

The Welsh Government's initial funding of the Circuit of Wales project

May 2018



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**Public Accounts Committee
National Assembly for Wales
Cardiff Bay
CF99 1NA**

Tel: **0300 200 6565**

Email: **SeneddPAC@assembly.wales**

Twitter: **[@SeneddPAC](https://twitter.com/SeneddPAC)**

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About the Committee

The Committee was established on 22 June 2016 to carry out the functions set out in Standing Orders 18.2 and 18.3 and consider any other matter that relates to the economy, efficiency and effectiveness with which resources are employed in the discharge of public functions in Wales.

Committee Chair:



Nick Ramsay AM
Welsh Conservatives
Monmouth

Current Committee membership:



Mohammad Asghar AM
Welsh Conservatives
South Wales East



Neil Hamilton AM
UKIP Wales
Mid and West Wales



Vikki Howells AM*
Welsh Labour
Cynon Valley



Rhianon Passmore AM
Welsh Labour
Islwyn



Adam Price AM**
Plaid Cymru
Carmarthen East and Dinefwr



Lee Waters AM
Welsh Labour
Llanelli

* Elected to the Committee on 21 June 2017 Mike Hedges AM substituted

** Elected to the Committee on 18 October 2017

The following Member was also a member of the Committee during this inquiry:



Neil McEvoy AM
Independent
South Wales Central

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Chair's foreword

The proposed Circuit of Wales was a unique and significant project, which appeared to offer the possibility of regenerating an economically deprived area. The Welsh Government was right to explore possibilities of making this project work and, quite properly, it is not this Committee's function to comment on the merits of the Cabinet's eventual decision not to provide the requested public finance support.

We are deeply concerned, however, at how this project was approached by the Welsh Government. We want Wales to be a first choice for investment and to achieve this, the decision-making processes followed by those charged with the expenditure of taxpayers' money, need to be both coherent and properly documented.

The Auditor General published his report on the initial funding of the Circuit of Wales in April 2017, which highlighted significant shortcomings in the Welsh Government's handling of this project. This report provided a firm foundation for the basis of our inquiry which expanded beyond the scope of the initial funding into the Welsh Government decision-making process for the final proposal.

The approach from the Welsh Government to this project has been one of two halves. The Welsh Government made some inexplicable decisions during its initial funding of this project, such as authorising payment for the purchase of FTR (a motorcycle company in Buckinghamshire) as part of the property development grant intended to buy land in Ebbw Vale. Then, having made the eventual decision not to provide the requested guarantee, the Welsh Government chose to focus its justification for this on a technical accounting matter, rather than citing the comprehensive due diligence which it had commissioned. This led to public confusion and did little to promote confidence in the Government's ability to handle public money wisely and well.

It is essential that the Welsh Government demonstrates effective management of Welsh public money and maximises the opportunities for investment in Wales. In response to successive reports in recent years from the Auditor General, and from this Committee and its predecessors, the Welsh Government has provided various assurances to us that "lessons have been learned". We certainly do not expect to see any recurrence of the basic errors, omissions and poor judgements on the part of officials that have come to light as a result of our work.

I would like to thank all those who provided evidence to the Committee, and contributed to this inquiry.

Nick Ramsay
Committee Chair, Public Accounts Committee

Glossary for Circuit of Wales

The Heads of the Valleys Development Company (HODVC) – Company proposing the development of the Circuit of Wales

Michael Carrick – Chief Executive of HoVDC

Richard Parry-Jones – HoVDC

Martin Whitaker – HoVDC

FTR – a motorcycle company in Buckinghamshire, purchased by the HoVDC during the initial stages of the Circuit of Wales project

Aventa Capital Partners – an Investment Management Company involved in developing the Circuit of Wales proposal (wholly owned by the controlling shareholder and Chief Executive of HoVDC, Mr Michael Carrick)

Ken Skates AM – Cabinet Secretary for Economy and Infrastructure (from 24 May 2016). Following a Cabinet Reshuffle on 3 November 2017, his portfolio title changed to Cabinet Secretary for Economy and Transport

Edwina Hart – The then Minister for Business, Enterprise, Technology and Science (Fourth Assembly 2011-2016)

James Price – Deputy Permanent Secretary for Economy, Skills and Natural Resources (until December 2017)

Tracey Mayes – Head of Governance and Compliance, Economy, Skills and Natural Resources Group, Welsh Government

Andrew Jeffreys – Director – Treasury, Welsh Government

Shan Morgan – Permanent Secretary, Welsh Government

Property Development Grant – A Welsh Government grant scheme which can be used to fund the purchase of land and property by the private sector to stimulate economic development.

Office of National Statistics (ONS) – Responsible for providing a formal classification of whether a project is “on” or “off” the Government’s balance sheet once a project has been finalised and a signed contract is in place

Infrastructure and Projects Authority (IPA) – the UK Government’s centre of expertise for infrastructure and major projects

1. Introduction

1. The Circuit of Wales (CoW) was an ambitious venture to construct a car and motorcycle racing circuit on moorland near Ebbw Vale in Blaenau Gwent. The racing circuit was intended to be of a high enough standard to accommodate a range of motorsports, including MotoGP motorcycle world championship racing, although it would not have been constructed to Formula One motor racing requirements. The CoW project was led by The Heads of the Valleys Development Company (HoVDC), which was established specifically for this purpose in 2011.
2. The Auditor General for Wales (Auditor General) published a report, on 27 April 2017 setting out the key matters relating to the Welsh Government's management of its initial financial support package for the CoW project. Up to that point, the Welsh Government had provided over £9.3 million to HoVDC.
3. Between 2011 and 2017, HoVDC submitted several different proposals for which it sought Government support in order to secure the £430 million of finance it eventually considered necessary for the construction of the circuit to proceed. The Circuit of Wales Ltd submitted a formal application in April 2017 to the Welsh Government which would have required the Government to provide a guarantee of the Aviva Investors loan facility of £210m.
4. The Cabinet Secretary for Economy and Infrastructure published a written statement on 27 June 2017¹ announcing that the Cabinet had decided not to provide a financial guarantee for the project.

Background to the Auditor General for Wales report

5. The Auditor General's Report focused on how well the Welsh Government had made decisions to provide initial financial support to the project; managed risks by applying conditions and assured itself that funds it provided were used for the intended purposes.
6. The report noted that the Welsh Government had provided over £9.3 million to support initial development of the CoW project, but identified significant shortcomings in how the Welsh Government had managed the associated risks to taxpayers' money.
7. The Auditor General's report focused on funding provided by the Welsh Government to the point of publication (April 2017). The Auditor General did not

¹ Welsh Government, **Written Statement**, 27 June 2017

assess the merits of the Welsh Government providing further publicly funded support to HoVDC or review the viability of the business cases for construction and operation of the race circuit.

8. The Auditor General found that the Welsh Government had not taken sufficient steps to ensure funds were used for the intended purposes. However, his Report did not directly examine the conduct of individuals or entities connected with the project. In response to concerns raised with the Auditor General by a Member of Parliament, the study team also examined certain specific payments made by a company associated with HoVDC, to establish whether these involved the use of public funds. They established that these payments did not constitute the use of public funds.

The Committee's report

9. Following the publication of the Auditor General's report, the Committee agreed to undertake an inquiry, and held an evidence session with the Welsh Government in June 2017. The scheduling of this evidence session was subject to a number of delays due to the availability of Welsh Government officials.

10. Following the Welsh Government's decision not to support the funding proposal from the HoVDC, the Committee also explored some issues arising from the decision making process for this project.

11. The Committee did not consider the merit of the decision, but instead focused on the process of making the decision, and in particular around the communication of information to the company.

12. As a result, this report is in two parts: the first part looks at the issues of the initial funding of the circuit and the second part considers the decision-making process. The conclusion chapter pulls together a number of key themes emerging from this inquiry.

Key Themes

13. The Circuit of Wales was a unique project, which appeared to offer the possibility of regenerating an economically deprived area. As such we believe that the Welsh Government was right to explore possibilities to try to make this work and, quite properly, it is not this Committee's function to comment on the Cabinet's eventual decision not to provide the requested public finance support.

14. We are deeply concerned, however, at how this project was approached by the Welsh Government. We want Wales to be a first choice for investment and, to

achieve this, the decision-making by those charged with the expenditure of taxpayers' money needs to be both coherent and properly documented.

15. The Committee's inquiry highlighted a number of concerns about the robustness of the decision making process, particularly regarding the rationale for various decisions by officials and the poor quality of their record-keeping. Some of the oral and written responses the Committee received in evidence from witnesses were evasive (evidenced by the number of times the Committee had to write on the same point),² and did not appear to be contemporaneous – for example, the value for money rationalisation of the monthly retainers paid to Aventa, and also the very weak justification for the inclusion of the FTR acquisition within phase 1 of the project. The Committee does not consider that the provision of £300,000 of taxpayers' money for the acquisition of FTR generated any value for money whatsoever.

16. Another theme which emerged during our inquiry was the use of over-extensive discretion by officials in not informing their Minister/Cabinet Secretary about the decisions being taken. There is no dispute that there needs to be some discretion for officials to take certain decisions, to ensure the effective operation of Government under the Carltona principle.³ However it appears in this instance that there were certain key decisions taken by officials for which Ministerial approval should have been obtained, such as the inclusion of FTR within the Property Development Grant.

17. Furthermore, the failure by officials to inform the Cabinet Secretary for Economy and Infrastructure of key information, such as the date of the publication of the Auditor General's report, together with the inaccuracies in the Welsh Government's written statement of 27 April 2017⁴ and press releases relating to this project, created a strong impression to the Committee of a department which was not properly in control of its business and which now, under its new leadership, needs to take stock and put in place robust and effective governance and internal communication channels to guarantee that such issues do not recur.

18. The final key theme which emerged in this inquiry was around the external communication of decisions. We defend fully the right of the Government to

² **Written Evidence, PAC(5)-02-18 P2, 22 January 2018**

³ The Carltona doctrine (or Carltona principle) expresses the idea that, in United Kingdom law, the acts of government departmental officials are synonymous with the actions of the minister in charge of that department. The point was established in *Carltona Ltd v Commissioners of Works*.

⁴ Welsh Government, Written statement, 27 April 2017

make decisions based on evidence in the best interest of Wales; however, in doing so it must communicate effectively, both to the public and to those directly involved. The suggestion that the Cabinet decision was based primarily on a technical accounting matter does not reflect what the Committee understands was a comprehensive due diligence appraisal of the CoW project's merits, and may itself have needlessly undermined public confidence in the Welsh Government's decision making process.

19. To address these issues the Committee has made the following 13 recommendations to the Welsh Government, which can be found within the body of the report:

Recommendation 1. We recommend that the Welsh Government strengthen their controls to ensure value for public money in relation to:

- Understanding relationships between funding recipients and their contractors and suppliers;
- Including requirements within funding conditions for recipients to put appropriate controls in place to secure value for money from their contractors and suppliers, and to provide evidence to the Welsh Government of their effective operation, in particular for:
 - Claims involving payments for services on the basis of retainers, to ensure that the services have been provided;
 - Claims for payment involving companies or individuals who are related parties, irrespective of whether or not they can exert direct influence over the claimant or over the conduct of the project being funded. Page 20

Recommendation 2. We recommend that the funding of the purchase of FTR is utilised as a case study for internal training purposes by the Welsh Government, given the highly unorthodox decisions made at official level, the accompanying lack of documentation and the apparent failure of officials to seek and obtain the requisite approvals from their respective Minister..... Page 29

Recommendation 3. We recommend that the Welsh Government confirms to the Public Accounts Committee that it has since recovered the £100,000 from the escrow account..... Page 30

Recommendation 4. We recommend that the Welsh Government ensures that a contractual requirement is included for future payments made to cover eligible expenditure related to escrow accounts in the event of a project failure..... Page 31

Recommendation 5. We recommend for all projects involving either significant risk or large sums of money that a requirement for applicants to elect for their financial statements to be independently audited is included within the Welsh Government's funding conditions, and that such terms are then rigorously enforced as part of robust ongoing monitoring arrangements..... Page 32

Recommendation 6. We recommend the Welsh Government strengthen its arrangements to ensure that whenever staff have concerns about instructions from authorising officers to make payments, they are able and confident to raise those concerns with a senior independent manager. Page 34

Recommendation 7. We recommend that all Cabinet Secretaries, Ministers and all Welsh Government Senior Civil Servants are reminded of the requirements within the Ministerial and Civil Service Codes to ensure the accuracy of all information released. Page 36

Recommendation 8. We recommend that the Welsh Government standardises the use of the "internal assurance group" mechanism for all future complex, novel or large-scale investment decisions..... Page 40

Recommendation 9. We recommend the Welsh Government establish a more sophisticated methodology for evaluating the overall economic impact of projects potentially involving public sector financial support, including robust analysis of the sharing of risks and rewards, and the value for money of loan guarantees and other non-grant funding options. Page 42

Recommendation 10. We recommend that the Welsh Government explore with Her Majesty's Treasury and the Office of National Statistics whether the published guidance on the risk weighting of projects of this nature can be enhanced to ensure that it is fully relevant within a devolved context. Page 50

Recommendation 11. We recommend that the Welsh Government work with relevant parties to establish a framework policy for decision-making in relation to large scale projects, which will set out potential sources of advice such as ONS, IPA..... Page 50

Recommendation 12. We recommend that the Welsh Government adopts a standard practice that meeting notes are agreed for factual accuracy by all relevant parties at the point of drafting. Page 53

Recommendation 13. Given the Creditors Voluntary Agreement and the uncertain financial status of the HOVDC, the Committee requires clarification from the Welsh Government on what action it is taking to safeguard its £7.3m debt from HoVDC arising from the Welsh Government loan guarantee.....Page 54

2. The Initial Funding of the Circuit of Wales

Overall Value for Money of the Initial Funding

20. The Auditor General found significant shortcomings in the way the Welsh Government handled the initial funding of the Circuit of Wales project. The Committee explored with the Welsh Government whether it believed it could demonstrate value for money from its funding support for the CoW project up until April 2017 (date of the AGW report). During the evidence session on 26 June 2017, James Price, the then Deputy Permanent Secretary for Economy, Skills and Natural Resources stated:

“I am persuaded that we have achieved value for money for what we have got, yes, which is a project that is ready, subject to finance, to be delivered. So, yes.”⁵

21. James Price suggested that the £9.3 million represented value for money regardless of whether the Project went ahead.⁶ In light of the Cabinet decision on 27 June 2017, the Committee sought clarification on whether he felt that this statement still remained valid. James Price set out that:

“... the cost of developing the Circuit of Wales project is considered to be appropriate for a project of this complexity and magnitude. Sometimes costs are incurred in developing projects which don't proceed. It is important to invest sufficiently to determine whether a project is viable; had we not done so then we would potentially have had less robust data on which to base our eventual decision.

When assessing the initial support to HOVDC, the Welsh Government assessed the risks of providing financial support to the Circuit of Wales (CoW) project and the relative potential benefits to the economy. It was determined that the benefit of providing the initial funding would be the advancement of the project and the securing of the economic impacts it would create. This was balanced against the risk of recovery of any costs incurred. Although recognised as a high risk at the time, these benefits were considered to represent value for money. The

⁵ National Assembly for Wales, Record of Proceedings (RoP), 26 June 2017, Paragraph 22

⁶ RoP, 26 June 2017, Paragraph 428

decision made by Cabinet does not affect the validity of this statement, which was informed by the evidence available at that time.”⁷

22. The Committee recognises that it can be appropriate for Governments to provide financial support for the preliminary phases of “high risk” private sector-led projects where benefits such as regeneration and job creation appear possible. We therefore agree with James Price that “It is important to invest sufficiently to determine whether a project is viable”.⁸ However, in this instance we do not believe that there was proper Welsh Government oversight of its investment, aspects of which are explored further in the following sections of this report. The Committee does not therefore believe that the Welsh Government can fully demonstrate the value for money of this investment.

Inadequate Welsh Government oversight of the use of public funds by the Heads of the Valley Development Company

Related Companies

23. The Auditor General found that nearly half of the £9.3 million total payments made by HoVDC that were funded by the Welsh Government under its Property Development Grant (PDG) and loan guarantee arrangements (excluding bank payments and charges) were conducted with or through nine companies with relationships to HoVDC.

24. Of £1.998 million paid to HoVDC under the £2 million Property Development Grant, transactions totalling £1.643 million (over 80 per cent) were conducted with or through companies with relationships to HoVDC. A further £2.342 million (just under 40 per cent) of the £6.523 million paid directly to HoVDC suppliers under the loan guarantee agreement was paid to companies with relationships to HoVDC.

25. The Committee were concerned to find that such a high percentage of both these funding streams went to companies related to HoVDC. Clause 18 of the terms and conditions for the Property Development Grant stated that “You [HoVDC] must buy all goods and services... in a competitive and sustainable way so as to demonstrate that you have achieved best value in the use of public funds”.⁹

⁷ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

⁸ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

⁹ Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, [Paragraph 3.12](#), April 2016

26. James Price explained that this did not necessarily require competitive tendering as:

“Our definition of ‘competitive’ is just that. They need to be able to demonstrate that what they have purchased represents competitive rates, not necessarily that they have gone through a competitive procurement. They are different things. The only time we would make people adhere to a competitive procurement process, i.e. an OJEU process, is if European funding was in the mix.”¹⁰

27. However, the Auditor General found that the Welsh Government had no evidence that any of the £2 million of services provided under the PDG had been subject to competition or value for money comparisons. The Welsh Government did not stipulate any value for money requirements at all in the loan guarantee agreement, under which the Welsh Government permitted payments to suppliers totalling over £6.5 million.

28. The Committee would expect, as a minimum, that there is a requirement for best possible value for money to be achieved as a condition for any finance provided. Tracey Mayes, Head of Governance and Compliance, Economy, Skills and Natural Resources Group, Welsh Government, told the Committee that the Welsh Government’s guidance for its officials had since been updated to make sure they were aware in future of the need to check:

“... if there is a related company, why it’s a related company and whether the service they’re providing is providing value for money.”¹¹

29. The Committee was also concerned that in its oral evidence the Welsh Government queried the number of related suppliers, and that its officials had had been completely unaware of many of the relationships until the Auditor General highlighted them during the course of his work. James Price stated that:

“The WAO figure, I believe, is of nine related companies or individuals. We don’t believe it’s as high as nine, but we’re not disputing the fact that there are related parties.”¹²

30. The figure quoted in the Auditor General’s Report had been confirmed with HoVDC itself prior to publication, and therefore it is surprising that the extant

¹⁰ RoP, 26 June 2017, Paragraph 127

¹¹ RoP, 26 June 2017, Paragraph 153

¹² RoP, 26 June 2017, Paragraph 111

Welsh Government definitions had failed to capture all of the related companies. James Price set out that:

“Whilst WAO have identified companies with links to HOVDC some of the links are wider than those that Welsh Government would consider to be a related company or individual.

Whilst Welsh Government accepts the WAO list of companies that have some wider links to HOVDC, none of the companies identified below have common directors or shareholders with HOVDC therefore they would not be able to have any effect on the day to day operations of HOVDC:

- Shaun Meadows Marketing Ltd;
- Barton Communications Ltd; and
- Kalergo Ltd.”¹³

31. The Committee is concerned that the Welsh Government would exclude from its consideration companies such as Kalergo Ltd (which received monthly retainer payments under the Welsh Government’s loan guarantee arrangement totalling nearly £97,000 against invoices that did not detail costs and services), when Kalergo’s sole officer and shareholder was also Aventa’s Chief Finance Officer.

32. The Welsh Government’s response argued that they do “not necessarily consider directors or shareholders of related companies as having the ability to influence the company being funded in the normal course of business and so would not look at them, focusing only on those individuals with direct means to influence”.¹⁴

33. However, the Committee is very concerned that this response suggests a worrying degree of either naivety or complacency on the part of the Welsh Government regarding private sector business relationships and conflicts of interest. It is not a question of whether the related companies and connected individuals were necessarily able to influence HoVDC overall. The crucial point is that the Welsh Government should have taken appropriate steps to ensure value

¹³ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

¹⁴ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

for money before approving payments to these companies because they were related to HoVDC.

34. The Welsh Government written response stated that

“Any [related] companies used as suppliers must provide their services on an arms-length basis and be able to demonstrate value for money.”¹⁵

35. However, the Welsh Government did not ensure that this was the case in relation to its funding support for the CoW project.

36. While we recognise it is not reasonable to have full scale tenders for all aspects of this type of funding, we cannot accept that value for money is not ensured. The Welsh Government should ensure that it sufficiently understands the projects it chooses to support, including related contractors and suppliers. It should then adopt and apply controls intelligently and flexibly, in proportion to the scale and complexity of the project, to mitigate the risks involved. In this case, the Welsh Government was unaware of several of the related companies, and therefore it would have been unable to verify the value of money of the use of funds in this instance. Nine related companies receiving over 80 percent of a grant award and nearly 40 percent of a loan facility raises some significant questions and it is unacceptable that the value for money to the taxpayer for this significant investment of public funds was not robustly substantiated by the Welsh Government.

Monthly Retainers paid to Aventa and other companies

37. In addition to an absence of evidence of competition, the Auditor General found that many of the payments made to the related companies simply represented monthly retainers, without any evidence of actual services being delivered.¹⁶ The Welsh Government told the Auditor General that:

“(b) officials had satisfied themselves as to value for money at the overall project level rather than at the individual service contract level.”¹⁷

38. Given the significant sums of money paid through retainers to companies with a relationship to HoVDC, the Committee was concerned that there was no

¹⁵ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

¹⁶ Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, [Paragraphs 3.22 - 3.34](#), April 2016

¹⁷ Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, [Paragraph 3.25](#), April 2016

evidence of value for money in relation to monthly retainer payments. The Welsh Government set out that:

“As a single purpose company, HOVDC does not have any direct employees but instead relies on contracting out all of their executive functions.

It is not unusual that professional advisors charge fees based on a fixed monthly retainer rather than charging on an hourly or daily basis rate. This is common practice in the commercial market place.”¹⁸

39. As an example of the monthly retainer, Aventa (a separate company wholly owned by the controlling shareholder and Chief Executive of HoVDC, Mr Michael Carrick) was paid a retainer of £42,500 per month. The Welsh Government told the Committee that this was based on:

“... an average of 20 working days per month, this retainer equates to £2,125 per day. The Aventa service contract with the HOVDC was for the provision of services including that of Michael Carrick. HOVDC told us [the Welsh Government] that the retainer also covered costs of service provision from a number of individuals with specialist knowledge in the following areas:

- Renewable energy
- Technology and data analytics
- Capital raising
- Finance and reporting
- Communication and marketing
- Construction and negotiation
- Commercial research
- Financial modelling.”¹⁹

40. This Welsh Government list does not match with services listed in information which had previously been provided by Mr Carrick to the Auditor

¹⁸ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

¹⁹ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

General. The Committee was surprised to note that the Welsh Government did not provide this explanation of Aventa's services to the Auditor General during his study work. This strongly suggests to us that the information provided to this Committee may have been prepared retrospectively.

41. The Committee was surprised and concerned that Michael Carrick had signed the contract between HoVDC and Aventa on behalf of both parties. HoVDC explained this arrangement to the Auditor General as "Two corporate entities entered into [a] contract for services. They happen to share a common shareholder whose potential conflicts were disclosed".²⁰ The Committee accepts this does not contravene company or contract law. However, it is illustrative of the very close business relationship between HoVDC and Aventa. This raises risks in relation to value for money that we consider the Welsh Government should have ensured were managed properly before approving expenditure eligibility and agreeing claims for payment.

42. The Auditor General also found that the Welsh Government had no evidence that HoVDC awarded Aventa's service contract following a competitive process.²¹ The Committee is greatly concerned that such a significant monthly retainer was paid as part of this process, seemingly with little explanation as to what the money was being utilised for, and that it had not been subject to any form of tender given that Mr Carrick had, in essence, entered into a contract with himself.

Recommendation 1. We recommend that the Welsh Government strengthen their controls to ensure value for public money in relation to:

- Understanding relationships between funding recipients and their contractors and suppliers;
- Including requirements within funding conditions for recipients to put appropriate controls in place to secure value for money from their contractors and suppliers, and to provide evidence to the Welsh Government of their effective operation, in particular for:
 - Claims involving payments for services on the basis of retainers, to ensure that the services have been provided;

²⁰ Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, [Paragraph 3.27](#), April 2016

²¹ Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, [Paragraph 3.27](#), April 2016

- Claims for payment involving companies or individuals who are related parties, irrespective of whether or not they can exert direct influence over the claimant or over the conduct of the project being funded.

The Acquisition of FTR

43. One of the funding support mechanisms available to the Welsh Government is its Property Development Grant (PDG). This is a grant scheme which can be used to fund the purchase of land and property by the private sector to stimulate economic development. It also covers related costs, including the professional fees associated with such purchases. As part of the initial funding for the Circuit of Wales, the Welsh Government awarded HoVDC a £2 million Property Development Grant in the autumn of 2012. HoVDC utilised £0.3 million of this grant to acquire FTR, a motorcycle engineering company based in Buckinghamshire which has since gone into administration (October 2016).

44. The Auditor General's report found that the Welsh Government was unable to provide any contemporaneous documentation explaining HoVDC's acquisition of FTR or for the Welsh Government's approval of its inclusion within the grant. In November 2016, Michael Carrick sent the Welsh Government a note in which he gave HoVDC's reasons for the acquisition (this was four years after the award of the grant and one month after the company had gone into liquidation). The note set out that HoVDC had intended to capitalise upon FTR's relationships within MotoGP and ultimately to re-establish the business in Wales.²² However, none of the stated reasons aligned with the approved objectives of the Property Development Grant scheme, or indeed with the Rassau site purchase requirements of the CoW project for which the Welsh Government had provided the funding.²³

45. The Auditor General concluded that the Welsh Government was unable to explain to his satisfaction why it had approved an element of grant funding intended for property development in Blaenau Gwent to be used by HoVDC to acquire a motorcycle engineering company in Buckinghamshire.²⁴ The audit

²² Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, [Paragraph 4.6](#), April 2016

²³ Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, [Paragraphs 4.4-4.7](#), April 2016

²⁴ Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, [Paragraphs 4.1-4.7](#), April 2016

report states that there was no evidence that the Welsh Government had undertaken due diligence or any other inquiries into FTR's financial standing.²⁵

46. The Committee had a number of concerns relating to the purchase of FTR as part of the Property Development Grant, in particular the lack of appropriate documentation about the decision for this purchase to be included as part of the Property Development Grant. The Welsh Government set out it utilised the PDG because:

“The Circuit of Wales is a unique property development project for which the company were seeking support to build a business proposition to secure private sector funding and to pursue a planning application. Whilst the CoW is not a standard property project, it is more aligned to property development than any other activity. Welsh Government has the power to provide grants for any purpose but it is preferred, where possible, to utilise a standard grant scheme.”²⁶

47. James Price explained:

“... particularly when it comes to inward investment or big regeneration or big capital schemes, the rules of grants, which are primarily around state aid, are not hard and fast and with legal advice and with wider interpretation can be interpreted broadly on occasions.”²⁷

48. The justification that “Welsh Government has the power to provide grants for any purpose but it is preferred, where possible, to utilise a standard grant scheme” is presumably based around Section 60 of the Government of Wales Act 2006, which confers wide powers on the Welsh Ministers “to do anything which they consider appropriate to achieve the promotion or improvement of the economic well-being of Wales”.²⁸

49. While we agree that it is important that there is flexibility within the system to accommodate schemes which may not fit neatly into an established grant envelope, there are risks associated with such an approach. The European Commission has approved the PDG scheme to confer an allowable State Aid (which, under EU competition law, would otherwise represent an unlawful state

²⁵ Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, [Paragraph 4.12](#), April 2016

²⁶ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

²⁷ RoP, 26 June 2017, Paragraph 70

²⁸ Government of Wales Act 2006

subsidy). However, this legal protection requires EU member states to make grants which are consistent with the stated purposes of the PDG scheme. A grant which falls outside the stated PDG scheme purposes risks being adjudged by the European Commission to be an unlawful State Aid. UK administrative law does not permit ministers, or officials acting on their behalf, to make unlawful decisions.

50. Whilst we appreciate why PDG was considered an appropriate mechanism to support acquisition of the main site, we cannot see any justification that accords with the purposes of the grant for FTR to be included in the PDG, let alone the timing for this purchase.

51. During the evidence session on 26 June 2017, the Committee questioned the Welsh Government on the reasoning for including this with the PDG and whether the expenditure on FTR could be considered value for money. James Price told the Committee that he considered the purchase of FTR as value for money. However, in subsequent written correspondence, it was concluded that:

“Unfortunately the delays resulting from the HOVDC being unable to access the required private sector investment meant that the proposed development of a ‘Welsh’ motorcycle was not undertaken and FTR went into administration.

As a result of these unforeseen circumstances the specific inclusion of FTR as part of the eligible costs for the PDG has not represented value for money in this particular instance.”²⁹

52. The Committee also explored the Welsh Government’s reasoning for including the purchase of FTR within phase one of the PDG, rather than at a later stage in the actual construction of the circuit and the adjacent development of the proposed automotive technology business park. In written correspondence, James Price explained that:

“The rationale for inclusion of FTR as part of the PDG was that the company would move to the CoW site and act as a catalyst for the development of a cluster of like-minded companies which could utilise the circuit. If HOVDC had been able to progress the project in the timescale initially suggested then FTR would have been able to relocate to Wales as proposed by HOVDC.

²⁹ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

The purchase of FTR was considered to be in line with Phase 1 of the CoW as officials agreed, during the negotiation of the PDG award letter, that the purchase of FTR was a key component in developing the planned business proposition particularly in reference to it being the catalyst around which the targeted Motor Racing and Advanced Engineering Sector cluster could be built. This cluster would bring the greatest benefit in terms of impact on local jobs and the broader Welsh economy.

If the purchase of FTR had been delayed until Phase 2 of the project then the business case being developed to access further private sector funding as part of Phase 1 would have been weakened. Inclusion of FTR in this phase of the project indicated that there was already interest and a level of commitment to the Circuit of Wales and the associated technology park.”³⁰

53. In light of this explanation, the Committee is surprised that the PDG award did not include any requirements for FTR to relocate to Wales, or for it to retain or create jobs in Wales.

54. When asked whether he considered the inclusion of the purchase of FTR within the PDG was unorthodox, James Price explained that:

“...at the time that that decision was taken, everyone believed that that was the most appropriate form of finance to use for that particular part of the project. Different types of finance were explored, including a loan and other grant mechanisms, but that was the particular grant mechanism that was alighted on.”³¹

55. Mr Price did agree that this was:

“...certainly not the core of what you would normally use that grant for, but I am content that not just the individuals who were involved at the centre of that decision, but the wider set of individuals, including the central finance team of the Welsh Government, considered this and considered different mechanisms, and concluded that that was the best mechanism that we had to deliver that particular part of the project.”³²

³⁰ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

³¹ RoP, 26 June 2017, Paragraph 47

³² RoP, 26 June 2017, Paragraph 47

56. Following the evidence session on 26 June 2017, the Committee sought further clarification on whether the inclusion of an item of £300,000 such as FTR, which the Auditor General stated does not align with a grant scheme's core purposes, would be considered exceptional. James Price stated:

“Looked at in isolation, we can see why the AGW might consider the purchase of FTR could have been considered to be exceptional. However, the provision of the PDG was focused on enabling HOVDC to undertake a property development process to get to financial close: planning consent and fund raising were the key drivers for success. At the time [Welsh Government] officials considered that the purchase of FTR was in line with the objectives of the HOVDC developments being funded by the PDG and therefore concluded the purchase of FTR was not exceptional.

The scrutiny process for PDG applications has been significantly enhanced since the funding to HOVDC was awarded. An application for PDG funding of £2m would now need to be considered by the Property Leadership Team (PLT), Investment Panel then the Welsh Industrial Development Advisory Board (WIDAB) before a recommendation is made to the relevant Minister. This significantly increased level of scrutiny is likely to ensure items of a potentially exceptional nature are fully discussed and explored.

Hence, if the PDG funding to HOVDC was to be considered under this new process, it is likely that the purchase of FTR would be highlighted as exceptional and would be reported as such in any recommendation to the relevant Minister.”³³

57. When asked for more detail on how the scrutiny of the decision was taken, Mr Price explained that:

“In relation to the FTR item, the rationale for the purchase was verbally questioned prior to agreement that the costs for the purchase would be included as eligible expenditure.

Scrutiny of the claim resulted in part of the expenditure relating to FTR being disallowed as it related to working capital, and not to the eligible expenditure for the purchase.”³⁴

³³ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

³⁴ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

58. He also highlighted that “the Welsh Government accepts that more scrutiny should have been undertaken at the appraisal stage before inclusion of the purchase of FTR within the PDG eligible costs” and that “the level of scrutiny now applied is significantly more rigorous”.³⁵

59. The Auditor General also found that the FTR transaction took place on 28 September 2012, before the PDG grant was actually awarded on 11 October 2012, but that the PDG funding start date had been backdated by officials to 1 August 2012 at HoVDC’s request. The Committee explored whether the Welsh Government reviewed the FTR sale/purchase contract before approving FTR’s inclusion as eligible expenditure against the PDG grant, and were told:

“The approval for the PDG funding to HOVDC was given by the Minister on the 9th August 2012. Following ministerial approval, officials developed the award letter in conjunction with legal services and met with HOVDC to explain the details of the letter and associated conditions. The final, agreed award letter was subsequently issued to HOVDC on the 11th October 2012 and signed by the company on the 16th October 2012.

It is not uncommon for the start date of the funding period identified in the award letters to be the date of approval, in this case the 9th August 2012. In this case the start date for the funding period was given as the 1st August 2012 in the award letter at the request of HOVDC. Such changes are made at the discretion of officials involved prior to formal approval of the project. Any work undertaken between the start date of the funding and the date of approval is undertaken at risk by the company requesting the funding.

In this case, HOVDC did not include any expenditure prior to the 9th August [2012] in any of the claims made against the PDG offer.

I am unable to confirm that the Welsh Government reviewed the FTR sale/purchase contract before including the purchase of FTR within the grant’s eligible costs. Sufficient evidence was provided by Shoosmiths, acting on behalf of HOVDC, to demonstrate that the contract had been signed and was in place prior to the claim being paid. However, in my view, the FTR contract should have been reviewed before the purchase

³⁵ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

of FTR was included as eligible expenditure or at least before the claim was paid.”³⁶

60. Given the Auditor General's findings that there was no evidence of the Welsh Government's approval of FTR's inclusion as eligible expenditure within the grant, the Committee explored whether the then Minister for Business, Enterprise, Technology & Science was aware of the inclusion of this within the grant. Tracey Mayes, , Welsh Government told the Committee that:

“We have no paperwork trail that says that the Minister was aware.”³⁷

James Price added:

“It is conceivable that the Minister would not have known about that particular use of that particular grant.”³⁸

61. The Committee were surprised that there was no evidence to confirm whether the then Minister was aware or not of this decision. During the Committee meeting on 26 June 2017 the then Deputy Permanent Secretary and Ms Mayes reflected on the record keeping that “officials should keep detailed records of all meetings and conversations with funding applicants”³⁹ and that “good practice would be the minimum level necessary to demonstrate why you did what you did”⁴⁰ which did not happen in this instance. James Price suggested that the:

“... error also appears to be an administrative shortcoming largely as a result of the volume of complex information being shared in a significant number of meetings and other discussions between officials and HOVDC; it does not reflect a conscious decision on the part of officials not to produce an appropriate record of the decision process or to retain contemporaneous documentation.”⁴¹

62. He sought to reassure the Committee though that:

“Since that time, there has been an increased focus within Welsh Government and the department on the need to keep appropriate

³⁶ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

³⁷ RoP, 26 June 2017, Paragraph 59

³⁸ RoP, 26 June 2017, Paragraph 63

³⁹ RoP, 26 June 2017, Paragraph 337

⁴⁰ RoP, 26 June 2017, Paragraph 343

⁴¹ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

records to demonstrate the rationale behind decisions being recommended and made, for example I have issued communications to all ESNR officials informing them of the importance of keeping accurate records and it has been discussed in management team meetings and at all staff events.”⁴²

63. The Committee is astonished that it appears unlikely that the then Minister for Business, Enterprise, Technology & Science was informed of the decision and that there are no records of any discussions.

64. The Committee is also deeply concerned by the fact that in April 2016, in response to concerns raised by a Member of Parliament, the Welsh Government issued an incorrect and misleading press statement that “...no Welsh Government funds were used for the acquisition and running costs of FTR Moto Ltd by the HoVDC”.⁴³ The statement also completely omitted the £2 million grant (which had included £0.3 million of approved expenditure for the FTR acquisition) from the reported total amount of funding that the Welsh Government had provided to HoVDC. The Auditor General found that these errors were particularly surprising because the press statement originated from the same team of officials in the Welsh Government that had been responsible for agreeing the eligible expenditure and authorising the grant claim payment to HoVDC for the acquisition.⁴⁴

65. The Committee considers the entire funding by the Welsh Government of the purchase of FTR by HoVDC to be exceptional, unconventional and almost inexplicable. We would expect a decision so far outside the definition of the Property Development Grant scheme, as purchasing a motorcycle manufacturing company based in England with public funds that had been provided to acquire and develop land in Blaenau Gwent, to have firstly been approved by the Minister concerned, and secondly for this decision to have been fully documented.

66. The Committee is concerned that the extent of discretion exercised by Welsh Government officials in this case, seemingly without any ministerial oversight, exposes the Welsh Government to an unacceptable level of risk of legal challenge which is compounded by the absence of appropriate record-keeping.

⁴² Written Evidence, PAC(5)-24-17 P7, 2 October 2017

⁴³ **Welsh Government Press Notice**, April 2016

⁴⁴ Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, Paragraphs 4.13 – 4.1, April 2016

Recommendation 2. We recommend that the funding of the purchase of FTR is utilised as a case study for internal training purposes by the Welsh Government, given the highly unorthodox decisions made at official level, the accompanying lack of documentation and the apparent failure of officials to seek and obtain the requisite approvals from their respective Minister.

Conditional Acquisition of the Circuit of Wales site

67. The Auditor General found that the Welsh Government's arrangements for authorising payments claimed by HoVDC were insufficiently robust. His study team identified a grant claim payment of £100,000 representing a deposit for a conditional purchase of the land for the main site, held by the seller's solicitor. This deposit would be paid to the seller by the solicitor if the sale transaction (which is conditional on the CoW project raising the finance necessary to proceed) is completed. Such deposits are frequently eligible for grant, but would not normally be claimable until actually paid over to the seller. However, in this instance the Welsh Government approved and paid HoVDC's claim for the deposit in advance of it being paid to the seller.

68. If the Welsh Government subsequently decided not to provide the financial guarantees necessary for the project to proceed, the land purchase would not be completed and the deposit, for which HoVDC had already been reimbursed by the Welsh Government, would be returned to HoVDC.

69. During the Committee meeting, James Price explained that this money was paid into an escrow account,⁴⁵ and that he "was not sure, having looked at the detail of this and spoken to internal governance colleagues, that this process was as far out of the ordinary as [the Auditor General's] report implies".⁴⁶

70. Tracey Mayes explained that:

"The nature of property development grants means that we can use escrow accounts, and it's not a common occurrence, but it's not a rarity either. It is something that does happen, and we do pay through those escrow accounts. I agree with the wording—'not normally eligible'—because it's only in specific instances, but in this instance we believe it was correct."⁴⁷

⁴⁵ An escrow account is an account where funds are placed so they are available, but those funds can only be drawn down if certain terms and conditions are met

⁴⁶ RoP, 26 June 2017, Paragraph 305

⁴⁷ RoP, 26 June 2017, Paragraph 317

71. While the Committee accepted that a deposit held in an escrow account is not unusual in conditional property sales transactions, it was also noted that such amounts are not normally claimable expenditure until paid to the seller and sought clarification as to why in this case the Welsh Government considered this grant claim payment to be correct. James Price set out:

“The PDG award letter stated that HOVDC would be paid on a defrayed basis, which means that the payment to suppliers etc. had to have left HOVDC’s bank account. The Welsh Government usually considers payment into an escrow account to be eligible for grant as the payment has been defrayed by the grant recipient. There have been a number of instances where grant payments have been made where the expenditure has left the grant recipient’s account and been placed in an escrow account.

In this case, the finance team requested specific additional information to demonstrate that the money had been defrayed by HOVDC. Confirmation was received from HOVDC’s solicitors that the £200,000 for the land was transferred to the land owner’s solicitor on 17 December 2012. In accordance with the contract between HOVDC and the land owner, £100,000 was held by the land owner’s solicitor (in the escrow account) as a deposit whilst the remaining £100,000 was paid to the land owner.

Hence, officials were content that the whole of the £200,000 had been defrayed by HOVDC and, as such, was an eligible element of the claim for payment.”⁴⁸

72. It appears to us that the Welsh Government failed to put in place adequate contractual or other provisions to ensure that the £100,000 in escrow would be returned to the Welsh Government by HoVDC if the conditional sale did not proceed.

Recommendation 3. We recommend that the Welsh Government confirms to the Public Accounts Committee that it has since recovered the £100,000 from the escrow account.

⁴⁸ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

Recommendation 4. We recommend that the Welsh Government ensures that a contractual requirement is included for future payments made to cover eligible expenditure related to escrow accounts in the event of a project failure.

The loan guarantee agreement

73. The loan guarantee agreement included the condition that HoVDC should provide audited financial statements to the Welsh Government. The Property Development Grant required access on request to financial information but did not specify any requirement for external audit.

74. HoVDC's annual turnover is below the £6.5 million HMRC requirement for companies to submit independently audited profit and loss accounts to Companies House. However, small companies can elect to be audited. At the point at which the Committee considered this, none of the accounts filed at Companies House by HoVDC and its related companies had been audited. In addition, the Auditor General had noted that the various companies within the HoVDC ownership structure had different annual accounting periods, making external scrutiny of related company accounts more difficult.

75. When asked why the HoVDC accounts were not audited, Tracy Mayes stated that this was because companies of that size were not required to do so under company law. The Committee had some significant concerns about this because a requirement of the loan guarantee agreement was for HoVDC to provide audited financial statements to the Welsh Government. In clarifying why that condition to provide audited financial statements had been imposed, but then not enforced, James Price told us:

“The guarantee loan agreement between the HOVDC and the Welsh Ministers states in the Conditions Precedent that HOVDC needed to provide a copy of their ‘audited financial statements for the period ending 31 May 2014’. This is a standard banking condition and was included in the agreement in order for it to operate under commercial terms in line with Market Economy Operating Principles (MEOP). Considering the status of the company the condition should have been better worded to require the provision of statutory accounts as legally HOVDC were not required to provide audited accounts

The external legal team advising the Welsh Ministers drafted the agreement and also sought the evidence for the Conditions Precedent from HOVDC's lawyers. Subsequently, HOVDC's lawyers confirmed in writing that they were unable to provide audited accounts for May 2014

as there were no audited financial statements prepared for HOVDC. Instead unaudited financial statements for the year ended 31 May 2013 were provided to our lawyers. Management accounts and cash flow forecasts to December 2014 were also provided at that time. Given the fact that the agreement was due to be signed in July 2014 it should not be surprising that accounts for the period up to 31 May 2014 were not available.

Our lawyers subsequently advised officials that sufficient evidence had been obtained from HODVC to provide assurance that this particular condition had been met and also provided hard copies of the evidence for this and other conditions."⁴⁹

76. As a provider of finance the Welsh Government can, and should, include reasonable conditions into the grant awards such as requiring audited financial statements.

- Given that the Welsh Government had little information about HoVDC due to: HoVDC was a new company without any previous trading history, which was established for the purposes of the project;
- The various companies involved in delivering the project were not fully in place and the structure continued to evolve.

We are disappointed that this requirement was not enforced by the Welsh Government, for the period mentioned or indeed for any period in which the company was in receipt of public funding. This external verification of the accounts is vital for providing assurance, particularly in projects such as the Circuit of Wales which involve significant risk or large sums of public money.

Recommendation 5. We recommend for all projects involving either significant risk or large sums of money that a requirement for applicants to elect for their financial statements to be independently audited is included within the Welsh Government's funding conditions, and that such terms are then rigorously enforced as part of robust ongoing monitoring arrangements.

Separation of Duties

77. The Auditor General found that:

⁴⁹ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

“... the Welsh Government officials who had liaised with the CoW project in bidding for public funds, drafted briefing notes and provided advice to the Minister for funding decisions also played a significant role in the payment authorisation process.”⁵⁰

78. The Committee sought reassurance from the Welsh Government that appropriate processes exist within the Welsh Government to ensure the separation of duties. The Committee was concerned that on 11 January 2013 an official instructed his finance colleague to pay a grant claim, even though no Welsh Government officials had seen the relevant parts of the conditional sale contract, and finance officials had correctly challenged this when the claim was submitted in December 2012. In seeking to justify to the Committee how this official's instruction and its execution demonstrated the maintenance of an appropriate separation of duties, James Price said:

“In this case, the team who were dealing with HOVDC on a regular basis received the grant claim and associated evidence from the company. The details of the claim were considered to confirm that evidence of expenditure was provided in line with the award letter. The evidence and the confirmation that the claim was valid were then issued to the finance team for consideration and approval.

In line with their independent assessment of the claim, the finance team required additional information from HOVDC including relevant VAT invoices and confirmation of payment from the relevant legal representatives. Consequently there was considerable email communication between officials in the two teams to clarify exactly what evidence should be provided. This additional information was obtained from HOVDC by the team dealing with the company which is standard practice.

Once this additional information was provided by HOVDC, the evidence was provided to the finance team for consideration and approval. Whilst the email from the officials involved in supporting HOVDC and their funding bid does state ‘I therefore would confirm my revised confirmation that the grant claim should be paid’, this was not an instruction but a recommendation. As demonstrated earlier in the email trail, the finance team were unwilling to approve payment without sufficient evidence being provided. The payment was approved

⁵⁰ Auditor General for Wales Report, The Welsh Government's Initial Funding of the Circuit of Wales Project, [Paragraph 3.35](#), April 2016

based on sufficient evidence being provided to the finance team to provide them with the assurance they required.

Whilst none of the officials involved in these processes had seen the whole of the conditional sale contract, sufficient evidence had been provided to demonstrate that the contract had been signed and was in place.

I am therefore content that the email trail demonstrates the maintenance of appropriate separation of duties.”⁵¹

79. We do not agree with the Deputy Permanent Secretary’s assertion that: “I therefore would confirm my revised confirmation that the grant claim should be paid”,⁵² in response to a wholly correct challenge for the provision of further documentary evidence prior to payment, could be construed by either the writer or the recipient only as a recommendation. Based on the evidence to date, it is this Committee’s view that a senior Welsh Government official inappropriately asserted their positional weight over colleagues in the finance department to make a payment without having seen all the evidence requested, which is wholly unacceptable.

80. We think that this demonstrates that the measures in place within the Welsh Government to ensure separation of duties between officials involved in sponsoring projects and authorising claims for payment are not sufficiently robust as they can be over-ridden in practice.

Recommendation 6. We recommend the Welsh Government strengthen its arrangements to ensure that whenever staff have concerns about instructions from authorising officers to make payments, they are able and confident to raise those concerns with a senior independent manager.

Welsh Government response to the Auditor General’s report

81. The Committee raised a number of concerns about how the Welsh Government responded to the Auditor General’s report.

82. The Committee was concerned by the Welsh Government’s Written Statement which expressed the Welsh Government’s “surprise and disappointment” at the Auditor General’s decision to publish his Report during

⁵¹ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

⁵² Written Evidence, PAC(5)-24-17 P7, 2 October 2017

the period leading up to the Westminster Parliamentary election; and stated that they had not had sufficient time to consider and respond to the Report prior to its publication.⁵³

83. A subsequent response to a written assembly question from Adam Price AM clarified that officials were informed on 17 March 2017 about the intended publication of the report in late April 2017. However despite officials knowing over a month before the Cabinet Secretary for Economy and Infrastructure was formally informed, James Price told the Committee, in written correspondence that:

“Officials have been unable to identify any evidence that the Minister was informally informed of the Auditor General’s intention to publish before being formally informed on 24 April.”⁵⁴

84. On a number of occasions during the evidence session, the then Deputy Permanent Secretary also inferred that there were factual inaccuracies in the Auditor General’s Report. This was surprising to the Committee, as we are aware that Auditor General Reports are subject to a substantial and rigorous clearance process with the Welsh Government and all named third parties, in order to be as fair and accurate as possible. When challenged by the Committee on what these alleged “factual inaccuracies” were, James Price said:

“My remarks about accuracy of the AGW report relate to our concerns that some of the details as presented in the WAO report, without associated context and additional information being given, could lead to a mistaken interpretation of those details or incorrect inference by a reader without any other knowledge of the matters covered.

Essentially, in a number of areas, we had asked the AGW to provide additional information to provide a fuller picture, allowing others to reach a fair conclusion when scrutinising the report.”⁵⁵

85. The Auditor General wrote to the Committee on 14 September 2017 and stated:

“I share the Committee’s concerns in this matter and I am particularly concerned that in its written response the Welsh Government has continued to imply that such shortcomings exist without actually

⁵³ Welsh Government, **Written Statement**, 27 April 2017

⁵⁴ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

⁵⁵ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

providing any evidenced examples, despite the Committee's direct request that it should do so.

I should therefore like to assure the Committee that:

- with the exception of one minor error (to which I have previously drawn the Committee's attention) in relation to the economic efficiency test being a UK test and not specifically a Welsh test [see Report, paragraph 2.8], I remain satisfied that my Report is factually correct; and
- there is nothing contained in any of the Welsh Government's evidence given in response to the Committee's oral and written questions that would cause me to modify my Report's conclusions."⁵⁶

86. The Committee finds this series of events to be very concerning, as it potentially hampers our ability to perform our scrutiny function effectively. We rely on the reports from the Auditor General to undertake further scrutiny of, often, sensitive subjects and we do not expect their accuracy to be called into question by the Welsh Government following their publication. We find it utterly unacceptable for a senior Welsh Government official to assert publicly that the report is inaccurate and then not be able to substantiate this.

87. Furthermore, for officials not to have informed their Minister that the Auditor General's report on such a high-profile topic would be forthcoming, and then for the Welsh Government to issue a Statement which suggested that the report's publication was unexpected and had left the Government unable to prepare, is also entirely unacceptable.

88. Information released by the Government, whether to the National Assembly or to the media, must be accurate and fair, to ensure that public trust is maintained in the process of democratic scrutiny of the executive by the Parliament. The Committee was deeply disappointed in the actions of Government officials relating to this report, and we would not expect to see action like this again.

Recommendation 7. We recommend that all Cabinet Secretaries, Ministers and all Welsh Government Senior Civil Servants are reminded of the requirements

⁵⁶ **Letter to the Committee from Auditor General for Wales, September 2017**

within the Ministerial and Civil Service Codes to ensure the accuracy of all information released.

3. The Welsh Government's Decision-Making Process

89. Following (although not related to) the Committee's consideration of the Auditor General's report, on 27 June 2017 the Welsh Government decided not to support HoVDC's request for a funding guarantee. The Committee therefore expanded the scope of its inquiry to explore issues arising from that decision-making process.

The role and use of "Internal Assurance Groups"

90. Given the concerns arising from the initial funding of the project, the Committee explored the due diligence that was being undertaken for the decision-making process about whether to proceed with the project. James Price explained that the process, which was ongoing at that point, had:

"... someone looking at the business plan, there are people looking at the assumptions under the business plan, including specialists in motor sports, specialists in engineering, specialists in extreme sports, specialists in music and events. Cost consultants—some of the same ones that we use on transport projects, routinely—have been employed to look at the total cost of building the circuit. Does that look like value for money? Do the contracts in place look like they're reasonable? The fit-and-proper person test, as we've talked about, that is really akin to the old FCA test, but I suspect goes a bit further than that. A whole series of legal tests, state-aid tests, balance sheet tests.

And added to that, we've had an internal governance group created within the Welsh Government, where we've almost purposely picked out the people who will ask the most difficult questions to ask questions of the project team to ensure that whatever the decision is tomorrow that it is as informed as it possibly can be.

So, I think we have done a proper process this time. It's very time consuming, though, I would say, and has involved an awful lot of people and will have cost quite a lot of money in and of itself. The judgment is, 'What type of project do you go to this level of expense on?' I guess part

of the answer is the type of project that is asking the public sector to take a £200 million risk.”⁵⁷

91. Following this reference to the “internal governance group”, the Committee requested further detail on that group and how this challenge was received by officials. James Price stated:

“The Internal Assurance Group was set up in March 2017 to provide an additional level of scrutiny to the decision making process around the Circuit of Wales project. The group met three times to discuss the proposal prior to the submission of the Cabinet paper in June 2017. The role of the group was to assist Economy, Skills and Natural Resources (ESNR) officials to deliver a fair and balanced report to Cabinet which covered all the key areas of concern.

The group consisted of key individuals from across the Welsh Government including the Director of Finance, Director -Communities & Tackling Poverty, the Chief Economist and Director of Legal Services Department. The group also included Directors and individuals with key skills (e.g. governance, Finance, communications) from across ESNR.”⁵⁸

92. In subsequent correspondence, Shan Morgan, Permanent Secretary, Welsh Government said:

“As the then Deputy Permanent Secretary, James Price, initiated the Internal Assurance Group as a ‘one off’ measure for the Circuit of Wales. The use of such a group does not form part of the normal Project Governance or Approval Process. Given the scale and broad reach of the project, Mr Price concluded that the draft advice to Ministers prepared by the lead officials should be scrutinised and challenged as comprehensively as possible to ensure the advice given to Ministers fully addressed all key issues, including benefits and risk as well as policy alignment.

The Assurance Group did not form part of the formal approval process but provided assurance to senior officials that the project appraisal and due diligence covered all aspects of the proposal and, as a consequence, that the advice to Ministers would be complete.

⁵⁷ RoP, 26 June 2017, Paragraph 350

⁵⁸ Written Evidence, PAC(5)-24-17 P7, 2 October 2017

Membership of the group was drawn from senior officials across Welsh Government who had particular areas of expertise or were potential stakeholders. This included Directors from the ESNR Corporate Leadership Team together with the Welsh Government Finance Director, Director Legal Services, Chief Economist and Director - Communities & Tackling Poverty.

This Assurance Group met on five occasions between February and June 2017, including one meeting with the Circuit of Wales management. The outcome of each meeting was communicated to the officials managing the due diligence process and preparing the advice for Ministers and Cabinet.”⁵⁹

93. The use of internal assurance groups appears to us to be a useful mechanism for providing additional scrutiny in those projects which are not run of the mill. It is vital that these projects are subject to robust and constructive internal challenge at the various pre-decision stages (including considering the results of due diligence), to help ensure the best possible deal for Wales.

Recommendation 8. We recommend that the Welsh Government standardises the use of the “internal assurance group” mechanism for all future complex, novel or large-scale investment decisions.

Job Creation

94. Between 2012 and 2017 several iterations of the CoW project proposal were submitted to the Welsh Government by HoVDC. The different iterations led to varying suggestions of how many jobs would be created from this project, and there were multiple studies during this period which provided differing estimates of job creation. During the evidence session on 26 June 2017, James Price quoted the “core assumptions” of 1000 jobs from the circuit and 4000 from the subsequent development.⁶⁰ These figures were based on work undertaken by the University of South Wales in 2012-13.

95. However later job estimates were significantly lower. For example, the information presented to Welsh Investment Development Advisory Board (WIDAB) in June 2014 was based on direct full time equivalent employees (FTEs)

⁵⁹ Written Evidence, PAC(5)-02-18 P3, 22 February 2018

⁶⁰ RoP, 26 June 2017, Paragraphs 24-41

of 304 which was made up of 49 full time permanent employees plus temporary staff for events equating to 255 FTEs.

96. In explaining the reason for not deciding to invest further in the Circuit of Wales the Cabinet Secretary for Economy and Infrastructure stated that:

“...once the initial track and directly related development... had reached a steady state of trading around the year 2024, the number of direct full-time-equivalent (FTE) operational jobs would be little over 100. In addition, the circuit development could create around 500 indirect FTE jobs through potential visitor spend, as well as approximately 500 FTE construction jobs while the track was being built.”⁶¹

97. James Price explained that the figures quoted to support the Welsh Government decision not to fund the Project were based on the due diligence information based on the final proposal from the HOVDC.

98. That due diligence information (much of which has since been published⁶² by the Welsh Government) is clear that the first-stage of the project would not deliver the volume of jobs initially thought for the level of investment, and that many of the stated jobs would be part of the second phase of the project with the construction of the technology park. That second phase did not form part of the funding application and could conceivably have required further public funding support at a later date.⁶³

99. The differences in the figures quoted for potential for job creation are quite significant and do raise important questions about how to establish what level of job creation/value for money target is appropriate for a loan guarantee. When issuing a grant, it is established practice to assign a job creation target which correlates to the investment made; however, with a loan guarantee where potentially (indeed, ideally) no public money is actually being expended, this process is much less straightforward. The nature of this project raises a number of questions about contingent job creation, as this is difficult to evaluate and map but could be rightly be considered as an important factor in projects. However, we recognise that in this instance the potential number of jobs likely to be created for the element of the overall Circuit of Wales “vision” that was being funded (simply

⁶¹ Written **Statement**, Cabinet Decision on Circuit of Wales 27 June 2017

⁶² **Welsh Government Due Diligence** on Circuit of Wales project, 6 October 2017

⁶³ BBC News Press Article, 27 June 2017 [Accessed 1 May 2018]

the construction of the circuit itself) was low, and that this would have been an important factor in the Cabinet's decision-making.

Recommendation 9. We recommend the Welsh Government establish a more sophisticated methodology for evaluating the overall economic impact of projects potentially involving public sector financial support, including robust analysis of the sharing of risks and rewards, and the value for money of loan guarantees and other non-grant funding options.

Balance Sheet Classification and Risk Analysis

100. On 27 June 2017 the Cabinet Secretary for Economy and Infrastructure announced that the Cabinet had agreed not to provide the requested underwriting support for the Circuit of Wales project. The reasoning behind, and the method for arriving at, this decision has raised a number of concerns for the Committee.

Balance Sheet Classification

101. The potential classification of the project by the Office of National Statistics / Her Majesty's Treasury as "on-balance sheet" was cited by the Welsh Government as a highly significant factor in the Cabinet's decision.

102. The publicly-available information shows that on 13 July 2016, the Cabinet Secretary for Economy and Infrastructure stated in Plenary that:

"Including both direct Welsh Government guarantees and local authority loans, the latest proposal put forward by the Circuit of Wales asks Welsh Government to underwrite around 75 per cent of the total £370 million cost of the project, with local authorities underwriting a further 8 per cent. Unfortunately, despite the efforts of the project backers, this leaves only around 17 per cent of risk being taken by the private sector.

That amount of risk falling on the Welsh taxpayer, through Welsh Government and local authority support, is unacceptable as it currently stands, especially at a time when we are facing significant economic uncertainty from a UK exit from Europe. In our view, this project does not currently provide the level of value for money necessary for the amount of public funding being put at risk. On that basis, I have today told Michael Carrick and Martin Whitaker that I believe further work is needed on this proposal. My door remains firmly open and I've urged

them to revise their bid in such a way where the private sector takes more of the risk in order for this project to be taken forward.

We need to see at least 50 per cent of this project funded and 50 per cent of the risk underwritten by the private sector to justify value for money for Welsh Government and the public purse and they have accepted this principle. My officials will now work constructively with the Circuit of Wales team to ensure this project can be successfully delivered to benefit the local economy of Ebbw Vale and Wales at large.”⁶⁴

103. Following the Cabinet decision on 27 June 2017 not to provide the requested £210 million underwriting support for the project, the Cabinet Secretary for Economy and Infrastructure made the following statement in Plenary on 27 June 2017:

“In July last year I told the company that I would expect to see at least 50 per cent of the project funded and 50 per cent of the financial risk of the project to be undertaken by the private sector, and for the project as a whole to provide value for money for Welsh Government and the public purse.

In February the developers submitted a new proposal to Welsh Government, which was followed by a formal application in April, requesting a guarantee of a loan facility of £210 million. Extensive and detailed due diligence by external experts employed by Welsh Government has shown that due to the way that the deal is structured, the current proposal would see the Welsh Government exposed to more than 50 per cent of the risk. This is because the £210 million underwriting element would carry a higher risk than other parts of the financial package.”⁶⁵

104. However, in response to that point, the Heads of the Valley Development Company have stated that:

“at no point during the due diligence process was the company told by the Welsh Government that this was an issue and that the Welsh

⁶⁴ National Assembly for Wales, **Plenary**, Paragraph 212, 13 July 2016

⁶⁵ National Assembly for Wales, **Plenary**, Paragraphs 241 -288, 27 June 2017

government believed that it would be exposed to more than 50% of the risk.”⁶⁶

105. In his 27 June 2017 statement, the Cabinet Secretary for Economy and Infrastructure went on to say that:

“As a result, following discussions with Office for National Statistics and Her Majesty’s Treasury during the due diligence process, it is assessed that there is a very significant risk that the full £373 million debt of the entire Circuit of Wales project would be classified against Welsh Government capital spending.”⁶⁷

106. In response, the Heads of the Valley Development Company has stated that:

“the company was never informed or made aware of this ONS and HM Treasury advice during the due diligence process. We were promised by Welsh Government officials that we would be consulted if any significant issues arose during due diligence and given an opportunity to respond.”⁶⁸

107. In light of these conflicting statements the Committee sought clarification from the Welsh Government on:

- the dates on which it communicated to HoVDC its concern that the public sector was being asked to take on more than 50% of the project risk in providing the requested £210 million underwriting guarantee for the Circuit of Wales project;
- the date the Welsh Government first communicated to HoVDC the views of Welsh Treasury officials regarding the potential on-balance sheet treatment of the project within the Welsh Government’s accounts;
- the responses received by the Welsh Government from HoVDC on both of these points in advance of the 27 June 2017 Cabinet decision not to provide the requested £210 million guarantee.⁶⁹

⁶⁶ **HoVDC press release, June 2017** [accessed 1 May 2018]

⁶⁷ National Assembly for Wales, **Plenary**, Paragraphs 241 -288, 27 June 2017

⁶⁸ **HoVDC press release, June 2017** [accessed 1 May 2018]

⁶⁹ Written Evidence, PAC(5)-31-17 P1, 4 December 2017

108. In response, the then Deputy Permanent Secretary told the Committee that these issues had been discussed with HoVDC “as early as spring 2016”. He stated that:

“Officials met with representatives of HOVDC on a regular basis particularly between October 2016 and June 2017. The level of risk to the public sector and balance sheet treatment would have formed part of these discussions. In terms of the proposal submitted by HOVDC in February 2017, the full extent of Welsh Government’s potential exposure only became apparent on receipt of the draft due diligence reports in May 2017 and after consultation with HM Treasury. ...Draft copies of the due diligence reports or extracts thereof were shared with representatives of HOVDC in May and June 2017 for fact checking, including the main Grant Thornton due diligence report. HOVDC provided detailed comments on the Grant Thornton report at that time to correct errors of fact and to highlight areas where they disagreed with Grant Thornton’s analysis. Whilst HOVDC made no explicit comment on balance of risk, they challenged the way the assessment of potential financial liability to Welsh Government under the guarantee was being presented. However, that was a matter of interpretation that Grant Thornton did not accept, and HOVDC nonetheless provided written confirmation of the factual accuracy of the report.

Whilst Welsh Government’s final assessment of project risk and classification was not communicated to HOVDC in advance of the Cabinet discussion on 27 June 2017, the general principles were understood and accepted by HOVDC during 2016.”⁷⁰

109. The Welsh Government’s announcement of its decision not to support the project emphasised the accounting classification issue as the primary reason for not supporting the project. This was a concern raised by the Committee with the Permanent Secretary. She sought to allay the concerns of the Committee, following careful reflection of the transcript, by explaining that:

“While the classification issue, and the responsibility of the Welsh Government to manage risk prudently in what is a highly complex area, played a significant part in the assessment of whether to support the Circuit of Wales proposition, it was by no means the sole issue informing that assessment. Indeed, other issues of a more commercial

⁷⁰ Written Evidence, PAC(5)-31-17 P1, 4 December 2017

nature gave cause for concern as detailed in the published due diligence reports on this project, such as job creation claims or the viability of the business model. Hence the Welsh Government's decision not to support this scheme did not come down to a narrow interpretation of accounting rules."⁷¹

110. The Committee also noted that at the evidence session on 5 February 2018, Welsh Government officials suggested that the guarantee would have needed to have been approximately 50 per cent lower or £100 million. Members asked the witnesses whether this was discussed with the company prior to the cabinet decision. The Welsh Government confirmed that a reduction in the guarantee was not discussed with the company in advance of the Cabinet decision because:

“The Welsh Government did not arrive at a formal conclusion as to what level of guarantee would not give rise to a significant classification risk. Given the scale of investment and the commercial risk to which the Welsh Government would have been exposed in the proposed structure, a much smaller guarantee would have been needed to mitigate the risk of an adverse classification ruling – a reduction potentially of more than 50%. However, no definitive number could be established in the abstract.”⁷²

111. While the Committee understands this argument, we do believe there may have been some value in discussing this issue with the company prior to making the decision to ensure that all options had been explored.

112. The Permanent Secretary's letter of 5 March 2018 to the Committee makes it clear that the Welsh Government had concerns about the funding structure and balance of risk which went beyond the issues around balance sheet classification highlighted in the Cabinet Secretary's announcement of 27 June 2017 that the Welsh Government would not provide the financial guarantees necessary for the Project to proceed.

113. We believe that a fuller statement by the Welsh Government at that time, of the various reasons behind its decision would have avoided much of the subsequent political, media and public controversy about the merits of the decision.

⁷¹ Written Evidence, PAC(5)-08-18 P1, 12 March 2018

⁷² Written Evidence, PAC(5)-08-18 P1, 12 March 2018

Advice from external sources

114. The ONS only provides a formal classification of whether a project is “on” or “off” the Government’s balance sheet once a project has been finalised and a signed contract is in place. However, alongside the formal classification process, the ONS operates mechanisms for providing informal advice to government bodies, who are able to request provisional ONS guidance prior to project finalisation and contract signature.

115. The Statistical Classifications Forum minutes from 12 June 2017 state:

“Wales: Circuit of Wales, currently under due diligence. If classification related issues arise then will inform ONS.”

116. The Committee sought clarification on whether the Welsh Government official present at this meeting was either not aware of any balance sheet classification issues raised by the due diligence reports by 12 June reflecting a cross-departmental view at that point in time; or was simply not aware of classification issues that were being discussed by Welsh Treasury or other Departmental officials. In response to this, the Permanent Secretary stated:

“The official present at the meeting was aware of potential classification issues arising from consideration of the Circuit of Wales proposition. On 12 June 2017, at the time of the meeting of the Statistical Classification Forum, that consideration was ongoing.

The Minutes allude to the fact that the ONS would only have been informed following a decision in principle to offer Welsh Government support and when contractual documentation was in near-final or final form. These conditions were not present at that time.”⁷³

117. The Committee is uncertain which part of the minutes allude to the fact that the ONS would only have been informed following a decision in principle to offer Welsh Government support and when contractual documentation was in near-final or final form. However, it seems prudent to us that the Welsh Government official would have flagged this as a potential issue on 12 June 2017 given that it was due to be considered later that month.

118. In making the decision that the level of guarantee for the project would most likely result in this project being classified as on balance sheet by the ONS, the Welsh Government did not seek any advice from the ONS on how this project

⁷³ Written Evidence, PAC(5)-02-18 P3, 16 January 2018

would be classified. The Committee questioned the Welsh Government on why they had not sought provisional guidance, and Andrew Jeffreys, Director – Treasury, Welsh Government explained that:

“That Ministers hadn’t made a decision in principle to go ahead with supporting the project.”⁷⁴

119. The Committee understands this reasoning as the ONS methodology of economic classification states:

“Most policy proposals are in a near-final form when presented to ONS and will include all the relevant details to enable ONS to make a judgement. Any classification decision based on a near-final policy proposal will be deemed as “provisional” and dependent on the proposal being implemented as described.”⁷⁵

120. However, this methodology goes on to state that:

“However, on rare occasions, government departments might seek a view on a proposal at an early stage of development. In such cases, ONS will provide provisional advice on the expected classification of the proposal, based on information available at the time. This is subject to the qualification that a final decision will not be reached until such a time as the policy is implemented.”⁷⁶

121. The Committee therefore explored why this provision to “seek a view on a proposal at an early stage of development” was not utilised in this instance, given the significance of the project to Wales. Andrew Jeffreys suggested that he thought that the ONS were referring mainly to Government projects/initiatives as opposed to private sector projects, but that:

“Private sector projects that have very significant Government subsidy do end up on—or Government support or Government guarantees—. So, just because it’s a private sector project, doesn’t mean it doesn’t engage classification issues. The only point I’m trying to make is that what the ONS usually have in mind when they’re talking about those kind of policy ideas are things that Government’s intending to do and they

⁷⁴ RoP, 5 February 2018, paragraph 146

⁷⁵ Office for National Statistics, [**UK economic statistics sector and transaction classifications: the classification process**](#) [accessed 1 May 2018]

⁷⁶ Office for National Statistics, [**UK economic statistics sector and transaction classifications: the classification process**](#) [accessed 1 May 2018]

want to shape that policy with advice from ONS rather than private sector projects that are looking for Government support. It's a slightly unusual arrangement, really, for them to be giving an opinion on."⁷⁷

122. Given there is a provision to seek advice on the classification of this type of project, and that there was significant emphasis placed on the classification by the Cabinet when deciding whether or not to proceed, that it would have been prudent for the Welsh Government to have sought early advice from the ONS about the interpretation of this. The Committee were unable to establish a satisfactory explanation about why this option was not pursued by the Welsh Government.

Risk Weighting Guidance

123. Andrew Jeffreys explained to the Committee that:

“...the risk weighting of the capital is an important part of the consideration. So, a guarantee that's not junior to the other elements of the funding carries less weight than a guarantee that is junior to other elements of the funding. So, it's not only the size of the guarantee that's crucial; it's what the relative risk of that guarantee is in the overall capital structure. So, where a guarantee is more junior to other elements of funding, then the classification guidance suggests that you should weight that funding more heavily than other elements. And the kind of standard metric might be twice as high—the more junior debt weighted twice as high as the more senior debt.”⁷⁸

124. The Committee established during the meeting that the Government utilised risk weighting guidance based on public-private partnerships rather than service concessions. Andrew Jeffreys told the Committee that this approach was based on the advice of “Treasury colleagues” despite the fact the Government had already concluded this project should be treated as a concession. He set out that:

“There's published and public guidance on consideration of these kinds of projects, so that's Office for National Statistics and Eurostat guidance, but then we consulted with colleagues in the classification branch in... HM Treasury, and also informally with ONS colleagues as well.”

125. He highlighted that:

⁷⁷ RoP, 5 February 2018, paragraph 156

⁷⁸ RoP, 5 February 2018, Paragraph 41

“Part of the problem with the guidance is that it’s not very specific about some aspects, and that there’s quite a lot of case-by-case consideration, not least because these projects, I suppose, are kind of unique in general.”⁷⁹

Recommendation 10. We recommend that the Welsh Government explore with Her Majesty’s Treasury and the Office of National Statistics whether the published guidance on the risk weighting of projects of this nature can be enhanced to ensure that it is fully relevant within a devolved context.

Recommendation 11. We recommend that the Welsh Government work with relevant parties to establish a framework policy for decision-making in relation to large scale projects, which will set out potential sources of advice such as ONS, IPA.

126. The Committee noted that the e-mail chain between the Welsh and UK Treasuries ended with the UK Treasury suggesting that it would not be appropriate for them to provide a view on whether the shareholding and re-financing of debt could be included as part of the total funding to determine the level of the guarantee, and suggest the Welsh Treasury speak to the Infrastructure and Projects Authority (IPA) (the UK Government’s centre of expertise for infrastructure and major projects). Andrew Jeffreys said that in the end the Welsh Treasury judgement was that it was not material if shareholding and re-financing of debt were counted. He explained that this was not discussed further with the IPA as having tried to establish what the overall cost of the project, and therefore the proportion cost of the guarantee being sought:

“...the £210 million was virtually 50 percent even of the unadjusted total cost of the project, and because of the risk-weighting issue that we’d been advised was important to consider, it wasn’t material whether to include or exclude those elements, because you were at 49 per cent if you included everything, and if you applied any kind of weighting to that 49 per cent, then clearly you were above 50 very, very quickly.”⁸⁰

127. We understand the reason behind the decision not to discuss this further with the IPA, but we were unable to ascertain whether the Cabinet was informed about this decision. The Committee sought clarification from the Cabinet

⁷⁹ RoP, 5 February 2018, Paragraph 45

⁸⁰ RoP, 5 February 2018, Paragraph 58

Secretary on whether the advice around the risk weighting guidance was caveated with decision in the Cabinet paper.

128. The Cabinet Secretary declined to share the Cabinet paper with the Committee in line with the “normal conventions” of withholding “sensitive Cabinet papers in order to protect the privacy of Government policy and commercial discussions”. However he did seek to reassure the Committee that he was satisfied that there was sufficient information in the paper for the Cabinet to make an informed decision.

129. As established, whether the shareholding and re-financing of debt could be included as part of the total funding to determine the level of the guarantee was only one of several factors which led to the Welsh Government decision, but the Committee would like to emphasise the importance of the Cabinet being sighted of the full picture when making decisions.

Communication with Heads of the Valleys Development Company

“No showstoppers”

130. There was reference in the Assembly’s Plenary debate (27 June 2017) the decision not to invest in the project and also in the media, about an e-mail sent by a senior Welsh Government Official to Aviva Investors on 14 June 2017. The e-mail outlined that they [Welsh Government] had spoken to lawyers about complying with EU state aid rules. It goes on to state that there were “no showstoppers” with regard to the project. The Committee were keen to clarify what was meant by this, given that the advice on balance sheet classification which was circulating within the Welsh Government was to be a significant factor in the Cabinet’s decision to decline funding on 27 June (13 days later). The Permanent Secretary confirmed that:

“The senior official was aware of potential classification issues arising from consideration of the Circuit of Wales proposition. However, the discussions on 13 June and subsequent email related solely to compliance with EU state aid rules. The full text of the email, dated 14 June 2017, which was sent to Aviva Investors states:

As we are drawing towards the close of our project appraisal process we had a conference with Counsel yesterday on state aid. The good news is that at the moment there does not appear to be

any showstoppers but there is one point that I would like to discuss with you in relation to deal structure.”⁸¹

131. The Permanent Secretary also outlined that the discussion relating to deal structure subsequently took place, and the necessary changes were made. The Committee believe that there is some room for interpretation around the wording of this e-mail, but accept the explanation that this was in relation to State Aid alone. We are however disappointed that the fuller explanation of this matter took so much time to come forward. The Committee asked the Permanent Secretary to confirm whether Welsh Government officials confirmed on 23 June 2017 to Richard Parry-Jones and Martin Whitaker of HoVDC that there were no outstanding issues. In response to this, the Permanent Secretary stated:

“An informal meeting was held with HOVDC on Friday 23 June, as part of the programme of pre-arranged regular progress meetings. Officials did not confirm to HOVDC that there were no major problems or outstanding issues. However, officials did confirm that there was no additional information being sought from HOVDC prior to cabinet considering their decision.”⁸²

Post decision Communication

132. The Welsh Government held a meeting with HOVDC on 30 June 2017, following the Cabinet decision not to provide the guarantee for the project. A formal note of the meeting was produced by Welsh Government officials to be retained as part of Welsh Government’s internal record on the project. However, the Committee was informed that these notes were not shared with HoVDC at the time of drafting, “in line with standard practice for internal documentation” within the Welsh Government.

133. The Committee asked for a copy of these notes to help clarify a number of concerns about what was communicated to the company regarding the timing for the commencement of the guarantee. The Welsh Government provided us with a redacted copy of the notes (redactions were for the identity of junior officials and the key funders for the project due to commercial sensitivity). However, we were surprised that the note had not been agreed at the time with HOVDC.

⁸¹ Written Evidence, PAC(5)-02-18 P3 ,16 January 2018

⁸² Written Evidence, PAC(5)-08-18 P1, 12 March 2018

134. We wrote to HOVDC to clarify whether they considered the Welsh Government's note to be a fair and accurate record of the meeting. In response to our letter, Michael Carrick set out that the HOVDC were not sighted of this note at the time of the meeting, and that the company did not consider this to accurately reflect the conversation. He also provided the Committee with a copy of the company's requested amendments to the Welsh Government's note, which are extensive. The Committee has not sought the Welsh Government's views on the amendments proposed by HoVDC.⁸³

135. We are surprised that the Welsh Government did not share their meeting note with HoVDC at the time of drafting. The note does not set out internal Welsh Government positions, reflections or advice to the Cabinet Secretary; instead it is simply a factual record of a meeting setting out who said what. The note has very little evidential value if it is not agreed at the time by all those included in it, as its accuracy can always be questioned later – as has since happened in this case. It appears to the Committee to be both prudent and common sense for notes of meetings to be circulated in draft to all attendees to confirm their factual accuracy, especially when the Welsh Government is engaged in commercial negotiations.

136. The lack of appropriate contemporaneous documentation was a key theme in the Auditor General's report on the initial funding of this project, and the Committee would hope that the Welsh Government learns from this so that similar issues do not occur in future projects.

Recommendation 12. We recommend that the Welsh Government adopts a standard practice that meeting notes are agreed for factual accuracy by all relevant parties at the point of drafting.

HOVDC and the Creditors Voluntary Arrangement

137. Since the conclusion of the Committee's evidence gathering, on 22 February 2018 HoVDC entered into a Creditors Voluntary Arrangement (CVA), which is an arrangement to pay creditors over a fixed period which allows a limited company to continue trading if creditors agree.

138. HMRC, which is owed £171k by the company, formally opposed the CVA but was outvoted by the other creditors (many of whose directors are either directly or indirectly related to HoVDC itself).

⁸³ Written Evidence, PAC(5)-10-18 P11, 16 April 2017

139. The Welsh Government is not a party to the CVA although it is owed £7.3 M by HoVDC in respect of the loan guarantee. A spokeswoman for the Welsh Government was quoted as saying:

“The Welsh Government is a secured creditor of HOVDC and as such has priority for repayment ahead of the unsecured creditors included in the CVA.”⁸⁴

Recommendation 13. Given the Creditors Voluntary Agreement and the uncertain financial status of the HOVDC, the Committee requires clarification from the Welsh Government on what action it is taking to safeguard its £7.3m debt from HoVDC arising from the Welsh Government loan guarantee.

⁸⁴ **Wales online press article**, Company set up to build Circuit of Wales has debts of more than £31m [accessed 20 April 2018]

Annex – Witnesses

The following witnesses provided oral evidence to the Committee on the dates noted below. Transcripts of all oral evidence sessions can be viewed in full at:

<http://senedd.assembly.wales/mgIssueHistoryHome.aspx?iid=15833>

Date	Name and Organisation
26 June 2017	James Price, Welsh Government Tracey Mayes, Welsh Government
2 October 2017	James Price, Welsh Government* * although Mr Price did not attend Committee specifically to discuss the Circuit of Wales project, questions did arise during his valedictory session
5 February 2018	Shan Morgan, Welsh Government Andrew Slade, Welsh Government Andrew Jeffreys, Welsh Government