



Committee of Public Accounts

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The Scottish Parliament
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23 November 2015

Dear Paul,

THE IMPACT OF OFFICE FOR NATIONAL STATISTICS CLASSIFICATION DECISIONS UPON CAPITAL INFRASTRUCTURE PROJECTS

Thank you for your letter of the 22nd October 2015 regarding the impact of Office for National Statistics (ONS) classification decisions upon capital infrastructure projects.

It is a requirement for European Union countries to compile National Accounts on the basis of the European System of Accounts (ESA). The ONS is responsible for the production of the UK National Accounts in line with the ESA, and in accordance with rules issued by Eurostat (the statistical body of the European Union). We are aware of the issues presented by the transition to the ESA 2010 standards, including the changes to the Eurostat interpretation of these standards provided through the Manual of Government Deficit and Debt, and the impact of these changes upon the National Accounts classification of some bodies.

To date, our Committee has not given explicit consideration of National Accounts classifications as determined by the ONS. This is because of the ONS's statutory independence in relation to classification decisions. However, the National Audit Office (NAO) has addressed some of the background to classification decisions and their impact as a part of its body of work for the Committee. The following reports have touched upon such classification matters, and address alternative forms of finance to fund capital spending:

1. *Financial institutions landscape*, September 2015¹
The report outlines the principal sources of guidance available regarding the classification of public bodies, including the relevance of ONS, HM Treasury and Cabinet Office guidance.
2. *The choice of finance for capital investment*, March 2015²
This report details the budgetary impact of financing options, and how the various options may impact the risk allocation between the private sector, taxpayers and consumers.
3. *UK Guarantees scheme for infrastructure*, January 2015³
This report examines the risks to value for money associated with guarantees for infrastructure projects. Figure 8 of the report details the range of National Accounts treatments (both on-

¹ National Audit Office, *Financial institutions landscape*, September 2015 <https://www.nao.org.uk/report/financial-institutions-in-government/>

² National Audit Office, *The choice of finance for capital investment*, March 2015 <https://www.nao.org.uk/report/the-choice-of-finance-for-capital-investment/>

³ National Audit Office, *UK Guarantees scheme for infrastructure*, January 2015 <https://www.nao.org.uk/report/uk-guarantees-scheme-for-infrastructure/>

and off- balance sheet) of five projects supported by government guarantees under the scheme.

4. *Review of the VFM assessment process for PFI*, October 2013⁴

This report examines the value for money assessment process and model for the Private Finance Initiative (PFI) but does not refer to any relationship between classification decisions and whether to fund a project through private finance.

5. *Lessons from PFI and other projects*, April 2011⁵

This report summarises the advantages and disadvantages associated with the use of private finance. The report highlights an incentive to use private finance due to its exclusion from Public Sector Net Debt; an incentive which in many cases may be lost due to the transition to ESA 2010. The report reasserts that decisions ought to be based "on value for money criteria, rather than [for] accounting treatment reasons."

6. *Financing PFI projects in the credit crisis and the Treasury's response*, July 2010⁶

The report provides an overview of common methods of infrastructure funding by sector, and provides example cases for each. It also provides a narrative summary of developments in the use of private finance prior to 2010.

We are aware that future NAO studies will also touch upon the impact of classification decisions, including:

6. *Companies in Government*, Winter 2015

This landscape review will set out the extent of the government's portfolio of companies, along with its oversight of this portfolio. The report will specifically refer to the classification of entities as 'companies in government', and will set out a description of the classification process, and the indicators of public sector control considered by ONS.

7. *Government balance sheet work programme*, Winter 2015

This planned series of reports will cover different aspects of the government balance sheet; the purpose is to provide an examination of risk exposure and management of the UK public finances. This will address differences between National Accounts and financial reporting.

I am also aware that the following committees of both the House of Commons and the House of Lords have previously inquired into and reported on this subject:

8. *House of Commons Treasury Committee*

The Committee's 2014 report, *Private Finance 2*⁷, addresses the accounting and budgetary incentives associated with private finance structures. The Committee's 2011 report, *Private Finance Initiative*⁸, also identifies the risk that such structures may encourage the use of private finance for reasons other than value for money. In this report, they recommend that "the form

⁴ National Audit Office, *Review of the VFM assessment process for PFI*, October 2013 <https://www.nao.org.uk/report/review-vfm-assessment-process-pfi/>

⁵ National Audit Office, *Lessons from PFI and other projects*, April 2011 <https://www.nao.org.uk/report/lessons-from-pfi-and-other-projects/>

⁶ National Audit Office, *Financing PFI projects in the credit crisis and the Treasury's response*, July 2010 <https://www.nao.org.uk/report/financing-pfi-projects-in-the-credit-crisis-and-the-treasurys-response/>

⁷ House of Commons Treasury Committee, *Private Finance 2*, March 2014 <http://www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/inquiries1/parliament-2010/private-finance-2/>

⁸ House of Commons Treasury Committee, *Private Finance Initiative: Government, OBR and NAO Responses to the Seventeenth Report from the Committee*, December 2011 <http://www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/inquiries1/parliament-2010/private-finance-initiative-/>

of financing which should be chosen for projects should be that which offered best value for money, regardless of accounting considerations."

9. *House of Commons Transport Committee*

The Committee considered this subject in light of the reclassification of Network Rail. Their report *Investing in the railway*⁹ highlights some of the practical impacts of reclassification, including impacts upon governance and accountability, future funding and government guarantees.

10. *House of Lords Select Committee on Economic Affairs*

In its 2010 report *Private Finance Projects and off-balance sheet debt*¹⁰, the Committee identifies an "institutional bias in favour of private financing of public procurement" and recommends taking a broader view of value for money when assessing the merits of procurement routes for projects.

11. *House of Commons Library*

Briefing Paper 6007¹¹, published in May 2015, provides a useful summary of current developments in the use of private finance in delivering public services. It provides a summary of the costs and benefits associated with private finance, and touches upon accounting for PFI projects in the National Accounts.

I hope you find the above consideration useful. Should you require any further information please do not hesitate to contact the Clerk, Stephen McGinness on 020 7219 3273 or by e-mail at Stephen.mcginness@parliament.uk.

Yours sincerely,



Meg Hillier MP,
Chair of the Committee of Public Accounts

⁹ House of Commons Transport Committee, *Investing in the railway*, January 2015
<http://www.parliament.uk/business/committees/committees-a-z/commons-select/transport-committee/inquiries/parliament-2010/railway-investment/>

¹⁰ House of Lords Select Committee on Economic Affairs, *Private Finance Projects and off-balance sheet debt*, March 2010
<http://www.publications.parliament.uk/pa/ld200910/ldselect/ldeconaf/63/63i.pdf>

¹¹ House of Commons Library, *Briefing Paper 6007 PFI: costs and benefits*, May 2015
<http://researchbriefings.parliament.uk/ResearchBriefing/Summary/SN06007>