OUTLINE

1. INTRODUCTION: PFIs & PPPs
2. BIRTH
3. GROWTH
4. DEATH
5. RESURRECTION
6. SOME CONCLUDING REMARKS
INTRODUCTION

What are Private Finance Initiative (PFI) contracts and Public Private Partnerships (PPP) arrangements?

Does accounting matter?
INTRODUCTION: PFI & PPP

PRIVATE FINANCE INITIATIVE (PFI)

PUBLIC PRIVATE PARTNERSHIPS
BROAD VIEW (Treasury, 2000; Kernaghan)
FEATURES OF PFI DEALS

- They are constructed as service contracts.
- Usually back by significant capital assets (roads, hospitals, prisons etc).
- They are long-term (e.g. 30+ years).
- Public sector pays an annual service charge based on availability and service performance.
- The private sector provider is typically a consortium headed by a shell company (SPV).
INTRODUCTION: FORMS OF PPP/PFI ACCOUNTABILITY

1. ACCOUNTABILITY FOR VALUE FOR MONEY
   - Contractual arrangements, risk transfer, authorisation and monitoring arrangements.

2. POLITICAL ACCOUNTABILITY
   - Of an executive body to a legislature on behalf of citizens (for public policy).

3. FINANCIAL ACCOUNTABILITY
   - By individual entities (financial accounting) or governments (national / whole of govt accounts).
THE MAJOR QUESTIONS ON ACCOUNTING FOR PPP

WHOSE ASSETS?

HOW WILL THEY BE PAID FOR?
ALTERNATIVE FINANCIAL ACCOUNTING TREATMENTS


<table>
<thead>
<tr>
<th>Grantor Assets</th>
<th>Operator Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>On the (public sector) B.S.</td>
<td>Off the (private sector) B.S.</td>
</tr>
<tr>
<td>Double Counted Assets</td>
<td>Orphan Assets</td>
</tr>
<tr>
<td>On the (public sector) B.S.</td>
<td>Off the (public sector) B.S.</td>
</tr>
<tr>
<td>Off the (private sector) B.S.</td>
<td>Off the (private sector) B.S.</td>
</tr>
</tbody>
</table>

BIRTH
THE EARLY YEARS OF PFI

- 1992: Conservative Government (Major) introduces PFI.
- It is made compulsory for consideration as a method of financing public schemes >£1M.
- Major capital assets are key to development of these schemes (Mayston, 1999).
- Very few schemes reach financial closure.
Number and Capital Value of Signed PFI Schemes

Ron Hodges
Inaugural Address 30 October 2013
There was an absence of specific disclosure requirements about PFI; little was disclosed in the accounts of public sector entities (Hodges and Mellett, 1999).

It becomes apparent that public sector obligations can be made ‘off-balance sheet’.

Interim guidelines for the public sector (Treasury Taskforce, 1997) were based on a loose interpretation of risks and rewards.
GROWTH
GROWTH YEARS OF THE PFI

- PFI takes off; it’s ‘the only game in town’.
- New Labour Govt (Blair) supports PFI/PPP, increased focus, restructures policy units.
- Schemes get bigger or are combined.
- Adaption to new sectors (e.g. social housing) remains problematic (Grubnic and Hodges, 2003; Hodges and Grubnic, 2005).
Number and Capital Value of Signed PFI Schemes

Ron Hodges
Inaugural Address 30 October 2013
## PFI cumulative capital £m

*(to February 2010)*

<table>
<thead>
<tr>
<th>Department</th>
<th>£m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Children, Schools &amp; Families</td>
<td>6,469</td>
</tr>
<tr>
<td>Health</td>
<td>11,244</td>
</tr>
<tr>
<td>Transport</td>
<td>12,029</td>
</tr>
<tr>
<td>Local government</td>
<td>2,056</td>
</tr>
<tr>
<td>Defence</td>
<td>8,805</td>
</tr>
<tr>
<td>Environment, Food and RA</td>
<td>2,687</td>
</tr>
<tr>
<td>Northern Ireland</td>
<td>1,737</td>
</tr>
<tr>
<td>Scotland</td>
<td>5,696</td>
</tr>
<tr>
<td>Others (each below £1.5 billion)</td>
<td>4,925</td>
</tr>
<tr>
<td><strong>Total (excludes approx £10 billion Tube PPP)</strong></td>
<td><strong>55,668</strong></td>
</tr>
</tbody>
</table>

*Source: Treasury 2011*
Private sector accounting is developed through an ASB (1998) standard FRS 5, based on a ‘risks and rewards’ analysis.

At the development stage the accounting firms and professional bodies support the ASB’s approach while the Treasury, govt departments, operators, developers do not (Hodges & Mellett, 2002; Broadbent and Laughlin, 2002).

## PFI: Treatment of capital values based upon UK GAAP

(Hodges and Mellett, 2012)

<table>
<thead>
<tr>
<th>Department</th>
<th>£m</th>
<th>CapVal £m ON</th>
<th>CapVal £m OFF</th>
<th>Projects ON</th>
<th>Projects OFF</th>
</tr>
</thead>
<tbody>
<tr>
<td>Children, Schools &amp; Families</td>
<td>6,469</td>
<td>1,101</td>
<td>5,368</td>
<td>17</td>
<td>124</td>
</tr>
<tr>
<td>Health</td>
<td>11,244</td>
<td>380</td>
<td>10,864</td>
<td>7</td>
<td>94</td>
</tr>
<tr>
<td>Transport</td>
<td>12,029</td>
<td>9,363</td>
<td>2,666</td>
<td>23</td>
<td>29</td>
</tr>
<tr>
<td>Local government</td>
<td>2,056</td>
<td>0</td>
<td>2,056</td>
<td>0</td>
<td>60</td>
</tr>
<tr>
<td>Defence</td>
<td>8,805</td>
<td>1,150</td>
<td>7,655</td>
<td>12</td>
<td>38</td>
</tr>
<tr>
<td>Environment, Food and RA</td>
<td>2,687</td>
<td>635</td>
<td>2,052</td>
<td>1</td>
<td>21</td>
</tr>
<tr>
<td>Northern Ireland</td>
<td>1,737</td>
<td>864</td>
<td>873</td>
<td>15</td>
<td>21</td>
</tr>
<tr>
<td>Scotland</td>
<td>5,696</td>
<td>847</td>
<td>4,849</td>
<td>9</td>
<td>76</td>
</tr>
<tr>
<td>Others (each &lt;£1.5 billion)</td>
<td>4,925</td>
<td>1,104</td>
<td>3,821</td>
<td>32</td>
<td>79</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>55,668</td>
<td>15,464</td>
<td>40,204</td>
<td>116</td>
<td>542</td>
</tr>
</tbody>
</table>
ACCOUNTING FOR PFI

Some difficulties

- Distinctions between what contacts which are ‘on’ and which are ‘off’ balance sheet may be marginal and may distort VFM issues (Heald, 2003).
- It is impossible to compare entities using the two different treatments (Hodges & Mellett, 2004).
- Disclosures in private sector accounts do not compensate for lack of public sector disclosures. There is some evidence that assets may not be on anyone’s balance sheet! (Edwards et al, 2004)
DEATH

Ron Hodges  Inaugural Address 30 October 2013
DEATH: of UK GAAP accounting for PFI

UK Listed Companies adopt IFRS from 2005

UK Government sector adopts IFRS from 2009/10

IFRIC 12 Service Concessions

IPSAS 32 Service Concessions: Grantor
The recognition of assets is based upon power to ‘control and regulate’ the use of those assets.

Recognition of obligations as either a financial liability or as deferred income.

Likelihood of bringing schemes onto public sector balance sheets.
UK Treasury Flow Chart for Public Sector PPP Client under IFRIC 12

**CONTROL OF THE INFRASTRUCTURE?**

**SIGNIFICANT RESIDUAL INTEREST IN THE INFRASTRUCTURE?**

**INFRASTRUCTURE ALREADY OWNED OR CONSTRUCTED BY THE OPERATOR?**

**REPORT ASSET AND RELATED LIABILITY USING ON BALANCE SHEET TREATMENT.**

**ON PUBLIC SECTOR ON BALANCE SHEET (IASB IFRIC12 MIRROR IMAGE / IPSAS 32)**

**IS A LEASE INCLUDED?**

**LEASE ACCOUNTING FOLLOWING IAS 17**

**INFRASTRUCTURE OF THE GRANTOR, OPERATOR IS GIVEN ACCESS**

**INFRASTRUCTURE ON BALANCE SHEET AS PP&E (IAS 16) OR AS A LEASED ASSET (IAS 17)**

**ON PUBLIC SECTOR BALANCE SHEET UNDER IAS16 OR IAS17**

**RECOGNISE AS EXPENDITURE**

**OFF PUBLIC SECTOR BALANCE SHEET – TREATED AS CURRENT EXPENDITURE**

Source: HM Treasury (2008, with additional explanation)  Inaugural Address 30 October 2013
## PFI: treatment of capital values based on IFRS / IPSAS

(Hodges & Mellett, 2012)

<table>
<thead>
<tr>
<th>Department</th>
<th>£m</th>
<th>CapVal £m ON</th>
<th>CapVal £m OFF</th>
<th>Projects ON</th>
<th>Projects OFF</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education</td>
<td>2,190</td>
<td>2,190</td>
<td>0</td>
<td>38</td>
<td>0</td>
</tr>
<tr>
<td>Health</td>
<td>11,887</td>
<td>11,530</td>
<td>357</td>
<td>111</td>
<td>4</td>
</tr>
<tr>
<td>Transport</td>
<td>6,644</td>
<td>5,547</td>
<td>1,097</td>
<td>46</td>
<td>10</td>
</tr>
<tr>
<td>Local government</td>
<td>1,538</td>
<td>1,298</td>
<td>240</td>
<td>41</td>
<td>6</td>
</tr>
<tr>
<td>Defence</td>
<td>9,064</td>
<td>9,064</td>
<td>0</td>
<td>46</td>
<td>0</td>
</tr>
<tr>
<td>Environment, Food and RA</td>
<td>3,059</td>
<td>0</td>
<td>3,059</td>
<td>0</td>
<td>24</td>
</tr>
<tr>
<td>Northern Ireland</td>
<td>1,786</td>
<td>1,583</td>
<td>203</td>
<td>26</td>
<td>11</td>
</tr>
<tr>
<td>Scotland</td>
<td>5,704</td>
<td>5,704</td>
<td>0</td>
<td>84</td>
<td>0</td>
</tr>
<tr>
<td>Others (each &lt;£1.5 billion)</td>
<td>4,728</td>
<td>4,583</td>
<td>145</td>
<td>91</td>
<td>8</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>46,600</td>
<td>41,499</td>
<td>5,101</td>
<td>483</td>
<td>63</td>
</tr>
</tbody>
</table>
Bringing PFI on balance-sheet: University Hospitals Birmingham NHSFT

- 2010/11 Accounts
- Additions to Fixed Assets of £479.6M
- Impairment cost £243.6M
- Borrowings up £448M
- Loss for year = £252.3M
- Net liabilities = £32.9M

THE FINANCIAL CRISIS & PFI

The financial completion of PFI schemes starts to dry up:

2008 = 63 schemes
2009 = 22 schemes.

PFI investment is bought into the public sector.

Ron Hodges  
Inaugural Address 30 October 2013
PFI GETS INVESTIGATED
PFI IS RESURRECTED

- March 2009 – the Treasury creates an ‘Infrastructure Finance Unit’ to support PFI projects under procurement.
- December 2012 – the Treasury announces ‘a new approach to public private partnerships’.
- This is PF2.
PF2: Some key features

- Public sector minority equity interest
- Public sector board membership
- Long term equity e.g. pension funds
- No windfall gains, use lifecycle reserves
- Greater transparency – private sector gains, off-balance sheet PFI control totals, procurement stage plans.
- Efficiency, flexibility, risk transfer...blah, blah
1. INTRODUCTION: PFIs & PPPs
2. BIRTH
3. GROWTH
4. DEATH
5. RESURRECTION
6. SOME CONCLUDING REMARKS
ACCOUNTING FOR PFI: SOME CONCLUDING REMARKS

- Accounting both communicates and creates realities (Hines, 1988).
- If PFI is a ‘Great British export’ then accounting for it is not.
- Academic commentators!
- WOT? NO IMPACT?
WHAT NEXT FOR PUBLIC SECTOR OFF-BALANCE SHEET FINANCE?

- It’s Guaranteed!!


Ellwood, S. (2012), Accounting Magic; (dis)appearing hospitals, mimeo, University of Bristol.


REFERENCES... possibly mentioned today


Treasury (2011), PFI deals signed March 2011, [www.hm-treasury.gov.uk/ppp_pfi_stats.html](http://www.hm-treasury.gov.uk/ppp_pfi_stats.html)

Thanks for listening... if you were

Ron Hodges  Inaugural Address 30 October 2013