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## **ADDENDUM TO DAO(GEN)02/14**

3 March 2015

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**Dear Accounting Officer**

### **Early Termination of PPP and PFI Contracts**

This letter follows on from DAO (Gen) 02/14 on the early termination of contracts providing further guidance specifically related to the early termination of PFI or PPP contracts through no fault of the supplier.

Please contact the following to deal with enquiries about this DAO:

- Specific cases: Peter Livesey, PPP Policy Team, IUK, HM Treasury on 020 7270 1021 or at [peter.livesey@hmtreasury.gsi.gov.uk](mailto:peter.livesey@hmtreasury.gsi.gov.uk);
- Regularity or propriety issues: Jim Duncan, TOA, on 0207 270 4833 or at [Jim.duncan@hmtreasury.gsi.gov.uk](mailto:Jim.duncan@hmtreasury.gsi.gov.uk)

#### **Action**

Each Accounting Officer should ensure that his or her staff are aware of the guidance in this letter and act accordingly. The guidance applies to arms' length bodies as well as to their sponsor departments.

#### **Context**

DAO 2/14 notified departments of Public Accounts Committee concerns over the inclusion of "termination for convenience" clauses in contracts providing for compensation to be paid to suppliers based on projected supplier profits to contract end where a contract is terminated by the public body, through no fault of the supplier. The DAO reminded Accounting Officers of their personal responsibilities in ensuring that the decision to include such a clause provides value for money and that the decision can be explained.

We are aware that some public sector contracting authorities in both central and local government (“Authorities”) are currently considering the option of exercising such clauses leading to the early voluntary termination of a PFI arrangement. The attached Addendum provides guidance specifically related to the early termination of PFI or PPP contracts in such circumstances.

A handwritten signature in black ink that reads "RDBrown". The signature is written in a cursive style with a horizontal line underneath the name.

**Richard Brown**  
**Treasury Officer of Accounts**

**Early termination of a PFI or PPP contract, where the contract is terminated by the public body at no fault of the supplier**

**PFI or PPP contract termination should be regarded as a novel, contentious and potentially repercussive transaction within the terms of *Managing Public Money*, for which business case approval must be sought by the proposing Authority from its sponsoring department. They must in turn seek the consent of HM Treasury.**

Termination of existing contracts will normally only be approved by the Treasury where it is likely that it will result in a significant improvement in the delivery of public value for money. Authorities should not work up proposals for termination unless they have strong reason to believe that such action gives a reasonable prospect of improving public value.

Any proposal for termination therefore requires a careful cost-benefit appraisal to determine whether it represents better value for money compared with leaving existing contract arrangements in place. A business case must be submitted for approval to the sponsoring department, which must in turn share it with, and seek approval from, the Treasury.

The value for money assessment carried out by the Authority must take into account both quantitative and qualitative factors and should be carried out in accordance with the *Green Book*. Value for money should be assessed from the perspective of the public sector as a whole, rather than from the perspective of an individual Authority or department, taking into account the impact on all public services. Tax paid by the Contractor should be deducted from the costs falling to the Authority in any given period in order to reflect true resource costs and allow a fair comparison of economic efficiency based on a level playing field.

Although the key consideration in assessing a case for termination will be the impact on value for money for the public sector as a whole, Accounting Officers should also consider other relevant factors in the assessment of the case for termination including:

- a. The affordability of the proposal to the sponsoring department;
- b. The opportunity cost of funding or providing financial support to a termination;
- c. The resources required and the ability of the terminating authority to continue to provide the services provided under the contract;
- d. The resources required and the ability of the terminating authority to successfully negotiate a public value for money outcome;
- e. For a local authority PFI, the terms and conditions of any grant support payments;

- f. The relative priority of the proposed termination against any other possible termination, in an environment of constrained resources.

The Treasury will consider the business case according to *Green Book* and Business Case Guidance in the context of the public sector as a whole.

Further technical guidance will be issued to departmental contacts shortly.