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Examining the Use of Corporate Governance Mechanisms in Public–Private Partnerships: Why Do They Not Deliver Public Accountability?

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The paper examines corporate governance mechanisms which aim to ensure financial accountability in the context of long-term Public–Private Partnership (PPP) contracts in Britain, and assesses the degree to which they provide taxpayers with control and accountability. The corporate governance arrangements are drawn from the private sector, and therefore downplay the traditional concepts of probity and stewardship, in part due to the British Treasury’s adoption of private sector financial reporting. The paper draws on Shaoul et al.’s (2012a) governance-based reporting framework to critique the corporate governance mechanisms of structure, financial reporting, contracts, and scrutiny in relation to British PPP projects. It shows that the way these mechanisms are set up means there is a lack of control by the public sector, thus rendering public accountability ineffective.

Key words: PPPs, corporate governance, contracts, public accountability, scrutiny

The government is in danger of creating a ‘shadow state’ of outsourcing companies that is neither transparent nor accountable to parliament or to the public. [Margaret Hodge, Chair of the Public Accounts Committee, March 2014]

Introduction

Britain’s Public–Private Partnerships (PPPs) policy, introduced in the 1990s, was one of a number of government policies aimed at opening up public expenditure to the private sector. Consequently, large corporations gained control of an assured stream of taxpayers’ monies. This move was coupled with an increasing private sector involvement in government decision making as the need grew for technical expertise to understand, deliver, and implement the contractual arrangements surrounding these very complex projects (Shaoul et al. 2007; Willems and Van Dooren 2014). However, there were not corresponding changes in the governance

mechanisms to enable the public or its representatives, the media and academics to scrutinise, call to account or sanction the private sector organisations.

Approximately 10% of central government’s capital investment is privately financed, although the aspiration is that up to 80% of new economic infrastructure should be wholly or partly privately financed (NAO 2015a). As of March 2014, there were 728 current projects with a capital value of £56.5bn, with a further 11 projects worth £0.8bn in procurement (HM Treasury 2014). But this list fails to give a complete picture as it omits the three PPPs for London Underground worth £30bn that have collapsed, and a number of other terminated projects. Whereas only about half of departments’ capital investment is for new assets, the rest being for maintenance of existing assets in their current condition, nearly all privately financed investment is for new assets (NAO 2015a).

Whole life unitary charges payable until 2050 are about £222bn (HM Treasury 2014), a figure that will rise as actual payments rise with inflation, changing needs, and contractual changes. These annual payments of about £10bn a year come on top of the purchase of external goods and services, and other outsourcing contracts. Consequently, substantial sums of public money are now committed in advance, irrespective of which government is in power, and no longer under the direct control of current governments. The policy thus creates a shadow state of companies that are de facto public authorities (Shaoul et al. 2008a) but have not been acknowledged as such by government, with the consequence that they are not subject to Freedom of Information (FoI) requirements.

Successive governments justify the outsourcing policy in terms of additional investment that could not otherwise be afforded; greater value for money (VFM); risk transfer; and construction on time and to budget. However, there has been no comprehensive ex post facto evaluation of the policy. Indeed, tellingly, in relation to long-term contractually based contracts, known in the United Kingdom as Private Finance Initiative (PFI) contracts, the NAO has stated that:

There is no clear data to conclude whether the use of PFI has led to demonstrably better or worse value for money than other forms of procurement. Although most PFI projects are delivering the services expected, we have previously highlighted the lack of systematic ongoing value for money evaluation by departments of operational PFI projects. (NAO 2011: summary page 6)

This conclusion implicitly highlights a deficiency in the governance mechanisms which should enable such evaluation to be possible. Because PPPs are hybrid organisations incorporating structures from both private and public sectors (Miller et al. 2008), governance mechanisms should reflect the governance needs of both sectors, however in practice there has been a transfer of corporate governance mechanisms to the public sector (Hodges et al. 1996).

The purpose of this paper is therefore to critique existing corporate governance mechanisms in the context of the operational phase of long-term PPP contracts in Britain, and

assess the degree to which they provide taxpayers with control and accountability. Although the policy remains very contentious despite revisions over time, it is not the purpose of this paper to focus on the differing views of the policy and its merits and demerits, anticipated or actualised, but on how corporate governance mechanisms provide accountability for public monies in the context of PPP policy. That is, it responds to public interest questions around the corporate governance arrangements of operational contracts (Hodge and Greve 2010).

The paper draws on Shaoul et al.'s (2012a) corporate governance-based reporting framework, which identified elements seen as important in the PPP governance process and questioned how corporate governance and public accountability mechanisms work below the level of central government. In the absence of comprehensive evaluation of the policy, the paper uses as its evidence-base necessarily fragmented examples and analyses derived from official reports, the research literature and the corporate press about PPP in the United Kingdom. It nevertheless has international relevance as the policy is being implemented elsewhere. The corporate governance arrangements, largely drawn from the private sector, downplay the traditional concepts of probity and stewardship, in part due to the Treasury's adoption of private sector financial reporting.

The paper proceeds as follows. First it compares notions of corporate governance in the private sector with the broader notions of governance and accountability in the public sector. In the next four sections, it identifies and critiques four important corporate governance mechanisms (structure, financial reporting, contracts, and scrutiny) that regulate PPP accountability processes. The final section discusses the implications of these findings and the likely impact on public policy and finance.

Private and Public Sector Notions of Governance and Accountability

As public sector services have been opened to private delivery, the public sector has been reformed to operate more like the private

sector in particular by outright privatisation, introduction of contracting out, and adoption of more managerial styles of leadership and performance management techniques. These trends have had a profound impact on public accountability (Hodge 2009). In particular, the widespread practice of contracting out weakened traditional systems of public accountability (Dubnick and Frederickson 2010), whereby individual and group accountability for program goals was achieved through hierarchical relationships, standardised procedures, policy directives, and bureaucratic control. Traditional systems of accountability were criticised for being risk-averse and retrospective (Acar et al. 2008) because they focused on accountability for errors rather than for achieving results (Hodge and Coghill 2007). As part of this reform, governance processes drawn from the corporate sector were introduced and market and managerial forms of accountability increased the emphasis on performance and outputs (Willems and van Dooren 2011).

However, the clarity of the principal-agent based corporate governance system that is the norm at least in the Anglo-American context did not necessarily blend well with the complexity of real-world public accountability (Willems and van Dooren 2011). In the Anglo-American context corporate governance focuses on how *individuals* direct and control companies while leaving directors free to drive their companies forward to make profit and retaining the essential spirit of enterprise (Cadbury 1992). In this context, openness is valued but only within the limits of companies' competitive positions (Cadbury 1992, Section 3.2).

By way of contrast, the public sector has a complex range of political, economic, social, and environmental objectives that in general terms enhance or maintain the well-being of citizens (IFAC 2013). Public sector governance is concerned with how *public service bodies and the individuals within them* (CIPFA 1995) are responsible for their actions in terms of: interactions between the state and society; how the state makes itself accountable to society; and how the state guarantees the security and rights of citizens (Turner 2013). Thus, the public sector must seek to reflect the interests of multiple

stakeholders who have various legitimate but potentially conflicting accountability expectations. Consequently, the state may pursue social policy that prioritises fairness and equality over financial performance, meaning that its constraints and incentives are distinct from the private sector (IFAC 2013). Furthermore, there is an assumption that governance should reach out to these stakeholders in a two-way process, with the United Nations (UNESCAP 2009) describing its aspirations for good governance as participatory, consensus oriented, responsive, equitable, and inclusive,¹ which is very different from the aspirations of good corporate governance. Although these characteristics are aspirational in nature rather than implemented, the implication is that information systems should be responsive, and that their information should be provided on a timely basis and be accessible to the public (Shaoul et al. 2008a).

Although it has been argued that public accountability of this nature suffers from too many hands and too many eyes, that is, multiple account-givers and receivers (Bovens 2005), it has nevertheless been the case that decision-making transparency has traditionally been a cornerstone of public accountability in democracies (Reynaers and Grimmelikhuijsen 2015). Public sector requirements for transparency and due process exceed those in the corporate sector (Schaeffer and Loveridge 2002). The intention is that no persons or entities are unduly or unfairly advantaged or disadvantaged by decisions (Rufin and Rivera-Santos 2012), that may have been taken in a discriminatory manner and/or without open and transparent debate and application of due process. To this end, directors and members of boards of governors are expected to deliver services and behave ethically in the public interest (UN 2008). Although actual practice may not meet expectations and the notions may be contested, good governance characteristics aspire to selflessness (CIPFA 1995; Nolan 1995), honesty (Nolan 1995), objectivity (CIPFA 1995; HM Treasury 2011), and probity (DoH 1994). UN guidance (2008) on PPP governance focuses on aspiring to fairness and the public interest at all stages of the project. It identifies expectations

of: a fair and transparent selection process for partners; contracts with fair incentives and fair returns for risk takers; assurance that VFM is achieved and services are provided in the public interest. Moreover, OECD (2012) principles note that public procurers should remain particularly vigilant over VFM during operational phases, implying that while desirable previously such vigilance was missing.

These distinctions mean that mixed accountability messages emerge from an analysis of PPP case studies by Hodge and Coghill (2007), which show political forms of accountability reducing with increases in market-based and managerial accountabilities. Moreover, Hodge and Coghill show that in PPP projects constituency relations forms of accountability tend to be low and that because FoI legislation typically does not apply to private companies judicial or quasi-judicial forms of accountability also tend to be low.

In hybrid PPPs, governance arrangements might ideally be expected to reflect the requirements, aspirations, and sanctions of both sectors. But this expectation raises questions about how structures and mechanisms can enable governance across organisational boundaries and sectors and especially how internal structures of governance filter down through organisational hierarchies into executive agencies (Shaoul et al. 2008a, 2012a). Spiller (2013) argues that public and private sector interactions suffer two fundamental hazards – government and third party opportunism – which interact to make regulatory processes and outcomes more rigid, formalistic, and prone to conflict than envisioned by relational contracting. Third party opportunism, he argues, thrives in an environment of political contestability and fragmentation in open access states, where oversight bodies and external stakeholders expect to challenge decisions (Ahadzi and Bowles 2004). However, such challenges may be self-interested creating risk to both public agent and investor. Therefore, governance relationships may be more formalised and relational contracting is less likely than in purely private contracting (Spiller 2013).

We draw on Shaoul et al.'s (2012a) governance-based reporting framework, which

explicitly recognises the governance needs of both public and private sectors, to examine the mechanisms of corporate governance and assess their effectiveness in enabling public accountability of PPP projects. This framework recognises four elements of governance identified initially by Smith et al. (2006) (complex corporate structures, external accountability, board member conduct and public access to information) and relates these to the specific and variable information requirements that attach to different reporting phases of PPPs (pre-financial close, post-financial close and during operations, and the project termination phase).

The framework also highlights the role of oversight and evaluation processes especially associated with those institutions whose primary function is to call public officials to account (Mulgan 2000). In setting out their agenda for future research Shaoul et al. (2012a) note the particular relevance to accounting and governance researchers of financial reporting and the annual disclosure about operational costs and profits, the detail about contract governance publicly available, and external scrutineers' needs for information. In addition, they note that there are interesting research questions about how information flows across partners' entity boundaries, how private sector reporting might be amended to facilitate the achievement of public accountability, and what level of disaggregated information might be needed. In this paper, we focus on just four corporate governance mechanisms, drawn from this framework, and chosen for their especial interest to accounting and governance researchers (complex corporate structures, financial reporting, contracts, and scrutiny). We critique each in turn and examine the extent to which they provide public accountability.

Complex Corporate Structures

In PFIs, a shell company known as a Special Purpose Vehicle (SPV) is set up for each project with governance becoming the responsibility of the SPV Board. Directors are drawn from the various members of the consortium financing and operating the project, so that decisions are controlled by the private sector. No public

sector officials have any direct involvement with project governance, although in a small number of cases a public official may attend board meetings as an observer.² In joint venture PPP structures, directors are drawn from both sectors, usually in proportion to their equity stake. But because the joint venture structures were deliberately designed by government to give the private sector a majority of shares (Agyenim-Boateng et al. 2014; Shaoul et al. 2013), control was deliberately ceded to the private sector. In these new and independent legal entities, the boards are controlled either wholly or predominantly by the private sector, which means they may prioritise profit over service delivery and user needs. Indeed, it can be argued that the directors have a fiduciary duty to do so (Agyenim-Boateng et al. 2014).

For projects that involve both construction and maintenance elements, the SPV normally raises finance through a 10% equity contribution and 90% senior debt provided by banks that normally require the SPV to have in place a risk mitigation package incorporating financial and performance supports. These essentially increase the credit rating of the project and protect the senior debt holders from loss in the event of contractor failure (Demirag et al. 2010). However, because debt holders use standardised evaluation models with specific requirements in relation to risks that may be held, including those that must be mitigated, the specification of underlying projects may need to be amended to meet debt holders' criteria (Demirag et al. 2012). The SPVs, which are normally shell companies, subcontract the operational phase of the contracts to subsidiaries of their parent companies that may in turn subcontract to other related companies. This corporate structure serves to minimise the risk for the lending institutions and the SPV, which aims to devolve risk down to its subcontractors, which may change over time. The SPV acts as the conduit to pass the monies received from the public authority (or the users) to its sister companies. As discussed in the next section this hierarchical chain of companies reduces the transparency of financial reporting. In practice, the numbers of companies involved in any given PPP is greater than suggested by

the pro forma structures issued by departments or bodies such as the NAO (Agyenim-Boateng et al. 2014; Demirag et al. 2010). Complex legal documents must set out the contractual arrangements between the SPV and the public procurer, the lending banks and the public procurer in relation to step-in rights, and the SPV and its multiple contractors and their subcontractors. Significantly, the PPP finance takes the form of project finance whereby lenders and investors rely exclusively (non-recourse) or mainly (limited recourse) on the cash flows of the project which must cover loan repayments and return on investment (European Investment Bank 2015). In the event of failure these organisational structures ensure that there is no access to the parent companies' financial resources. The controlling organisation therefore cannot be held accountable in a financial sense for project failure.

The implications are best illustrated by the failure of two of the three 30-year contracts worth £17bn to upgrade and maintain London Underground. Despite all the government subventions, including the government's underwriting of the SPVs' debt (Jupe 2009), within 2 years the two Metronet companies were behind with their investment programme and over budget (Jupe 2011). In July 2007, they went into administration with debts of at least £2bn after their owners, five international corporations, were able to use their corporate structure arrangements to refuse to commit further funding to their Metronet subsidiaries (Vining and Boardman 2008).

Particularly relevant here is the NAO's attribution of the failure of Metronet to its corporate structure, governance, and leadership (NAO 2009). The five shareholders had to agree many of the decisions unanimously, but with shareholder-dominated supply chains, they had conflicting interests depending on their roles. The top management was therefore in an impossible situation, changed frequently, and was unable to manage the work effectively (NAO 2009). Furthermore, despite underwriting Metronet's debt, the Department for Transport was not party to the contract and therefore was unable to manage its own risk (Shaoul et al. 2012b).

These issues of structure must be germane to many more contracts. This example illustrates how multiple partners with different interests can use and manipulate complex corporate structures to obscure information sharing and diffuse effective control.

Financial Reporting

As a governance mechanism, financial reporting enables boards to assess financial performance and thus safeguard stakeholders' interests. It is predicated upon the availability of substantial internal information particularly for public sector stakeholders who need a detailed understanding of the actual costs and profits on each contract to ensure VFM.

Whilst private companies prepare external financial reports which appear to be heavily regulated by the national or international accounting regulators, there is leeway for substantial judgement and choice in determining what information is aggregated, what is publicly disclosed and how it is presented. The complex structures, discussed above create a hierarchy of parent companies and subsidiaries that are in turn parents and SPVs in particular are thus able to take advantage of reporting rules to present the minimum information permissible. Exemptions from sub-consolidation disclosure are claimed so that only the ultimate parent company discloses information that is highly aggregated (Agyenim-Boateng et al. 2014). Monitoring of SPVs and their sub-contractors, usually related parties, is therefore difficult to undertake and it is difficult to track public money through the corporate web (Shaoul et al. 2008a). Although the NAO, through the rights of the Comptroller and Auditor General (HM Treasury 2013, para. 1.6.3) can investigate the books of many public organisations, it has no legal remit to cross the private sector barrier, despite calls to change this (Edwards et al. 2004). Without this, financial performance and profits earned are obscured. To overcome this criticism, HM Treasury (2012) has stated it will introduce an open-book approach with a gain share mechanism for the life cycle fund for new projects under the UK's revised Private Finance 2 framework. Open-

book accounting is intended to give procurers greater access to information about the actual costs of outsourced public services and therefore about the profits that suppliers are making. When coupled with agreements to share cost savings, known as gain sharing, open-book accounting can incentivise innovation because the open-book accounting confirms the cost reduction (NAO 2015b). It is however unclear how effective this will be (Public Accounts Committee (PAC) 2014); the announcement may simply be aimed at reassuring the public. For example, the NAO technically has a right to roam into the financial records of contractors, but has rarely used this right. However, although noting that only about 23% of projects include open-book accounting, the NAO (2015b) report did cite examples of successful implementation.

The public sector financial reporting of these contracts mirrors the private sector model in terms of regulations and format. Typically this means that information provided on specific projects is limited due to data aggregation. Specific problem areas identified in the literature include significant inadequately explained changes in asset values (Ellwood and Garcia-Lacalle 2012a), poor disclosure of contingent liabilities which obscures potential risk (Shaoul et al. 2008a; Stafford et al. 2010) and opaque reporting resulting from the complexity of joint venture-style structures (Agyenim-Boateng et al. 2014; Shaoul et al. 2013). This lack of transparency is important because while it does not capture the whole process, transparency is a vital condition of accountability (Mulgan 2003).

Contracts

Contracts are drawn up between a public agency and a private sector partner. They are legally binding, forming the basis of the governance relationship between public procurer and private supplier, and may represent a form of transparency about inputs (Reynaers and Grimmelikhuijsen 2015). Although necessarily incomplete, these complex and lengthy documents must attempt to cover all potential aspects of the project over its long life. Unsurprisingly, they are subject to numerous

amendments. For example, standard PFI contracts first introduced in 2000 were amended in 2003, 2004, 2006, and 2007.³

Contracts identify the services to be delivered and establish key performance indicators that typically include aspects of performance management, output measurement and management reporting (4Ps 2006) to enable a robust assessment of contracted performance. They cover payment mechanisms including arrangements for amendments to the contract and market testing or quasi-competitive comparisons, such as Best Value reviews and benchmarking. They typically include penalties for non-performance or performance failures.

Although the UK's experience in relation to transparency is better than elsewhere, most contracts are either not in the public domain, have been heavily redacted, or contain gagging clauses thereby limiting an independent assessment of whether contracts operate as effective governance mechanisms. The following three subsections examine the available evidence in terms of key elements of the contract: performance measurement, payment mechanisms and penalties that collectively reflect the allocation of risks between the various parties, and the VFM that PPPs are supposed to deliver.

Performance measurement

For contracts to operate as effective governance mechanisms, performance must be monitored, measured and compared against contractual agreements. However, the organisational arrangements of PPPs involve subcontractors monitoring and reporting on their own performance (Edwards et al. 2004). Consequently, public sector directors are dependent on performance data provided by the contractors, a practice which lacks transparency and is not appropriate for governance purposes (Hood et al. 2006; Willems and Van Dooren 2011).

Moreover, despite early and authoritative warnings about the need for sufficient resources to be committed to performance monitoring (NAO 2001), there is still a lack of resources devoted to this, for example, in local councils (Nisar, 2007), and in hospitals to the extent that VFM is at risk (NAO 2010a). In practice, especially in early contracts, perfor-

mance management structures have had mixed results (Audit Commission (AC) 2001). Performance measurement against contract performance indicators was limited (NAO 2003) because monitoring structures were inappropriate (NAO 2002) and key performance indicators proved unworkable and had to be rewritten (Edwards et al. 2004). Numerous cases of poor data collection persist and, even where data does exist, government departments and agencies fail to make the best use of it (NAO 2010b). By way of contrast, negotiators from large multi-national private sector companies learn quickly from their experience in other similar deals (Shaoul et al. 2013).

Payment mechanisms

The payment mechanism puts into financial effect the allocation of risk and ensures that objectives are delivered and outputs achieved as set out in the service output specification. To be effective, payments and penalties must balance rewards for success and penalties for failure so that financial incentives appeal to self-interested agents (Schillemans 2013). However, limited financial data about whether investors' returns are aligned with the risks they take undermines any assessment of the payment mechanism's effectiveness (NAO 2011). What is known is that even if there is evidence of poor performance or excess profit taking, the public sector has struggled to respond effectively. For example, 69% by monetary value of early contracts had no provision at all for claw back (Wintour 2000) and signalling an end to the era of PFI, Francis Maude, Cabinet Office Minister was reported as saying,

Some of the deals done were ghastly. Some of the deals we've come across, the people on the other side must have been laughing all the way to the bank. (Kirkup 2011)

Kirkup (2011) further reports that Cabinet Office and Treasury officials are examining PFI contracts worth billions of pounds, looking for ways to claw back money for taxpayers. Such claw back mechanisms were aiming to reflect unforeseen efficiency gains in the operational phases of agreed contracts. However, in 2014 the NAO was still finding that:

Government needs to be better at enforcing its contracts and deducting penalties. We see post-contract audit reviews, gain-share arrangements and profit claw back playing a greater role in ensuring incentives are aligned and value is not lost in adversarial behaviour. (NAO 2014c: 14)

Claw back mechanisms in particular would likely be unpopular and serve to deter future bidders, and for example, survey evidence confirms that banks may require changes to payment terms and risk allocations before lending (Demirag et al. 2010).

Contrary to the oft-claimed benefits of PPPs that they provide certainty about future costs 21 out of 25 UK housing projects signed at the time of the NAO's evaluation had been subject to cost increases rendering them excessively costly (NAO 2010c), and hospital Trusts found that their payments rose by an average of 20% within a few years of operation (Shaoul et al. 2008b). The causes may be a combination of inflation, volume increases, and contract changes. There may be failure to anticipate requirements, or make provision for competitive tendering (NAO 2008) or benchmarking (NAO 2010b) so that procurers are locked into long-term deals that can increase costs over other methods of provision. In extremis cost concerns may be overridden to ensure service provision continues (NAO 2012). That is, contracts contain numerous provisions for payment increases, which in schools saw prices rise substantially within a few years of the contract start date (Education Executive 2015).

Penalties

Without effective governance to ensure that penalties are enforced to incentivise good performance, risk – and cost – can easily be pushed back to the public sector. The evidence about sanctions is however variable and may not be verifiable. Procurers do not routinely report penalty deductions in their financial statements (Edwards et al. 2004) or other forms of financial settlement in the case of contract failure. Moreover, the NAO (2014c) estimates that 38% of public entities had not sought the financial redress to which they were entitled despite previous exhortations by the NAO to do so. Public

entities may be reluctant to apply penalties or may be unable to assess whether payment should properly be made due to performance monitoring and measurement problems (AC 2001; Shaoul et al. 2011). Furthermore, tiny potential deductions in relation to the monthly contract payment are not credible incentives (Edwards et al. 2004). Thus, there have been few and only small deductions on PPP contracts because their complexity renders them difficult to enforce in practice (Standard and Poor's 2003), so that the service element of PPP contracts continues to carry little risk for contracting companies (NAO 2007).

Summing up its evaluation of lessons to be learned from PPP contracts based on an examination in five previous reports of 162 projects with a capital value of £18bn, the NAO (2011) concluded that the government needs to be a more intelligent customer. This NAO report highlighted, as does the Shaoul et al. (2012a) governance framework, the importance of accurate data in the different phases of a PPP to improve control over the contract, and the need for procurers to push the boundaries of commercial contractual arrangements.

Public Oversight and Scrutiny

There are various levels and mechanisms of public oversight the intended purpose of which is to hold public managers to account for their decisions after the event. Although external ex post scrutiny is the original core sense of accountability (Willems and van Dooren 2011) internal mechanisms drawn from the private sector also play a role. For example, the audit committee, comprising non-executive governors, is responsible for scrutinising and advising on governance issues, frequently working with internal and external auditors to evaluate risk management. However, although there is general best practice guidance (see, e.g. HM Treasury 2013), the rules, requirements and objectives of audit committees vary across the public sector so that it is impossible to identify in any systematic way what it is they examine. Like their private sector counterparts, whose performance has been described

as mixed (Turley and Zaman 2007), their level of success is likely to be variable.

Externally UK public bodies have been subject to oversight and scrutiny by parliament and nationally organised audit bodies established in the 1980s that report to parliament. The NAO was established in 1983 with responsibility for auditing and carrying out VFM studies at central government level. It reports to the House of Commons' PAC and other specialist select committees. PAC may also call relevant public and private sector officials for questioning, although its precise powers to enforce attendance in relation to those who are not public officials are unclear. PAC will publish a further report to which the government responds via a Treasury minute.

The AC⁴ was established in 1983 with a remit to protect the public purse, mostly in relation to expenditures in Local Government. It was responsible for appointing auditors to all local authorities, and to health authorities from 1990. It set the standards for these auditors and oversaw their work, which was regarded as high quality (Ellwood and Garcia-Lacalle 2012b). Until the announcement of the closure of its 'expensive inspection regime' (Lewis 2014),⁵ it used information gathered from auditors and elsewhere to produce more extensive reports on public performance management.

There is an additional more recent scrutiny mechanism for large high-risk projects. The Major Projects Authority was established in 2011 following criticism by the NAO of government capability in project and programme management (NAO 2010b). Its remit includes improving government capability and carrying out regular assurance reviews of very large projects (Cabinet Office 2011; NAO 2010b). It currently covers 191 of the largest, most impactful and highest risk projects, financed by both traditional and PPP mechanisms. It claims to have saved taxpayers £1.7bn through better intervention in failing projects (Cabinet Office 2014). The NAO (2014a, 2014b) states that there have been improvements in the analysis and quality of data available and in the training and development of project leaders. It equally, though, notes continuing concerns over the overall status of the portfolio of major

projects (there is a decline in delivery confidence ratings), the turnover of project leaders and the need for difference government departments to work together more effectively.

Such routine oversight and scrutiny as exists follows the annual auditing of public bodies. Under typical risk assurance auditing, the amount of attention given to any PPP project is dependent on its significance within the context of the public body being audited. This means that new and/or large PPP and service delivery projects receive more attention, whilst small revenue or capital value projects using well-established models are less likely to be sampled.

More extensive oversight and scrutiny is carried out at sector level in the form of VFM or performance management studies by one of the public watchdogs. During its lifetime, the AC published 730 reports, which focused on general performance management, with only three reports relating specifically to PPPs. Early PPP projects were mainly procured by central government agencies, so by way of contrast the NAO has published over 80 VFM reports on PPP projects and PFI policy, as well as reports on government procurement strategy in general. These have covered ex ante VFM studies of individual projects, as well as ex post facto issues such as refinancing, tendering, and operations and have provided a long list of recommendations for improvement.

Similarly, the PAC makes regular recommendations for improvement of monitoring and scrutiny arrangements. Although one third of contracts are open book, PAC notes that government rarely uses its rights of access to the subcontractors' accounts due to a lack of capability (PAC 2014). Another report (PAC 2012) emphasises poor scrutiny practice as government monitors failed to obtain internal audit reports detailing fraud and malpractice, whereas the PAC (2014) concludes that there is a pressing need to improve government skills in this area.

However, in practice policy lessons do not necessarily follow from the scrutiny of the NAO and PAC. New arrangements such as PF2 or standard contracts pick up on specific details but substantially do not resolve the public accountability problems that PPP inevitably

creates. At the same time, the fragmentation of the public sector reduces the opportunity for routine and systematic drawing together of the issues. The abolition of the AC, which removes oversight by one national body with considerable expertise and resources, means that this capacity will be further reduced, just at a time when PPP type arrangements are becoming more common at local level.

In summary, these governance mechanisms provide a range of practices that purport to provide control over PPPs and related contracts. Some mechanisms are legally very prescriptive, such as the contract, whilst reporting and scrutiny provide the opportunity for substantial financial reporting and evaluation at regular intervals. However, all demonstrate to a varying extent a lack of effective control by the public sector which means that public accountability is compromised.

Conclusion

Although this review has focused on British PPPs, it demonstrates a global trend as PPPs are commonly employed internationally. The trend is important because the PPP model is defined by a *continuing* relationship between the public authority and private providers.

Such policies create para-statal companies that are de facto public authorities. However, the British government has so far refused to designate them as such and thus bring them within the remit of the *Freedom of Information Act 2000*. Simultaneously, the public authorities refuse FoI requests about these contracts on the grounds of 'commercial confidentiality'. Protected by FoI, the corporations' control and power are shielded from public scrutiny and visibility. Openness is limited by competitive position. The corporate and financial sectors have become quite explicitly powerful players with a corresponding reduction in especially political and judicial forms of public accountability.

Despite being essential public service providers, these corporations remain outside the limited governance procedures established for public authorities. Although the Government requires the publication of much factual

information to be available online, this is very fragmented and difficult to analyse, resulting in no meaningful analysis of it taking place and a widening accountability gap. Eckersley et al. (2013) conclude that the private firms supplying the services will be the only people with both the interest in assessing public sector performance and the capacity to analyse the raw data available. Complex parent and subsidiary company structures together with regulatory exemptions allow disclosure to be limited as companies choose to claim reporting exemptions. Furthermore because different organisations within these structures have different and possibly conflicting interests information flows and collaboration across entity boundaries can be problematic.

Governments of all political persuasions have actively championed PPP despite their problems. Generally, their approach has been to pursue the policy on a 'lessons learned' basis resolving problems by revisions and amendments, whose efficacy is unknown and even unknowable. Such reforms include variations to the standard contracts, and negotiations to provide a sharing of refinancing gains, including retrospective gain sharing. New ownership models have been designed with a greater equity stake and including a public equity stake. But this attempt to make the policy work better ignores the fundamental reality that irrespective of operational success this policy entails more input from the corporate and financial sectors to public service delivery. Control of the special purpose vehicles lies with the private partner. The outcome is that none of these 'reforms' resolve the public accountability problems that this agenda inevitably creates. Indeed, the opacity that surrounds contracts and financial reporting is not always driven by the private partners. For example, a number of large PPP contractors are prepared to allow open-book accounting, while a former Chair of the PAC has acknowledged that the main barriers to greater transparency in PPP projects lie within government.⁶ Policy recommendations have focused on initiatives such as open-book accounting and the auditors' right to access contractors financial records, but their implementation remains limited in practice.

There is little public debate about the involvement of commercial interests in public decision making and the resulting changing nature of financial governance within the public sector. This matters because without public accountability and control, such policies risk waste, mismanagement, fraud, and corruption that will in turn increase costs and reduce service provision.

It is a well-established democratic principle that citizens and their political representatives should be able to hold government and public officers to account for decisions made and resources used. Whilst there was never a 'golden age', this paper shows that in the context of PPPs current corporate governance mechanisms are ineffective in providing public accountability.

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1. There are also four other UNESCAP characteristics – accountable, transparent, effective and efficient, and follows the rule of law.
2. For example, a Highways Agency official is an observer on the M25 DBFO board (NAO 2010d).
3. <http://webarchive.nationalarchives.gov.uk/20120503092128/http://www.dh.gov.uk/en/Managingyourorganisation/NHSprocurement/Publicprivatepartnership/Privatefinance-initiative/Standardcontract/index.htm>, accessed 19 May 2014.
4. With equivalent bodies in Scotland (Audit Scotland) and Wales (Wales Audit Office).
5. The AC was disbanded as part of the Coalition Government's pledge to reduce bureaucratic public bodies. Closing down an expensive inspection regime and outsourcing the

audit practice would produce savings of £1bn according to the Local Government Minister Brandon Lewis.

6. <http://www.parliament.uk/business/committees/committees-a-z/commons-select/public-accounts-committee/news/public-services-private-contractors-report/>.

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