

House of Commons
Treasury Committee

**GOVERNMENT RESPONSE TO THE
COMMITTEE'S FIRST REPORT:
NATIONAL STATISTICS: THE
CLASSIFICATION OF NETWORK
RAIL, SESSION 2002-03**

Third Special Report of Session 2002–03

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THIRD SPECIAL REPORT

The Treasury Committee has agreed to the following Special Report:

NATIONAL STATISTICS: THE CLASSIFICATION OF NETWORK RAIL: GOVERNMENT RESPONSE TO THE COMMITTEE'S FIRST REPORT OF SESSION 2002-03

1. On 20th January 2003, we published our First Report, *National Statistics: The Classification of Network Rail*, as House of Commons Paper No. 154. We have now received a response from the Government (dated 17 March 2003) which is appended below.

APPENDIX

The Treasury Committee's First Report of Session 2002-03 covered the classification of Network Rail in national accounts and in the accounts of central government departments. The Government's response to the Committee's conclusions and recommendations, which are shown in bold type, is given below. It incorporates the views of the National Statistician.

- a. **We consider that the separate views reached by the National Statistician and the Comptroller and Auditor General on the appropriate classification of Network Rail are confusing to those not well versed in statistical and accounting practice. We agree with the Statistics Commission that in these circumstances, where two different processes based on the same facts appear to have produced contradictory results, namely whether Network Rail is in the private or the public sector, the onus is on the parties concerned to align their different positions and explain the rationale for them to the public.**

The national accounts are prepared by the Office for National Statistics (ONS), following international rules for the compilation of economic statistics. The financial statements of central government departments are prepared, in accordance with the Government Resources and Accounts Act 2000, following UK Generally Accepted Accounting Practice (GAAP), adapted as necessary for the public sector. The Treasury is responsible for developing accounting guidance for central government departments. This guidance is reviewed by the independent Financial Reporting Advisory Board, which reports annually to Parliament. The accounts are audited by the Comptroller and Auditor General (C&AG), who is an officer of the House of Commons and is responsible for providing an independent and objective audit opinion on them.

The Government agrees that, in circumstances where these two processes produce apparently contradictory results as regards sector classification, it is appropriate that the parties concerned should explain to the public the rationale for their views. Up until now this has only occurred in the case of Network Rail. However once this has been done, and the issues fully explained, it is inappropriate for the Government to attempt to "align" the different positions, if that means forcing one or both of the parties to agree to a compromise solution that would be inconsistent with the underlying principles of national accounts, or with UK GAAP. It would also be inconsistent with the independence of the C&AG, and with that of the National Statistician on statistical matters.

- b. **We welcome the joint statement by the Comptroller and Auditor General and the National Statistician explaining their respective positions on the classification of Network Rail. We accept that the two positions reflect different professional**

requirements and traditions, but believe it would be helpful to public understanding of the position if the rules for accounting of liabilities with varying degrees of perceived risk were reviewed by both to see if greater transparency can be achieved.

Central government departmental accounts and national accounts follow common definitions as regards the accounting treatment of liabilities with varying degrees of perceived risk. Departmental accounts directly apply the UK Accounting Standards Board (ASB) Financial Reporting Standard 12 (FRS12) on Provisions, Contingent Liabilities and Contingent Assets. The ONS accepts the decisions of the accounting professionals with regard to whether liabilities are contingent, or whether provision should be made in the accounts. Any review of the existing accounting guidelines would be a matter for the ASB. The different positions explained by the Comptroller and Auditor General and the National Statistician in their joint statement were in respect of the sector classification of Network Rail.

- c. We note that ONS relies on departmental accounting advice in determining whether government guarantees are actual liabilities to be included in the National Accounts or contingent liabilities, which are excluded. The advice in this case, from the Head of Accountancy profession at the Department for Transport that the Government support facilities for Network Rail were contingent liabilities, has been confirmed by the National Audit Office. We are however concerned that there is the perception of a conflict of interest in ONS seeking advice on arrangements from the department responsible for making them. To avoid any potential question of a conflict of interest in the future, the advice given by accountants working within departments should in analogous cases be made subject to confirmation by the National Audit Office.**

Because national accounts follows GAAP definitions in this area, ONS relies on the judgement and supporting evidence of professional accountants in departments when deciding on whether a specific liability is to be treated as actual or contingent. Such advice is provided on a professional basis. Departmental accountants have the option of seeking advice from the C&AG as auditor, if they think it necessary. In order to facilitate this, the Government, with the C&AG, will consider whether the procedure already in place for PFI schemes, which allows for the C&AG to comment on the proposed accounting treatment at key stages during the development of each scheme, might be extended to cover a broader range of policy proposals.

- d. We recognise that contingent liabilities are reported to Parliament when they are created and are disclosed annually in the Consolidated Fund and National Loans Fund Accounts Supplementary Statements. We consider that the extent of contingent liabilities are of interest in relation to the state of public finances, and we therefore recommend, in the interest of greater transparency, that the existence of all contingent liabilities be stated in the Red Book with an estimate of the proportion of those liabilities which in aggregate may mature. The Red Book should indicate where the full list is to be found.**

In accordance with the principles underpinning the Government's fiscal framework, transparent arrangements are in place for the reporting of contingent liabilities. As the report recognises, contingent liabilities are already reported to Parliament, in line with the requirements of *Government Accounting 2000* (Chapter 26), when they arise. They are also disclosed in departments' resource accounts (under the requirements of FRS12) and have been drawn together in the annual *Supplementary Statements to the Consolidated Fund and National Loans Fund Accounts*. The Government agrees that the extent of government contingent liabilities is of interest in relation to the state of public finances. The Treasury will continue to

ensure that, where material contingent liabilities constitute a risk to the economic and fiscal outlook, they are identified in the *Financial Statement and Budget Report* (FSBR). The FSBR will also indicate where a comprehensive list of contingent liabilities is to be found (for example, in the Supplementary Statements). However the Government does not believe that it is possible to make a meaningful estimate of the proportion of contingent liabilities that in aggregate might mature. Contingent liabilities are by definition both uncertain and unlikely - if a liability is at all likely to be realised, then a provision in the accounts would be required - and in many cases the actual amounts at risk are unquantifiable.

- e. **We expect the introduction of Whole of Government Accounts to provide greater transparency by bringing information currently available in different places together to form a picture of the Government's financial accounts as a whole. We support the proposal that contingent liabilities be disclosed with these accounts.**

Whole of Government Accounts will be prepared under the same framework as outlined above in respect of departmental accounts, and will provide consolidated disclosure of contingent liabilities in accordance with FRS12.

- f. **We expect that the introduction of Whole of Government Accounts will also raise questions concerning the function of National Accounts. We therefore recommend that any significant differences between the two accounts should be shown in a published reconciliation and fully explained.**

The Treasury and ONS will work together to ensure that Whole of Government Accounts can include a full reconciliation with relevant national accounts data.

17 March 2003

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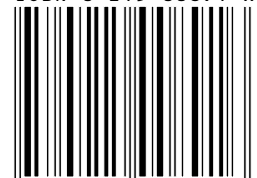
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