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PFI rule change could hit state capital projects

By Chris Giles and Nicholas Timmins

A squeeze on capital spending on schools, hospitals and other public infrastructure could be in prospect as billions of pounds worth of private finance initiative projects are poised to come back on to the government's balance sheet,

The move – the result of the government's promise to adopt international financial reporting standards for public accounts from next April – is also likely to lead to Alistair Darling, the chancellor, rewriting one of Gordon Brown's key rules for running the economy.

If only two-thirds of the £29bn of PFI projects that do not currently count as government debt come back on the books, the existing sustainable investment rule looks set to be broken.

It will also lead to worries over a potential shortage of capital for big public building projects as the government loses access to the off-balance sheet funding that has allowed it build new hospitals and schools without having to find the cash up front.

The move could see the government breaking one of Mr Brown's two cherished rules for running the economy.

But the sustainable investment rule is seen as increasingly discredited and both economists and the Conservatives have been urging a rewrite – something Mr Darling could use the accounting change to achieve with minimal political damage.

The change has no implications for taxation so long as the government modifies its fiscal rules. It may, however, have implications for NHS Trusts, and for levels of capital spending if the Treasury does not increase departmental capital limits to allow for future PFI projects – such as schools and hospitals – counting as debt.

The Treasury concedes that the new accounting standard will bring at least some PFI projects that are off the balance sheet back on.

It says it is too early to say how many, and that each will have to be examined on a case-by-case basis. But, according to key government advisers, most projects should be affected.

Ken Wild, a member of the government's Financial Reporting Advisory Board and of the International Financial Reporting Interpretations Committee, said that in the last analysis the Treasury could decide the rules, so it was impossible to be certain how much debt would return.

"But there is a lot of logic that says most of it will," Mr Wild, a partner at Deloitte's, said. "The Treasury will have to come up with some very good arguments if it does not. While it remains anyone's guess how much will be on the balance sheet, there is a pretty strong expectation that it is going to be a lot – most of it."

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David Heald, another member of the advisory board and professor of financial management at Sheffield University, said the logic of the new accounting standard was that the majority of PFI deals would not be on the private sector's balance sheet. They should therefore be on the public sector's, counting as public sector debt, he said.

"My personal view is that you should bring them on and change the fiscal rules at the same time," he said.

The Treasury said last night: "The government will work with the FRAB to determine those standards, but it is too early to draw conclusions about those outcomes."

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