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Dear [REDACTED]

Review of the Welsh Mutual Investment Model for Public-Private Partnership Projects

As you are aware, the Welsh Government (WG) contacted the Office for National Statistics (ONS) to request a classification on the Welsh Mutual Investment Model (WMIM).

ONS has now completed an assessment of the classification, and as the projects that will use this model will be delivered through a Public-Private Partnership (PPP), ONS is required to identify the economic owner of the assets (i.e. roads, accommodation) and to establish the nature of the project companies.

The ONS has thoroughly analysed the documentation provided for the WMIM, culminating in a meeting of the Economic Statistics Classification Committee (ESCC) on 14 December 2016. This meeting considered classification of the model in the context of the internationally agreed rules laid out in the European System of Accounts 2010 (ESA 2010), the accompanying Manual on Government Deficit and Debt (MGDD 2016) and also the September 2016 European PPP Expertise Centre (EPEC) publication "A Guide to the Statistical Treatment of PPPs" compiled by Eurostat and the European Investment Bank.

Following a detailed discussion, which included analysis of the WMIM template Shareholders' Agreement, Project Agreement and User Guide, ESCC reached the following conclusions:

1. That the Project Co and Hold Co are to be treated as a single institutional unit for practical statistical purposes. This is due to Project Co being a wholly owned subsidiary of Hold Co, and the sharing of directors between the legal units which means that they cannot take decisions independently of each other.
2. Hold Co and Project Co are likely to be private sector controlled companies and the assets linked to this arrangement would likely be on the private sector partner's balance sheet. In reaching this opinion the Committee observed that almost all of the risk and rewards in the

PPP arrangement rest with the private partner and there is no "rebate" of proceeds to government, nor is government providing the majority of the finance or acting as a significant guarantor.

In reaching these conclusions ESCC did note that effectively the public sector has some veto powers through operation of the Reserved Matters in the Shareholders' Agreement. Specific concern was raised with Reserved Matter C3, which states "Any increase in the payment of fees and remuneration to directors to the Company save as expressly provided under this agreement". However, neither this nor the other Reserved Matters were considered, in discussion, to be enough to signify control over the corporate policy of Project Co and Hold Co (the company). ESCC, therefore, concluded that the companies should not be classified to the public sector. However, any changes to the Reserved Matters would need further investigation, and ESCC would need to review these as part of an actual project's documentation.

ESCC also raised some concerns about whether Project Co and Hold Co (the company) are actually institutional units under the ESA 2010 definition of an institutional unit. On balance it was felt they were, but ESCC would like the Welsh Government to provide examples of the types of decisions the Directors of the Special Purpose Vehicle would have to make in order to assure itself that the company is "able to take economic decisions and engage in economic activities for which it is responsible and accountable at law".

When considering the classification of the project assets ESCC noted a number of caveats to its conclusion that the assets are likely to be recorded on the private sectors' balance sheet. These caveats were:

1. Schedule 23, paragraph 2 of the Project Agreement, states that "the Authority shall be entitled to receive a one-third share in any refinancing gain arising from any Qualifying Refinancing". In the EPEC Guidance, Theme 14.6.2, this is the second approach to refinancing gain sharing that does not influence the statistical treatment. Welsh Government will need mechanisms in place to ensure that the one-third share is not exceeded, as this will result in an ON balance sheet classification.
2. The User Guide states in Section 6.1 that "The WMIM Standard Form Project Agreement does not envisage that any third party revenue generation activities will form part of the Project." It does however draw attention to the fact that if the Authority is forecast to receive more than 50% of the payments that the Authority is forecast to make to Project Co over the life of the contract from users of the asset, then it is recorded on the government's balance sheet.
3. The types of project which are likely to be recipients of the third party revenue generation payments relate to health and education. WG estimates that if payments are made, they will be below 20% but equal or exceed 5% which would be an issue of moderate importance to the statistical treatment. However, WG needs to consider if the revenue received is below 50% but equal or exceeds 20%. This level is of HIGH statistical importance and would mean that a WMIM project could have 2 HIGH issues and more than one moderate issue, and would be classified ON the government's balance sheet.

Limitations to this advice

This advice relates only to the model outlined and understood by ONS at this time. If there are any key changes to the model, or in specific project documentation, or if additional Authority controls are added please ensure that ONS are notified.

ONS wishes to review initial projects set up under this model, and we look forward to discussing these further with you next year.

ONS will treat this advice as given in confidence. If any indication of the contents of this advice are made public, by yourself or otherwise, we reserve the right to publish the advice in full, or confirm that

we have been approached to provide advice. You are free to make this advice public but we ask that if you wish to do so that you contact us in advance to discuss.

I trust this provides sufficient explanation of the decision reached. Please do get in touch if you have any questions or comments.

Yours sincerely,

David Beckett