

**MINUTES OF THE 72nd FRAB MEETING HELD ON
MONDAY 7th MARCH AT HM TREASURY
COMMENCING AT 12.00**

Present: Elwyn Eilledge (Chair)
John Aldridge
Ross Cranston
Russell Frith
Robin Lynch
Martin Sinclair
Ken Wild
Tomas Wilkinson
Mike Ashley
Beverley Evans
David Heald
Michael Romberg
John Thornton

Secretariat: David Watkins (Secretary)
Sarah Solomon
Chris Ruston

1. The Chairman welcomed everyone to the meeting. Apologies were received from Martin Evans, Heather Foster, Nigel Reader, David Thomson (who was substituted for by Tomas Wilkinson), Jeff Tomlinson and Trevor Woolley (substituted for by John Thornton).

***Item 1: Minutes of the Last Meeting: Paper FRAB (72) 1
and Matters Arising***

2. The minutes of the last meeting were agreed.
3. The Treasury had spoken to TOA with reference to paragraph 23 of the last minutes, and concluded that, as the Accounting Officer has to take responsibility for the Remuneration Report, it should continue to be the Accounting Officer, and not the chair of the Remuneration Committee, who signs the report.
4. In Paragraph 24 of the minutes Jeff Tomlinson asked that the FReM should reinforce the fact that prior consent of individuals named in the Remuneration Report has to be obtained before personal information can be disclosed. This point was already covered, but the FReM was amended to introduce the point at an earlier stage.

Item 2: Private Finance Initiative (PFI): Consistency Of Accounting Treatment Adopted By The Public And Private Sectors – Progress Report (FRAB (72)2)

Background

5. The Treasury presented this paper which provided an update on the progress made on action points lying with it in achieving consistency of accounting treatment adopted by the public and private sectors for PFI projects.
6. HM Treasury explained the action taken on promoting Value for Money, and that it had issued its “Value for Money Guidance” to departments in August 2004, with the primary intention of ensuring that Value for Money was the sole determinant of the decision to use PFI in procurement and that the balance sheet treatment of projects was immaterial to the decision. HM Treasury’s Corporate and Private Finance Team is enforcing the guidance.
7. The Treasury reported that it had successfully communicated to departments that they should not use the Method Statement, which had never been formally issued. This message was made clear in the Value for Money Guidance, and the message was further reiterated in meetings between Treasury and departmental Private Finance Units.
8. The Treasury reported it had held robust discussions with the Department of Health and the Department for Education and Skills on their sectoral PFI guidance. As a result, the departments have removed their guidance from their respective websites. Both departments at Treasury’s request are additionally reviewing their guidance to ensure that it is compliant with the Treasury’s Value for Money Guidance and with the Technical Note 1. It was confirmed that the guidance would be revised in the next few months and Treasury continues to monitor departments’ progress.
9. The Treasury reported it had received helpful suggestions from the NAO and the Audit Commission in relation to how Technical Note No 1 might be amended. There had been no suggestions for amendment from the Northern Ireland Audit Office or Audit Scotland, although the Northern Ireland Audit Office had recently confirmed that it concurred with NAO’s suggestions for amendment. The Treasury warned that successfully amending Technical Note 1 involved significant difficulties. These included:
 - a. the difficulty from a drafting perspective in fully understanding how the effects of proposed amendments may impact in practice on future auditing determinations by the National Audit agencies, and the need for consensus on their practical interpretation;

- b. the length of time involved in gaining ASB agreement to proposed amendments post consultation, post FRAB;
 - c. the burdens that may be imposed on bodies having to revisit the accounting treatments of schemes due to the retrospective effect of any changes to Technical Note 1.
10. The Treasury also expressed its wish to take into account international developments, e.g. the work being undertaken on service concessions, before committing to amending the Technical Note.

The Board's comments on the progress made by the Treasury

11. Board members were generally supportive of the progress made by the Treasury, but remained concerned at the lack of consistency across the public sector: David Heald, Martin Sinclair and Tomas Wilkinson all referred specifically to schools and hospitals. They reiterated the point that the PFI accounting guidance was being interpreted differently. Martin Sinclair noted that the Method Statement, whilst never having been formally issued, still appeared to be used in certain areas. His concern was that telling departments not to use it might not work.
12. Ken Wild, agreeing that progress was being made in the right direction, suggested that the Treasury should remind departments of the original principles underlying FRS 5 Application Note F. Like items should be treated like for like. Martin Sinclair highlighted the fact that the accounting treatment of PFI projects needs to be resolved in time for Whole of Government accounts, as the inconsistencies across the public sector would cause difficulties for the audit opinion. He suggested that withdrawing Technical Note No 1 and relying solely on FRS 5 might help, if it was not possible to amend it. It was noted, however, that the use of the Technical Note is entrenched and withdrawal was unlikely to achieve the desired aim. The Board agreed that the Treasury should look again at Technical Note 1 to see how it might be amended, and that it should report back in the early summer.
13. The Treasury nominee warned that departments worried about unexpected decisions by the auditors at a late stage in the process. He would be concerned about compliance costs and diminished usefulness of reports if new guidance was issued only to be revised a little later if the accounting framework changed.
14. While Ross Cranston felt that the Value for Money (VFM) approach addresses political concerns he wondered where the assessment of VFM came in the process: to what extent is there scope for review of VFM evaluation and to what extent is there publication of any evaluation so that decisions are open to scrutiny?

15. At the start of the meeting, the Secretary tabled the three draft interpretations issued on 3 March by the International Financial Reporting Interpretations Committee (IFRIC): D12 (Service Concession Arrangements – Determining the Accounting Model); D13 (Service Concession Arrangements – the Financial Asset Model); and D14 (Service Concession Arrangements – the Intangible Asset Model). Subject to due process, (comments are due by 3 May), the interpretation will apply to accounting periods beginning on or after 1 January 2006, and will apply only to operators' accounts. The accounting treatment to be applied by grantors (the public sector) is not covered. There are two models: the financial asset model where the grantor pays the operator direct, and the intangible asset model where the operator is paid by a third party.
16. Ken Wild commented on the thinking behind the draft Interpretations, which were then discussed briefly on the presumption that if the operator had only a receivable (financial asset) or an intangible, the apparent consequence was that the physical asset would be on the public sector balance sheet, since, in the context of the Interpretations, the grantor "controlled" the asset. This approach is different to the "risks and rewards" approach in FRS 5. However it was acknowledged that FRS 5 would eventually change under the ASB convergence programme, although it was likely that it would be one of the last standards tackled, possibly in four to five years' time.
17. Members noted that some departments were starting to think about possible changes to PFI accounting. In the MoD people were trying to anticipate the changes in rules and the assumption was that everything would be on the balance sheet. The Scottish Executive felt there was more certainty about how the rules might change and some projects weren't going ahead because they couldn't afford for them to be on balance sheet. In Northern Ireland projects planned for 2008 that were expected to be off balance sheet, may now be considered on balance sheet and as a consequence may not go ahead. Foundation Trusts, have particular worries about debt/equity issues and look at liquidity as a factor in whether or not they should go ahead with a project. In some cases projects may be affordable in resource terms, but not as capital, where the full expense hits the budget in one go.
18. It was agreed that the FRAB should respond to the paper. Ken Wild, David Heald, Robin Lynch and Martin Sinclair should form the subgroup. They also suggested that Martin Evans who was not present at the meeting should also be part of the group. The working group would also draw on the Treasury's expertise. It was felt that the Board could comment on the areas of interpretation, although the areas relating to the balance sheet were unlikely to be changed. The paper would be circulated to the Board for comment before being sent to IFRIC by 3 May.

Item 3: Review of Corporate Governance in Central Government Departments

19. The Treasury presented a progress report on the review of corporate governance in central government departments.
20. The Chief Secretary wrote to Cabinet colleagues in January and the draft code is currently being considered with a view to it being introduced from 1 April 2005.
21. The code largely draws together established (and published) practice in central government departments, together with some advisory guidance reflecting private sector practice set out in the Combined Code for listed companies. Once departments have moved to the new code, a more radical agenda will be considered. The code was still developing, in particular in relation to the role of ministers in relation to the Board.
22. In response to a question from Ross Cranston regarding audit coverage, the Treasury said there was no statutory basis for the code, although in some cases departments have a Board based on a statutory requirement. However the NAO do comment on Statements of Internal Control. John Aldridge was concerned that some of the provisions were not appropriate to devolved administrations, for instance, the relationship between ministers and Accounting Officers.
23. The Treasury explained that the summary of key features was intended to clarify the limitations of the code.
24. The full code would be circulated before the end of the month under a Dear Accounting Officer letter. (FRAB members will receive a copy.)

Item 4: The Government Financial Reporting Manual

25. The Secretary presented this paper which brought together the whole Manual. The Secretariat demonstrated the new FReM website.
26. The Board had not previously seen chapter 3 (Statement of Parliamentary Supply), chapter 6 (Balance sheet – other assets and liabilities) and chapter 7 (annual reports and accounts) and associated annexes. The chapters that the Board has already seen have been amended where necessary to reflect the Board's comments. The Secretariat was happy to receive any further drafting suggestions.
27. Chapter 3 deals with the Statement of Parliamentary Supply. It reflects the agreement reached between the Treasury, the parliamentary authorities and the NAO that the accounts should not at this time, contain notes reconciling accounts to budgets. Discussions are ongoing but it is hoped that they will be completed in time for the May

meeting. Chapter 3 is unlikely to change as a result of those discussions.

28. Chapter 7 proposes that departments be required to analyse the information in and supporting the operating cost statement between core and consolidated (or parent and group) as well as provide the balance sheet analysis. The Secretary is currently working with Treasury colleagues and the Scrutiny Unit, and will consult the NAO and others, on what this will mean in practice. The Board will be presented with the conclusions at its meeting in May.
29. Chapter 7 doesn't yet include a section on the Operating and Financial review. The ASB is due to issue Reporting Standard 1 later in the year but to come into effect from 1 April 2005. A paper will be brought to the Board (probably in June) to insert the material on RS1 into Chapter 7, with proposals for its interpretation in the public sector context. Disclosures of reconciliations between budgets and accounts may be included within the OFR.
30. Russell Frith queried Charging for the Cost of Capital (FReM paragraph 4.5.4). He asked how FRS17 deficits should be dealt with. Significant deficits will send departments into a net liabilities situation. He asked whether this should be another exemption.
31. The Head of the Government Accountancy service has asked the Board to consider the cost of capital in Financial Reports as part of their forward work programme. The Treasury are currently looking at the implications in terms of DEL and AME and will consider the impact on accounts. The example of FRS 17 deficits will be covered as part of that work.
32. The Secretary confirmed that worked examples for eg PFI, together with Department Yellow and Magenta, will come as a package to the Board in May.
33. Mike Ashley remarked that in the section on FRS 5, application note F promotes Technical note 1. The Secretary will consider the text of the FReM and report back to the Board.
34. John Aldridge asked for an outline of the publishing strategy. The Treasury would be managing the new website. The manual will not be published in hard copy. The Head of the Government Accountancy Service will write to Finance Directors (copied to NDPBs, Trading Funds and RABIG) to introduce the new guidance. All existing accounts directions will need to be reviewed to refer to the new guidance. The guidance will be launched around the end of March, beginning of April.

Item 5: FRAB Report 2004-05

35. The Secretary introduced this paper, which included a first draft of the report. The report writing sub-group was due to meet immediately after this meeting.

Item 6: Forward work programme

36. The Secretary introduced this item which suggested a forward work programme for the Board, based on comments received. The work programme was divided into three sections: developments in accounting standards; other reporting matters; and administrative matters. Meetings for the coming year were planned for 9 May, July, September, November and February. There is a lot of work to get through in the early part of the year. The Secretary confirmed that there are no outstanding issues left to come to the Board in terms of WGA. The Board agreed that the Treasury should be invited to give a presentation on the first published set of Central Government Accounts in the Autumn. Robin Lynch will report to the Board on the work being carried out by the Task Force on Harmonisation of Public Sector Accounting as part of the work on revisions to SNA 93 and the Balance of Payments Manual later in the year.

Item 7: Resource accounting boundary

37. Michael Romberg gave an oral update. Discussions had continued in the Treasury about extending the resource accounting boundary to include non-departmental public bodies, with implications for the coverage of Supply Estimates. There had also been informal consultation of departments: extending the boundary would bring simplification which would be welcomed, but officials were nervous about Accounting Officer issues. Proposals to address departments' concerns had been developed and the Treasury would soon consult departments formally. In the light of departments' views advice could be put to Treasury Ministers on whether to approach Parliament to discuss a proposal.

Item 8: Salary and pension disclosures: update on legal position

38. The Treasury gave an update on progress towards getting legislation to put the salary and pension disclosures on to a statutory basis. As mentioned at the previous meeting, Cabinet Office were planning to introduce a Handout Bill, but Ross Cranston thought it unlikely that there would be a sponsor. The Treasury had passed on to the Cabinet Office the Board's comments regarding increasing Parliamentary interest in the remuneration packages for senior officials. The Treasury also referred to an earlier suggestion that the inclusion of the disclosure requirements as part of UK GAAP might give the necessary powers to require disclosure and asked whether this should be pursued again with the Treasury Legal Advisers. The Board agreed that this line should be pursued, and it was also agreed that the Chairman should

write to the Cabinet Office. The draft will be agreed with Ross Cranston.

39. The Cabinet Office intends to carry out consultation on making the disclosure more comprehensive. Beverley Evans reported that Foundation Trusts were already asked to follow Companies Act requirements.

Items 9 and 10: Updates on Interpretation for Public Benefit Entities of Statement of Principles for Financial Reporting and Heritage Assets

40. There was little to report for either of these subjects. The Secretary asked whether they should be included in the report. It was agreed that they should be flagged to consider.

Item 11: Any Other Business

41. Ross Cranston reported on the resource accounts workshop that was held at Portcullis House on 10 February. A reasonable number of people had attended, including MPs, researchers and members of the clerks department. It was considered a good first attempt. The intention is to incorporate the training for all new MPs.
42. Ross Cranston said that if an election was called, this could be his last meeting, as he was not intending to stand for re-election. The Chairman thanked him for his contribution to the work of the Board.
43. At the request of the Chairman, Robin Lynch explained to the Board the reason for the changes to accounting for road maintenance in National Accounts. He explained that there were two approaches for recording road maintenance expenditure. These are the depreciation approach and the renewals approach. The Public Sector Finances are compiled from a variety of source data. Depreciation is currently estimated from a Perpetual Inventory Model. The central government road maintenance data for England are from audited Highways Agency sources. The current methodology pre-dates the adoption of Renewals Accounting by the Highways Agency, and its adoption has resulted in a combination of the two approaches, which generated the double – counting. This revision corrects that.

Item 12: Date of the Next Meeting

44. The Board confirmed the timing of the next meetings as:

Monday 9th May 2005 (FRAB73)

Friday 24th June 2005 (provisional, to be confirmed)

