



Section 4
Managing
Government
Assets and
Liabilities

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Introduction

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The Department manages various liabilities, such as nuclear liabilities and residual liabilities arising from the coal, steel and shipbuilding industries. It also, through the Shareholder Executive, manages shareholdings in a number of Government businesses, including Royal Mail, British Nuclear Fuel Plc (BNFL), the Royal Mint and QinetiQ.

The Department's challenge is to deliver safe, economic and efficient management of Departmental (and, where relevant, Government) assets and liabilities, and to become a centre of excellence within Government on corporate finance issues.

The Shareholder Executive works with Government Departments and management teams to help Government businesses perform better, ensuring that Government is an intelligent and professional shareholder. It also has a wider corporate finance role, for example examining and negotiating applications for support under regional and industrial assistance programmes.

Assets and Liabilities

Performance in 2005-06

£1billion value enhancement across the Shareholder Executive's six core portfolio businesses (BNFL, CDC, NATS, QinetiQ, Royal Mail, Royal Mint) in the three years to March 2007.

- 4.1 In aggregate the value of the businesses increased £1.7billion in 2004-05, the first year of the three-year target. Company financial data for 2005-06 is not yet available.
- 4.2 The most significant factor was the continuing recovery of Royal Mail profitability in the final year of its Renewal Plan. However, there were also important contributions from NATS, QinetiQ and CDC, partially offset by a negative contribution from the Royal Mint. Although this was a strong performance, the £1billion target has not yet been achieved on a sustainable basis. All six businesses face challenges going forward. In particular, both Royal Mail and NATS face implementing price reviews from their respective regulators and BNFL has to respond to the demands of the new nuclear decommissioning market.

Figure 4.1

UKAEA Analysis of Turnover 2005 (£million)

Decommissioning and environmental restoration	287
Fusion Research	64
UKAEA Constabulary	22
Other	29
Total	402

Figure 4.2

BNFL Financial Data 2005 (£million)

Turnover	2364
Loss on ordinary activities before taxation and exceptional items	(228)
Exceptional profits/(charges)	(243)
Loss on ordinary activities before taxation	(471)
(Decrease) / Increase in cash	775

Royal Mail Group to be successful and profitable in an efficient and competitive postal market.

4.3 Royal Mail now faces the challenge of competition for all its services following Postcomm's decision to fully liberalise the postal services market from 1 January 2006.

4.4 In September 2005, The Department responded to Postcomm's consultation about initial proposals for the control of Royal Mail's regulated prices. The Department emphasised the need for Royal Mail to be able to generate sufficient revenue to enable it to present a robust investment case to the shareholder.

4.5 Following the publication of Postcomm's final proposals in December 2005, the Department worked with Royal Mail to assess the impact of these proposals on the company's financial position and strategic direction. This work also considered the structure of Royal Mail's balance sheet which is dominated by a £4bn pension deficit. On 31 March 2006 Postcomm published its proposed licence modifications for the 2006 price control. These are subject to a statutory notice period which lasts until 2 May 2006.

4.6 Royal Mail's interim results for April to September 2005 built on the successful return to profitability of the renewal plan. The operating profit of £159m was up 20.5% on the previous year. General Logistics Systems (Royal Mail's European parcels business) almost doubled its operating profit to £43m. However, letters volumes were down 1.2%, dropping for only the second time in 25 years. This resulted in a 3% drop in operating profits on the Royal Mail letters business against the same period in the previous year. Post Office Limited's operating losses were £70m. During the year, Royal Mail also achieved some of its best ever quality of service results.

4.7 In March 2006, the European Commission approved the transitional financial facility for rural post offices for a further two years from April 2006 to March 2008. Up to £150 million will be made available each year to maintain the non-commercial rural network. In the same month, Post Office Limited published its report of the findings of their pilots to test innovative and more cost effective ways of delivering post office service in rural communities and the Department announced an extension of the policy of preventing avoidable closures of rural post offices until the autumn.

Figure 4.3
Royal Mail financial targets 2004 (£million)¹⁰⁴

	Financial Targets	Outturn
2003-04 Group profit target	42	220
2004-05 Group profit target	257	537

Figure 4.4
Royal Mail expenditure (£million)

	2003-04 outturn
Profit and loss	537
Gross Capital expenditure	219
Net Capital Expenditure	124
Cost of Capital Charge	191

The Shareholder Executive will become a centre of excellence within Government on corporate finance issues.

- 4.8 The Shareholder Executive has continued to work to ensure that where Government provides financial support to businesses it does so intelligently, and as commercially as possible within the bounds of policy objectives.
- 4.9 In this role over the last year, the Shareholder Executive led Government involvement in MG Rover (an application for rescue aid), Bombardier Aerospace (an application for launch investment in connection with the proposed C Series aircraft) and Airbus (also an application for launch investment in connection with the A350).

Nuclear Liabilities

The Nuclear Decommissioning Authority

- 4.10 The Nuclear Decommissioning Authority (NDA) was established on 1 April 2005 under the Energy Act 2004. The NDA are now the owners of the plant and facilities of BNFL (the Magnox stations, Sellafield, THORP/SMP and Springfields), and took responsibility for managing

clean up at the UKAEA sites. The NDA is charged with cleaning up the UK's historic civil public sector nuclear legacy at its sites safely, securely, cost effectively and in ways that safeguard the environment for this and future generations. In creating the NDA, our aim is to provide a more effective means of dealing with the legacy than has previously existed by driving forward greater efficiencies and through the introduction of competition for site clean up. This is a significant change to our approach to the clean up of the historic civil nuclear legacy in as much that for the first time ever there is a single 'controlling mind' providing a national strategic direction to managing the UK's nuclear clean up programme. And it is a considerable long-term, resource intense challenge – with civil liabilities currently estimated by the NDA (and set out in its strategy) as £35.4 billion.

- 4.11 The NDA has a budget of £2.2 billion; for 2005-06 approximately half funded by grant-in-aid, the other half from commercial income from its productive sites. The contribution from income will probably rise in the short term as opportunities are exploited but then fall off in the medium term as commercial units are progressively taken out of service.

¹⁰⁴ The 2005-06 Royal Mail Accounts will be published in May/June. Updated figures will be available then.

4.12 In its first year of operation the NDA has focused on delivering the existing clean up plans of BNFL and UKAEA who now act as contractors to NDA. This programme of work was set out in its Annual Plan for 2005-06 which followed extensive stakeholder consultation. The NDA has prepared its programme of work for 2006-07 as set out in its 2006-07 Annual Plan. A significant achievement in 2005-06 has been securing efficiencies in programme delivery i.e. more work for less money at its sites by requiring its contractors to effect 7% efficiency savings. This requirement will be rolled over to future years.

4.13 But the NDA's great achievement is the preparation of its over arching (cradle to grave) Strategy to clean up the civil nuclear legacy. It should be noted that this is the first time that the UK has ever had such a Strategy. The NDA acknowledges that in an ideal world its Strategy would have come before the 2005-06 Annual Plan but in the period from its inception to its being established on 1 April that was not feasible. The NDA drew up its Strategy after completing a round of very extensive public consultations (held August – November 2005) with site stakeholder groups, Trades Unions, regulators, Government Departments, Scottish Executive, supply chain companies, and NGOs. All comments were considered and taken on board where appropriate. Feedback was overwhelmingly positive. This first Strategy is ostensibly for 5 years although it might be revised at the end of its first year as the NDA gains in experience. The Strategy provides options for: the restoration of the NDA's sites and their final use; as well as for prioritising safety, security and the environment by making the reduction of high hazards a key NDA focus; an aspiration to deliver accelerated clean up wherever feasible;

a competition schedule to create a strong competitive market to achieve value for money for the tax payer; maintenance and delivery of skills; effective stakeholder engagement; and the provision of socio-economic support for communities affected by decommissioning and clean up of its sites. In addition, the strategy covers how the NDA intends to meet the PSA targets for decommissioning, efficiency, and competition agreed in SR04. As mentioned above the NDA has already achieved its efficiency gains well in advance of the PSA implementation date.

4.14 At the end of its first year the NDA has established itself as a key player in the nuclear industry. It is known and respected as an organisation focussed on deploying innovation, and engineering excellence in delivering the best outcome for the UK in tackling the civil nuclear legacy. Its core value of openness and transparency in its business dealings has been welcomed by stakeholders.

Coal Health Liabilities

Settle coal health compensation claims efficiently and effectively.

4.15 The Department, in conjunction with miners' solicitors and the judge in charge of the lung disease Chronic Obstructive Pulmonary Disease (COPD) Scheme, has continued to work with all parties on the implementation of initiatives to speed up claims processing. As a consequence of two new 'fast track' processes, offer production more than doubled in 2005, from 70,000 in 2004 to 150,000.

4.16 As at 19 March 2006 the Department has made 321,000 payments under the COPD scheme from 521,000 claims received, with £1.8 billion paid in compensation to claimants.

4.17 The total number of claims received under the Vibration White Finger (VWF) compensation scheme is 170,000. The Department has now settled 121,000 claims with £1.2 billion having been paid in compensation to claimants.

4.18 During 2005 the Department's targets for VWF changed to focus on the closure of the scheme through the application of cut-off orders with the Court and the agreement of a Scheme Closure Plan with Capita, the Department's claims handlers. The passing of cut-off dates in the first half of 2005 for submission of Services, Wages Loss and Group 3 claims has enabled the Department to plan and resource more effectively. It is hoped to substantially complete the General Damages part of the scheme by end 2006 and the Services part by end 2007.

4.19 In July 2005 a tender was issued for the procurement of a new three year claims handling contract for COPD/VWF commencing from August 2006. This has been awarded to the current contractor, Capita.

4.20 An external review of the handling of the Department's coal health compensation schemes was published on 15 December 2005. Commenting on the report, Malcolm Wicks, the Energy Minister, said in a written statement to Parliament:

▼ "Given the scale of the task, it is important that there is confidence that the schemes are being well run. I am therefore pleased to take from the report the assurance that:

▼ The administration of the schemes is basically sound although there are lessons to be learned about how the schemes were put into operation;

▼ That, aside from continuing efficiency improvements, no major changes are needed to improve the running of the schemes; and

▼ That the fraud procedures in place are appropriate."

Other Residual Industrial Liabilities

Effectively managed the concessionary coal scheme and acted as Guarantor of the pension funds.

4.21 The National Concessionary Fuel Scheme provides concessionary solid fuel (or cash in lieu) to former employees of the British Coal Corporation and, at the end of 2005; there were 113,000 beneficiaries in the Scheme. Some 28,000 beneficiaries took their entitlement as solid fuel and the remainder as cash in lieu.

4.22 Provisions in EU and UK legislation impacted on our relationship with the two coal pension schemes. As a result the Department reduced its involvement with the governance and investment processes of each of the schemes.

4.23 The trustees of each scheme have undertaken a three yearly investment review and are in the process of making adjustments which marginally reduce exposure to equity volatility, which introduce a cash buffer to avoid the need to sell equities in extreme conditions but which aspire to maintain the same expectation of investment return.

Discharged other physical coal liabilities through the Coal Authority

4.24 The Coal Authority successfully met its liabilities in the year. The minewater programme is making good progress with new schemes being commissioned. Other hazards and property damage arising from the legacy of the coal industry were made good. The mining reports service

continues to provide house purchasers in coalfield areas with information about historic, current and planned coal mining activities.

Shipbuilders Liabilities

4.25 The Department is also responsible for managing the settlement of personal injury liabilities arising from the former employees of the British Shipbuilders Corporation on behalf of the Government. British Shipbuilders Corporation, the former nationalised shipbuilding company, still exists under statute even though the shipyards were sold off during the 1980s. The Corporation has no active trading operations and exists solely to meet its residual liabilities, which relate mostly to personal injury claims of its former employees, primarily through working with asbestos. These have been settled to date by the Corporation directly out of their current assets, which are invested with the National Loans Fund.

4.26 Following a review of the Corporation's liabilities, and an increased likelihood of asbestos related claims from former employees, the Department has taken on the future liabilities of asbestos related claims in line with a Minute to Parliament in 1988, (at the time of re-privatisation) that Government would meet any financial obligations arising from the Corporation in the future.

Plans for 2006-07

The Department will manage its assets to increase value, within the agreed policy and regulatory framework, by:

- ▼ Enhancing the value of the Shareholder Executive's six core portfolio companies (Royal Mail, BNFL, QinetiQ, National Air Traffic Services Ltd and CDC) by £1 billion by 2007 by improving the professional management of those businesses;
- ▼ Continuing to emphasise quality of service and efficiency delivery in these businesses;
- ▼ Applying professional expertise to other businesses owned by Government in order to improve value.

The Department will discharge historic liabilities in a just and efficient manner that delivers value for money by:

- ▼ Ensuring that the Nuclear Decommissioning Authority (NDA) makes progress towards the PSA target of reducing the civil nuclear liabilities by 10% by 2010;
- ▼ Effective management of the health and concessionary coal schemes (including lung disease, vibration and knee injuries schemes) and shipbuilders liabilities.

In achieving these objectives the Department will monitor performance, manage risk and drive out inefficiencies while providing a safe and quality service. For example, the NDA will deliver at least annual 2% efficiency benefits from 2006-07, against its planned programme of work.

Figure 4.5

Expenditure on Assets and Liabilities (£million)

	2003-04 Outturn	2004-05 Outturn	2005-06 Working provision	2006-07 Plans	2007-08 Plans
Total Resource Del	279.8	467.4	1,588.4	1,665.5	1,581.3
<i>of which:</i>					
Nuclear Decommissioning Authority	0	0	1,282.7	1,406.3	1,323.3
UKAEA	198.9	304	11.2	0.0	0.0
British Energy – Historic Liabilities	0.0	184.5	186.2	195.0	200.0
Coal Authority	26.0	27.3	26.3	26.3	24.9
ECGD	0.0	0.0	5.0	5.0	0.0
Post Office ¹⁰⁵	69.3	75.8	28.9	1.8	1.8
Other	31.5	32.2	48.1	31.1	31.3
Total Resource AME	4,772.5	-384.3	-127.9	-258.2	-252.2
<i>of which:</i>					
Health claims and associated expenditure – non cash	941.4	-315.6	-122.5	-6.6	-2.1
<i>Of which: increase/decrease in provision</i>	664.6	-239.3	-54.4	31.3	15.3
<i>Cash expenditure (excluded from resource cost)</i>	894.3	873.2	1,160.5	979.7	531.7
Coal operating subsidy – non cash	0.4	0.5	0.0	0.0	0.0
<i>Cash expenditure (excluded from resource cost)</i>	0.0	0.8	0.0	0.0	0.0
British Coal Corporation External Finance – non cash	0.3	0.0	0.0	0.0	0.0
<i>Cash expenditure (excluded from resource cost)</i>	0.0	0.0	0.0	0.0	0.0
Coal Privatisation – indemnities – non cash	0.0	-0.2	-2.7	-2.6	-2.4
<i>Cash expenditure (excluded from resource cost)</i>	0.0	0.0	7.0	2.5	9.5
Coal privatisation – Avenue Cokeworks – non cash	0.0	8.4	-2.7	-2.5	-2.5
<i>Cash expenditure (excluded from resource cost)</i>	0.0	0.0	7.0	2.0	8.0
BNFL/Magnox decommissioning ¹⁰⁶ – non cash	2,538.8	216.4	0.0	0.0	0.0
<i>Cash expenditure (excluded from resource cost)</i>	0.0	0.0	0.0	0.0	0.0
Managing Nuclear Liabilities (See footnote 104 below)	1,291.6	-293.8	0.0	0.0	0.0
<i>of which:</i>					
UKAEA Decommissioning – non cash	1,281.3	-295.6	242.7	-90.2	-101.9
<i>Cash expenditure (excluded from resource cost)</i>	305.6	288.5	0.0	0.0	0.0
UKAEA other – non cash	10.3	1.8	0.0	0.0	0.0
<i>Cash expenditure (excluded from resource cost)</i>	9.8	7.2	6.5	0.0	0.0

105 Figures for the Post Office include expenditure between 2003-04 and 2005-06 on Post Office Ltd's Urban Regeneration Programme

106 Under the Energy Act 2004, the NDA have taken on responsibility for expenditure on the civil nuclear legacy, and from 2005-06 these liabilities will feature on the NDA balance sheet.