

12 Contract Management in Education PPP Projects

- 12.1** Public private partnerships (PPPs) have been used as a method of procuring public infrastructure in the education sector for more than a decade.
- 12.2** The State has outstanding commitments totalling nearly €4.2 billion in respect of all PPP contracts in place, with six PPPs in the education sector accounting for about 35% of this.
- 12.3** This report examines the control of expenditure on the education sector PPPs that are at the operational stage. In particular, it considers the adequacy of controls in place in respect of price indexation, service performance and benchmarking.
- 12.4** There are currently five PPPs in operation within the education sector. Three contracts relate to bundles of primary and post-primary schools with the remaining two relating to schools within the Cork Institute of Technology – the National Maritime College of Ireland and the Cork School of Music. All of the PPP contracts are on a design, build, finance, operate and maintain basis (DBFOM). The schools included in each PPP contract are set out in Annex A.
- 12.5** To date, the five PPP contracts have incurred cumulative expenditure of just over €300 million, with outstanding commitments estimated at over €1 billion (see Figure 12.1).

Figure 12.1 Expenditure on operational PPPs in the education sector

| PPP contract | Service commencement | Contract end | Expenditure | | Outstanding commitment ^a |
|---------------------------------------|----------------------|--------------|-------------|-----------|-------------------------------------|
| | | | Pre 2012 | In 2012 | |
| | | | €m | €m | |
| First/second level^b | | | | | |
| Pilot schools bundle | 2002 | 2027 | 107 | 11 | 188 |
| First schools bundle | 2010 | 2035 | 18 | 9 | 238 |
| Second schools bundle | 2011 | 2036 | 14 | 12 | 326 |
| Third level | | | | | |
| National Maritime College | 2004 | 2029 | 72 | 9 | 116 |
| Cork School of Music | 2007 | 2032 | 44 | 8 | 177 |
| Total | | | 255 | 49 | 1,045 |

Source: Department of Education and Skills

- Notes:
- a The outstanding commitment figure incorporates an assumed inflation rate of 4% for the pilot schools bundle, 2.5% for the Cork School of Music and 2% for the other contracts.
 - b Commitments of over €400 million in respect of the third schools bundle PPP (contract signed in November 2012) are not included because the project has yet to reach operational stage.

Contract Management Arrangements

- 12.6** The Department of Education and Skills (the Department) is the contracting authority for all PPP contracts in the education sector.
- 12.7** The National Development Finance Agency (NDFA) operates as the State's financial advisor in respect of public investment projects. In relation to PPPs in particular, a centre of expertise within the NDFA performs a specialised procurement delivery function, except in respect of local government projects and projects in the transport sector. Contracting authorities retain responsibility for assessing and approving projects and set the parameters within which the NDFA carries out its procurement function.
- 12.8** The remit of the NDFA was extended in September 2012 to allow it to provide contract management services in respect of PPP projects. Where contract management services are provided by the NDFA, the contracting authority generally retains responsibility for certain activities (see Figure 12.2).

Figure 12.2 NDFA role in contract management

| NDFA responsibilities | Contracting authority responsibilities |
|--|--|
| Reviewing and confirming amount of monthly unitary payments, including any performance related deductions. | Approval and payment of invoices (on receipt of NDFA recommendation). |
| Monitor PPP company performance against project agreements. | Approval of changes to the project agreement. |
| | Issuing warning or termination notices to the PPP company. |
| | Determination of benchmarking and market testing of testable services. |
| | Approval of changes to the ownership structure of the PPP company. |

- 12.9** Following a request for support from the Department, the NDFA took on certain functions in October 2012 for managing the contracts for all three bundles of first and second level schools. The Department stated that the decision to request support was made in view of the expertise and skills available within the NDFA for management of PPP projects. It cited resource issues within the Department as another consideration.
- 12.10** The Department has an 18 month service agreement with the NDFA for contract management services. The duration of the agreement can be extended if agreed by both parties and approved by the Department of Public Expenditure and Reform.
- 12.11** The NDFA has produced payment mechanism user guides for the Department for all three school bundle projects. Different management arrangements are in place for the two third level projects. The Department stated that it manages the payment process and Cork Institute of Technology (CIT) manages all other aspects of the contract. A staff member of CIT is named as the contract manager on behalf of the Minister for Education and Skills.
- 12.12** The CIT staff member acting as the contract manager for the two CIT projects has been involved with the projects since the procurement stage and has been involved in managing the contracts since the two projects became operational. The examination found that the contract manager has detailed knowledge of the project agreements.

Payment Indexation

- 12.13** The Department makes monthly unitary charge payments to the PPP company on all of the five operational PPP projects. Unitary charge payments will continue over the term of the contract. The charge is made up of two elements - a fixed cost element and a variable (indexable) element which changes in line with the Consumer Price All Item Index (CPI).
- 12.14** At each indexation review date (specified in the contract), the PPP company submits its calculation of the annual charge for the coming 12 month period. This is based on the terms set out in the payment mechanism schedule of the contract.
- 12.15** Certain information is required in order to calculate the annual unitary charge including
- key dates – the service commencement date and the unitary charge base date (i.e. the date from which indexation is to be applied)
 - CPI indexation values – the value at the base date and the value at review date
 - base date unitary charge values – the fixed and variable elements.
- 12.16** Once the indexation factor is determined, the annual unitary charge can be calculated by adding the fixed and adjusted variable values.
- 12.17** At the request of the Department, the NDFA carried out reviews of the indexation calculations submitted by the respective PPP companies during 2012 for each of the five PPP contracts.
- For the three schools projects, the NDFA found that the indexation calculations were correct.
 - For the Cork School of Music project, the NDFA noted an error resulting in an overcharge of €38,600 to the Department. The Department received the appropriate refund from the PPP company in February 2013. The NDFA subsequently reviewed the indexation calculations for 2011 and confirmed that the error had not occurred in that year.
 - For the National Maritime College, the NDFA noted that a 'utilities margin' had been inflated, which was not in accordance with the contract. It estimated that the potential overcharge arising from the error would have amounted to about €4,800 a year. Since the error was highlighted before the October 2012 invoice had been issued, the PPP company was able to adjust the invoice accordingly. The Department stated that it is currently examining whether any refund is due in respect of this issue.
- 12.18** This examination found that the indexation reviews carried out by the NDFA were calculated correctly and that the key information used was in accordance with that set down in the project agreement.

Monitoring Service Performance

- 12.19** Deductions can be applied to the unitary charges payable if the PPP company fails to satisfy performance standards as set out in the contract.
- 12.20** The two main types of deductions common to all five contracts relate to unavailability and service performance.¹
- Unavailability – a deduction is applied if an area does not meet one or more of the availability criteria set out in the project agreement
 - Service performance – a deduction is applied if the PPP company fails to meet the response time for a required performance standard set out in the project agreement e.g. relating to cleaning, heating or caretaking.
- 12.21** Under the terms of the contracts, PPP companies are obliged to report failures to meet availability and service performance requirements when they occur.

Helpdesk Calls Logged

- 12.22** The PPP companies provide a help desk facility, through which individual schools and colleges can submit service requests.
- 12.23** Under the three school bundle projects, a total of around 5,000 calls were logged by the fifteen schools during 2012. There was an average of around 470 calls per month between September and May, falling to around 250 per month during the June to August holiday period.
- 12.24** The rate of reporting of issues varies considerably between the fifteen schools. The highest number of calls reported to the helpdesk in 2012 from an individual school was 850, while the lowest was just 88.

Monthly Performance Reporting

- 12.25** PPP companies are also required to submit monthly performance reports outlining activities over the previous month. The reports detail any failures to meet service standards, the measures taken by the PPP company to address those service failures and the level of related deductions proposed. Under the service level agreement with the Department, the NDFA circulates the monthly performance reports to each school principal, seeking confirmation that all service failures are included and that the dates for submission and completion of service requests are correct. On receipt of feedback from schools, the NDFA ensures that the appropriate deduction (if any) has been made by the PPP company regarding the next monthly unitary charge payment.
- 12.26** The NDFA meets with the PPP companies on a monthly basis to discuss the performance monitoring report and any issues raised by the individual schools. Any outstanding issues relating to proposed deductions are also addressed at these monthly meetings.
- 12.27** The examination found several instances in 2012 where individual schools did not respond to the request from the NDFA seeking confirmation that the monthly performance report produced by the PPP company was complete and accurate. Payments to the PPP companies were not delayed in these cases. In effect, non response is treated as confirmation from the school that the monthly performance report is correct.

¹ The two most recent PPP contracts (School Bundles 1 and 2) include a further 'reporting' deduction which is applied to the unitary charge if the PPP company payment mechanism report omits details of an unavailability or service performance deduction.

Deductions Applied

12.28 No deductions were made to unitary payments by the Department in respect of any of the contracts prior to 2007. Figure 12.3 shows the deductions applied by the Department since 2007.

Figure 12.3 Deductions applied to project unitary charges, to end 2012

| | Pilot schools bundle | First schools bundle | Second schools bundle | National Maritime College | Cork School of Music |
|------|----------------------|----------------------|-----------------------|---------------------------|----------------------|
| | €000 | €000 | €000 | €000 | €000 |
| 2007 | 35 | | | — | — |
| 2008 | — | | | — | — |
| 2009 | — | | | — | — |
| 2010 | — | 57 | | — | — |
| 2011 | — | 695 | — | — | — |
| 2012 | 15 | 67 | 153 | — | — |

Source: The Department of Education and Skills
 Note: Indicates that schools were not operational.

12.29 Up to the end of 2012, the total deductions in respect of all PPP projects in operation were just over €1 million, which represented about 0.3% of the cumulative expenditure. The deductions were in respect of both unavailability and service performance issues post occupancy. The Department has stated that deductions in 2011 were mainly as a result of the main contractor (Pierse Contracting Ltd) going out of business just prior to the schools becoming operational with resultant unavailability of some services.

Benchmarking and Market Testing

12.30 Benchmarking and market testing processes are used in PPP contracts to ensure that the sponsoring authority is continuing to receive value for money in respect of contract services provided, over the life of the contract. Either the public or private partner can enforce the testing processes.

12.31 The testing is primarily focused on the services provided by the facilities management company. These services, commonly referred to as soft services, may include catering, cleaning, security and waste management services.

12.32 Benchmarking is the process by which the PPP company compares its own (or its subcontractors') charges for providing services to the current market price of equivalent services. If the PPP company charges are higher than the benchmark prices, the public body would receive a reduction in the unitary charge. The benchmarking process can result in an increase to the unitary charge where the PPP company charges are lower than the current market price level.¹

12.33 Where public and private partners do not agree on the outcome of a benchmarking process, the PPP contracts generally allow for the parties to carry out a market testing exercise.

¹ The individual project agreements specify the relevant percentage movement in the PPP company costs which would trigger a price change to the unitary charge.

- 12.34** Market testing involves the retendering by the PPP company of the relevant services in order to test the value for money of current services against competing market suppliers. Any increase or decrease in the cost of such services following market testing should be reflected by an adjustment in the unitary charge payable by the sponsoring authority.
- 12.35** In all five educational PPP contracts, the options of benchmarking and market testing are available in the fifth year of the operational stage and every five years thereafter. Consequently, the Department has had two opportunities to consider the potential for savings to be delivered through benchmarking in relation to the pilot schools bundle and one opportunity in relation to each of the CIT projects.
- 12.36** The examination found evidence that the Department had considered whether to invoke the benchmarking provisions, as opportunities arose under each of the contracts, but decided against it in each case. However, there was no documentary evidence of any detailed analysis supporting those decisions. Such analysis would need to identify current market costs for similar services and compare them to the charges for the services provided by the PPP company.

Third Party Income

- 12.37** In all five projects, the State parties to the respective contracts can receive income from third party use, catering or vending under the contract provisions.
- 12.38** In 2012, CIT received income totalling €44,000 in relation to the Cork School of Music. This was the minimum income CIT could have received as it was the guaranteed payment level set out in the contract. CIT also received €20,100 as its guaranteed share of third party use in respect of the National Maritime College.
- 12.39** The PPP contract for the National Maritime College provided for a further guaranteed minimum annual income that CIT would receive from the PPP company in relation to catering and vending, regardless of the actual level of income generated. The level of guaranteed annual income (subject to indexation) specified in the project agreement was €9,000 in the first contract year, rising in stages to €15,000 in the fifth contract year and remaining at that level thereafter.
- 12.40** At the end of 2008, the PPP company served notice to CIT that it was invoking the benchmarking provisions under the contract in relation to the catering and vending services, as it was becoming loss-making for the PPP company to provide the services. In 2009, the Department and the PPP company reached agreement that the PPP company would withdraw its request to trigger the benchmarking of the catering services in exchange for the cessation of that element of the guaranteed payments to CIT.

Conclusions and Recommendations

Contract Management Arrangements

- 12.41** PPP contracts are underpinned by project agreements that are complex and detailed. In order to manage the contracts effectively, the responsible staff need to fully understand the contract provisions, including the output specifications and payment mechanisms. Financial and technical skills are also required.
- 12.42** Within the NDFA, a multidisciplinary team is responsible for contract management of the schools bundles. Skill sets available include financial analysis, project management and engineering. The contract management services provided by the NDFA in respect of the school bundles since October 2012 have proven to be effective.
- 12.43** The CIT also has significant skills and experience in relation to the management of PPP contracts. However, there is a risk of over-reliance on a single individual, as much of CIT's capacity in this area is vested in the contract manager for the two CIT projects.
- 12.44** The Department's Accounting Officer stated that its move in the course of 2012 to vest responsibility for management of existing PPP schools contracts with the NDFA represented a significant change in the Department's approach. He indicated that the Department intends to further avail of the NDFA's expertise through outsourcing contract management arrangements for future PPP schools. The Department is also committed to exploring the potential for further NDFA involvement in contract management for the CIT projects.

Payment Indexation

- 12.45** The NDFA identified errors in the indexation calculations submitted by the respective PPP companies in 2012 in respect of the National Maritime College and Cork School of Music projects.

Recommendation 12.1: All future annual indexation calculations submitted by PPP companies should be forwarded to the NDFA for review.

Accounting Officer's Response: Agreed. This recommendation is already being implemented. Arrangements are in place for the NDFA to review indexation calculations.

Recommendation 12.2: In light of the errors identified by the NDFA in respect of indexation calculations for 2012, the Department should satisfy itself that calculations for prior years were correct and that no overpayments have been made.

Accounting Officer's Response: Agreed. The Department will pursue the question of the NDFA conducting further sample checks for the pre-2012 period in respect of the pilot schools and third level colleges with a view to verifying the accuracy of previously conducted internal checks.

Monitoring Service Performance

- 12.46** Feedback from schools on service performance issues provides valuable information on whether contracted services are being received. Several instances in 2012 were noted where schools did not respond to the request from the NDFA to confirm that the monthly performance reports prepared by PPP companies were complete and accurate.

Recommendation 12.3: The Department should remind schools staff responsible for monitoring service delivery of the importance of providing formal feedback on the monthly performance monitoring reports to ensure that contracted services are being delivered and that deductions, where appropriate, are being applied.

Accounting Officer's Response: Agreed. The Department will continue to ensure that robust and effective systems are in place to monitor service performance and will re-iterate to the schools involved the importance of providing formal confirmation of the accuracy and completeness of the monthly performance reports.

Benchmarking and Market Testing

- 12.47** Benchmarking provisions in PPP contracts provide an opportunity to test at regular intervals whether the price paid for contract services remains competitive. In the past, this was not done by the Department. A benchmarking exercise requested by the Courts Service in 2011 resulted in an 8% reduction in the costs of certain services at the Criminal Courts complex.

Recommendation 12.4: As future opportunities arise, the Department should consider whether savings could potentially be delivered by way of benchmarking and market testing and should document the reasons for proceeding, or not, as appropriate.

Accounting Officer's Response: Agreed. The Department is acutely aware of the option for benchmarking and will continue to keep the option under review and to document the reasons for its decisions.

Annex A Schools included under PPP Contracts

| PPP contract name/school name | Location | County | Service commencement date |
|---------------------------------------|--------------|----------|---------------------------|
| Pilot schools bundle | | | |
| 1. Ballincollig Community School | Ballincollig | Cork | November 2002 |
| 2. Largy College | Clones | Monaghan | December 2002 |
| 3. Maria Immaculata Community College | Dunmanway | Cork | November 2002 |
| 4. St. Attracta's Community School | Tubbercurry | Sligo | November 2002 |
| 5. St. Caimin's Community School | Shannon | Clare | November 2002 |
| First schools bundle | | | |
| 1. Gallen Community School | Ferbane | Offaly | October 2010 |
| 2. St Mary's CBS | Portlaoise | Laois | August 2010 |
| 3. Scoil Chríost Rí | Portlaoise | Laois | July 2010 |
| 4. Banagher College | Banagher | Offaly | October 2010 |
| Second schools bundle | | | |
| 1. Gaelscoil Bheantraí ^a | Bantry | Cork | July 2011 |
| 2. Bantry Community College | Bantry | Cork | October 2011 |
| 3. Kildare Town Community School | Kildare | Kildare | October 2011 |
| 4. Abbeyfeale Community College | Abbeyfeale | Limerick | August 2011 |
| 5. Athboy Community School | Athboy | Meath | October 2011 |
| 6. Wicklow Town Community College | Wicklow | Wicklow | September 2011 |

Source: Department of Education and Skills, NDFA

Note: a Primary school. All others are post-primary.