or the public sector body that decides. The initial answer to that debate can often be found in the invoicing provisions. These often provide for an initial invoice with the associated reports to be presented to the public sector body. In crude terms, the public sector body is then given a choice to dispute or to pay. It seems sensible that if the public sector body finds the reports wanting, it is at this stage that a complaint would be made. Historically, in many cases, this did not happen. Further and ultimately, however, the complaint would have to be resolved by adjudication. It remains very much an open question as to whether an Adjudicator could decide what should be in any given report (or KPI) and if they could against what benchmark that decision would be made.

This last issue over uncertainty links to the operational issue. PFI contracts often leave the precise scope of the KPIs and the reports to the parties' agreement. That, in a long term contract, can seem sensible but experience shows that in many cases the parties have simply forgotten or been unable to reach agreement. Therefore, unless precise arrangements are made for the process of agreement or what happens in default of agreement, the parties are left with an agreement to agree. Tritely agreements to agree are unenforceable. The result will be that there are no enforceable benchmarks permitting the levying of Deductions.

Looking at the current landscape of PFI claims, it is very unlikely that monitoring and reporting Deductions claims will become less of a feature. Further, as much turns on the precise wording of the contract at issue, it is unlikely that, other than setting out views on the general themes, consideration and resolution of monitoring and reporting Deductions by a court will assist across the industry. It is therefore reasonable to assume that monitoring and reporting will remain a historic, current and future problem for all parties to PFI arrangements.

1 Much will turn on the generation of PFI arrangement at issue and its particular wording – these, however, are the general themes.

2 Chartbrook Ltd v Persimmon Homes Ltd [2009] 1 AC 1101 at [14]