Better Management of Public Services

Resource Budgeting and the 2002 Spending Review

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The Public Enquiry Unit
HM Treasury
Parliament Street
London SW1P 3AG

Tel: 020 7270 4558

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1 Resource budgeting is a central part of the Government's drive to provide world class public services. This major reform of public finance brings to central government the highest standards of financial management and reporting used in the rest of the economy, providing better information for managers and better incentives to reward good management. The 2002 Spending Review sees the full implementation of resource budgeting. This means that for the first time, departments' budgets will reflect the full costs of providing services.

2 This paper:

- describes how resource budgeting contributes to improvements in the delivery of services through better public sector management;
- sets out how the new system will operate, and how it fits in with the Government's overall framework for public spending and fiscal policy; and
- explains the effect of the change on the way spending data will be presented in the 2002 Spending Review and beyond.

The Government's objectives

3 The Government believes that high quality public services require first-rate management. Managers of public services must have the best information on which to base decisions. The right incentives must be in place to reward good management. Furthermore, taxpayers and Parliament have a right to the best possible information on the quality of service and value for money.

Weaknesses of existing system

4 Yet historically, central government has failed to keep pace with improvements in basic financial management in the rest of the economy. The system for authorising, controlling and accounting for public money has, until now, changed little since the middle of the nineteenth century. This system, based almost solely on cash, gave a distorted picture of the cost of providing services, building in perverse incentives and in particular a bias against essential long-term investment.

The move to RAB

5 Because of these weaknesses, the Government has actively and vigorously pursued the introduction of resource accounting and budgeting (RAB). Resource accounting applies best practice from commercial accounting government finance, and resource budgeting uses this as the basis for planning and controlling expenditure. RAB addresses the limitations of a solely cash-based regime and builds on the other significant reforms in public spending in recent years, which have been designed to foster better long term planning, a focus on outcomes rather than inputs, and an emphasis on investment for the future, underpinned by long-term fiscal stability. Internationally, RAB and other changes to the management of public spending have placed the United Kindgom at the forefront of public sector reform.

Benefits of resource budgeting

6 In particular, resource budgeting supports the Government's agenda by delivering:

- new incentives for the management of assets and investment, supporting the Government's plans for increased investment, to reverse the decline in the nation's infrastructure;
- a long-term planning framework removing distortions and perverse incentives intrinsic in the old system, and building in new incentives to reward good management;

- better information for managers on the costs of providing public services on which to base decisions, and better information for Parliament and the public with which to scrutinise the Government's performance; and

- higher quality financial management throughout Government.

Management of investment

7 Many, but by no means all the benefits of resource budgeting involve the better management of public capital – both existing assets and new investment. The plans set out in the 2000 Spending Review provide for a more than doubling of public sector net investment between 2000-01 and 2003-04, with significant increases particularly in health, education and transport. It is important that this additional investment is accompanied by improvements in management. To this end, the Government has already reformed the public spending framework to provide departments with greater freedom and incentives to invest.

8 Resource accounting information underpins some of the key achievements in this area to date, particularly by requiring departments to maintain balance sheets setting out their total assets and liabilities. The ground-breaking National Asset Register, builds on this by identifying the assets owned by the nation and their value. And resource based data informs Departmental Investment Strategies, which are published as part of the Spending Review.

9 The move to full resource budgeting in the 2002 Spending Review will further help the Government to get the most from its assets and new investment. Under RAB, departments' accounts and budgets reflect the full cost of holding and using capital. This means a charge for depreciation – using up an asset – counts as part of the budget, as does a cost of capital charge, reflecting the fact that the Government has borrowed to fund investment and has tied up resources in assets which could have been used elsewhere.

10 As a result of the inclusion of the costs of holding and using capital in departmental budgets, there will, in the 2002 Spending Review, be new incentives to drive down capital costs, to improve the quality of maintenance, to extend the useful lives of assets where it is cost-effective to do so, and to dispose of assets no longer required.

Other benefits

11 But the benefits of RAB go well beyond asset management. Because of the increased sophistication of the financial data available under RAB, decision takers have information available to allow them to view the long-term consequences of their actions, not just the immediate cash consequences. And the resource budgeting system has incentives built in to reward good decision taking, allowing resources to be redeployed into priority areas.

12 Some examples of the other benefits for the management of public services brought about by the full introduction of resource budgeting include:

- improvements in the management of public liabilities – including early retirement costs for public servants and a range of compensation liabilities;

- better management of working capital– debtors, creditors, stock and cash;

- a new framework for managing some of the remaining publicly owned companies, providing them with greater commercial freedoms;

- better measurement of the cost of providing services, supporting the delivery of key Government targets; and

- significant improvements in the level of financial expertise within government departments.

13 Parliament's fundamental role in authorising and scrutinising Government spending is enhanced by resource budgeting. Both Parliamentary Estimates and departmental resource accounts contain a far greater level of information on government spending than before. The process is also given greater transparency through the work of the independent Financial Reporting Advisory Board (FRAB), which provides the Government with expert advice on accounting practices.

RAB and the public spending framework

14 The move to full resource budgeting complements the new framework for public spending introduced by the Government. This framework aims to encourage long-term planning through fixed three-year spending settlements and a focus on delivering high quality outcomes through Public Service Agreements (PSAs). This structure will form the basis of the Spending Review in 2002.

Timetable for full implementation

15 2001-02 is the first year of RAB. Parliamentary Estimates have been presented on this basis, and accounts will be prepared for this year in resource terms. In budgeting terms 2001-02 and 2002-03 are transitional years because the non-cash costs in resource budgets are outside the main departmental budget. From 2003-04 these non-cash costs will be brought into the main budgets.

Resource budgeting and public spending data

16 The inclusion of new costs for public services in departmental budgets, and some consequential changes in the budgetary control framework, will impact slightly on the presentation of public expenditure data. Chapter 4 of this paper describes what they are by restating the existing spending plans set out in the 2000 Spending Review in full resource budgeting terms. This section allows users of public spending statistics to see how the new information will be presented in the 2002 Spending Review.

RAB and the fiscal rules

17 The change in measurement for departmental spending does not, however, have any effect on measurement of the Government's adherence to the key fiscal rules. These will continue to be measured on a different basis.

Changes in departmental data

18 Among the main points of interest in the data for individual spending programmes are:

- total spending managed within the three-year Departmental Expenditure Limits increases on average by around £10 billion per year;
- the level of resources consumed by **Defence** is shown to be considerably higher than previously measured. This is because the costs of the large defence asset base – some £87 billion worth in total – held by the department are measured in budgets for the first time;
- the measure of spending by the **Department of Health** rises by around £2 billion per year, because of the apportionment of capital costs on the NHS Estate into the health budget and because there is a better measure of clinical negligence costs;
- the figures for spending on the **Department for Education and Skills** remains largely unchanged, mainly because the schools estate falls within the control of local authorities and thus is not subject to capital charging;
- the data for the **Department for Environment, Food and Rural Affairs** reflects more fully the economic effect of the foot and mouth outbreak. Although most cash payments were made in 2001-02, the outbreak occurred in March 2001. As resource budgeting records expenditure when the activity first arises, total foot and mouth spending was recorded in the 2000-01 financial year. The treatment of the liability in this way is in line with best accounting practice as it recognises the full cost to government when it accrues.

19 Present Government has pledged to raise the share of national income spent on education to 5.3% by 2003-04, and has said it wishes to see the level of national income spent on health, including private spending, rise towards the European average. Measures against these objectives are unaffected by the move to full resource budgeting, because, like the fiscal measures on a different basis. The outcome of the 2002 Spending Review will be presented on both the existing and new RAB model to ease comparison and prevent confusion.

INTRODUCTION

Resource budgeting is a central part of the Government's drive to provide world-class public services. This major reform of public finance brings to central government the highest standards of financial management and reporting applied in the rest of the economy, providing better information for managers and better incentives to reward good management.

The 2002 Spending Review sees the full implementation of resource budgeting. This means that for the first time, departments' budgets will reflect the full cost of providing services.

This paper:

- **describes how resource budgeting will contribute to improvements in the delivery of services through better public sector management;**
- **sets out how the new system will operate, and how it fits in with the Government's overall framework for public spending and fiscal policy; and**
- **explains the effect of the change on the way spending data will be presented in the 2002 Spending Review and beyond.**

INTRODUCTION

1.1 The Government is committed to delivering world class public services within a framework of long term fiscal stability. The 2000 Spending Review set out the Government's agenda for public services, with increased levels of investment to deliver major improvements in the quality of services. The 2002 Spending Review will build on what has already been achieved and will set the Government's spending plans and objectives for the rest of this Parliament.

1.2 Achieving these objectives requires first-rate management of public resources. Managers of public service must have high quality information on which to base decisions. The right incentives must be in place to reward good management. And taxpayers and Parliament need to hold the Government to account with the best possible information on how their resources have been used and the quality of service they are getting for their money.

1.3 Yet historically, central government has failed to keep pace with improvements in basic financial management in the rest of the economy. In fact, the system for authorising, controlling and accounting for public money has, until now, changed little since the middle of the nineteenth century. The old system, based almost solely on cash, failed to capture the full cost of providing government services. Consequently, this encouraged short-termism in decision making – in particular a bias against investment – and was not conducive to effective public and Parliamentary scrutiny of government spending.

1.4 That is why the Government has actively and vigourously pursued the implementation of resource accounting and budgeting (RAB). In essence, resource accounting involves applying the best commercial accounting and reporting practices to central Government, while resource budgeting uses this information as the basis for planning and controlling public spending.

I.5 The 2002 Spending Review sees the full implementation of resource budgeting. This is a major change in public sector management, as, for the first time, departmental budgets will fully reflect the economic costs of providing services, in particular the costs of holding and using capital assets.

I.6 The purpose of this paper is to explain the implications of the changes:

- **Chapter 2** explains what resource budgeting is, and why the Government sees it as central to its vision for better public services. In particular, this section focuses on how resource budgeting will bring about a step change in the management of publicly owned assets. It will also provide better information for public sector managers on which to base decisions and for Parliament and the public to scrutinise these decisions;

- **Chapter 3** examines in more detail how RAB works in practice, and how it fits in with the new spending framework introduced by this Government; and

- **Chapter 4** shows the impact of resource budgeting on public expenditure data, and the relationship between resource budgeting and the key fiscal aggregates used to measure the Government's performance against the fiscal rules. This chapter illustrates to users of public spending statistics, the way in which data will be presented on the new basis in the 2002 Spending Review. The outcome of the 2002 Spending Review will be presented on both the existing and new RAB model to ease comparison and prevent confusion.

2 How resource budgeting improves service delivery

This chapter describes why and how resource budgeting will bring about major improvements in the management of public services. In particular, this chapter explains how the new system:

- **delivers a step change in the management of capital – both in the utilisation of existing assets and new investment – supporting the Government's plans for increased investment to reverse the decline in the nation's infrastructure;**
- **removes distortions preventing sensible long-term planning intrinsic in the old cash-based system, and builds in new incentives to reward good management;**
- **provides high quality data on the costs of public services, giving managers better information on which to base decisions and providing Parliament and the public better information with which to judge success; and**
- **increases the standard of financial management throughout government.**

2.1 The move to resource accounting and budgeting (RAB) is one of the most significant reforms of the public finances in over a century. The change reinforces the Government's drive to deliver long-term macroeconomic stability and high quality public services. It also brings the Government fully into line with best practice in the rest of the economy, and marks the United Kingdom out as a world leader in public sector reform.

Problems with a cash-based system

2.2 The Government has introduced RAB as part of a wider programme of reforms aimed at removing obstacles to the delivery of first class services. These reforms have been introduced to remedy some of the structural weaknesses identified in the management of public spending in the past.[1] One significant weakness has been the failure by successive governments to keep pace with improvements in financial management and reporting in the rest of the economy. Until now, public spending has been controlled and accounted for almost entirely in terms of cash, a system which has changed little since its introduction in the mid-nineteenth century.

2.3 But the nature of government in the early 21st century bears little resemblance to that of the 1860s. The Government in 2001 is a major presence in the national economy. Total public spending – some £394 billion in 2001-02 – accounts for around 40 per cent of the overall economic activity in the country. The Government is also a major owner of assets. Overall, the public sector owns about one tenth of the UK's total assets, nearly £600 billion.[2]

2.4 Cash-based control alone is an inadequate framework for managing modern public services. The limitations of a cash-based system have contributed to some of the distortions and perverse incentives in the management of public spending. In particular, under a cash-based system:

- there is an in-built bias against **investment**, as long term capital is expensive to fund initially relative to short term current pressures;

[1] The Treasury paper 'Planning Sustainable Public Spending – Lessons from Previous Policy Experience' (November 2000) described lessons learned from previous policy experience in public spending and identified some structural weaknesses in the public spending framework in the past.

[2] Source: National Statistics "United Kingdom National Accounts". chapter 10.

- there is an **absence of incentives** to manage, maintain and fully utilise capital assets once they come into use, as there is no cost for using up or holding capital;
- the timing of payment often may not relate to the actual activity, giving a **misleading picture** of costs incurred in a given time period;
- there is no mechanism for managing **working capital**, such as movements in stocks and delays in payments; and
- no account is taken of **committed future expenditure**, such as compensation payments or clean-up liabilities, all of which count only when they have to be paid, not when they were incurred. Thus the interests of future taxpayers and even generations are not fairly represented.

How does RAB address these problems?

2.5 RAB removes some of the major weaknesses and distortions of a cash-based system. Resource accounting takes as its starting point the main accounting principles and disclosure requirements for private companies (adapted where necessary to take account of the specific circumstances of government). Resource budgeting takes this information and uses it as the basis for planning and controlling public expenditure. RAB is based on the concept of accruals, i.e. that the full consequences of economic activity should be accounted for – not just the flows of cash – and in particular that the treatment of capital spending should reflect its longer-term economic value.

2.6 This helps the Government to set a framework for budgeting better suited to delivering high quality public services by bringing about:

- a new approach for treating **capital investment;**
- Resource budgeting fully recognises the importance of the existing capital stock, not just new investment, supporting the Government's aim to improve the quality of public capital;
- better **incentives** for managers of public services, particularly in the area of asset management, thus encouraging the allocation of resources to priority areas;
- better **information** for managers on which to base their decisions, and for Parliament and the taxpayer to scrutinise them thus improving accountability and transparency; and
- better quality **financial management** across government, in line with best practice in the private sector.

A new approach to capital spending and asset management

2.7 The Government holds a wide range of assets in support of its objectives and responsibilities. The National Asset Register revealed that government departments and their sponsored bodies own some £270 billion of assets, including defence assets – some £87 billion alone – roads, prisons, major IT systems, and equity in NHS trusts. Chart 2.1 below summarises the main asset holdings, and Table 2.1 breaks down the total value of assets held by departments.

Chart 2.1: Central Government Assets

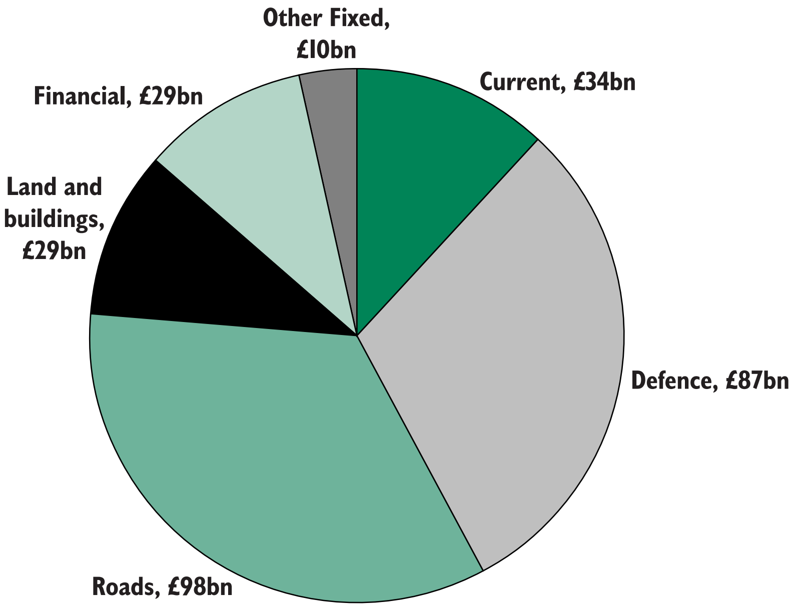


Table 2.1: Assets by Department[1]

£m	1999–2000 financial year
Education and Employment	3,589
Health	25,149
Transport, Environment and Regions	74,593
Home Office	4,803
Lord Chancellor's departments	1,667
Attorney General's departments	31
Defence	86,721
Foreign and Commonwealth Office	1,291
International Development	2,144
Trade and Industry	18,683
Agriculture, Fisheries and Food	1,778
Culture, Media and Sport	3,889
Social Security	200
Scotland	16,723
Wales	8,199
Northern Ireland Executive	21,379
Northern Ireland Office	582
Chancellor's Departments	2,147
Cabinet Office	164

Source: National Asset Register

1 Departmental structure prior to 2001 General Election

2.8 But despite this extensive portfolio of assets, central government's systems and procedures for managing capital have not always encouraged the best stewardship of public resources. The weaknesses of cash based annual planning and control in relation to capital, discussed in Section 2.4 above, have contributed, in part, to an overall decline in the quality and quantity of public investment in the last thirty years. Public sector net investment has fallen steadily from a peak of nearly £29 billion in real terms in 1968-69 to just £5.3 billion in 1996-97. This is a dramatic decline which cannot solely be explained by changes in the structure of the public sector brought about by asset sales – for example of council houses – and privatisations.

2.9 The Government is taking steps to address this legacy of declining investment. In the 2000 Spending Review, the Government set itself the target of more than doubling net investment by 2003-04. Box 2.1 summarises the Government's investment plans.

Box 2.1: The Government's investment plans

The 2000 Spending Review settlement provides for public sector net investment to more than double between 2000-01 and 2003-04. This increase in public investment aims to deliver major improvements in public infrastructure after years of decline.

The plans set out in the 2000 Spending Review for 2001-02 to 2003-04 include:

- **an annual increase of over 9 per cent in real terms on capital spending on health;**
- **a further £1 billion increase in capital investment in education; and**
- **an increase in transport investment of 25 per cent per year as part of the Government's ten year plan for transport.**

2.10 This additional investment needs to be accompanied by reforms in the management of capital, if the improvements in public infrastructure the new investment is designed to bring about are to be realised. To this end, the Government has already implemented significant changes to the public spending framework to tackle some of the structural problems hindering good quality public sector investment, notably:

- the introduction of a separate capital budget for each department, to protect long-term investment from being sacrificed to meet current, short term pressures;
- allowing departments to carry forward underspends from previous years, tackling the 'use it or lose it' mentality which can lead to poor value for money and wasteful end-year surges in spending;
- allowing departments to recycle the proceeds of asset sales to fund new investment; and
- requiring departments to publish Departmental Investment Strategies, detailing how they will deliver their investment programmes, and linking plans for investment to effective management of the existing asset base.

2.11 The move to full resource budgeting will further help the Government to get the most from new investment. RAB transforms the way in which capital is treated in the public finances, thus eliminating any remaining perverse incentives against effective asset management in the spending control framework.

2.12 In particular, under RAB:

- departments, like companies, are required to maintain balance sheets, showing their total assets and liabilities. To do this, they are required to maintain **registers of the assets they own**, and report significant changes in asset holdings in their accounts. This **balance sheet information** helps departments to identify where additional investment is needed and where surplus assets can be replaced. RAB therefore underpins departments' plans on asset management, acquisition and disposal set out in Departmental Investment Strategies;

- a charge for **depreciation** – using up an asset – is included within departments' budgets. This means that the cost of assets are spread over their useful lives rather than just when they are purchased – typically 20 or 30 years for a hospital or a prison, or 3 to 5 years for IT equipment. This gives a much truer picture of the cost of running government services, and places a budgetary discipline on departments to maintain assets properly so as to reduce costs; and

- **a cost of capital charge** is levied on departments' net assets to reflect the opportunity and financing costs of capital – i.e. reflecting that the Government has had to borrow to finance investment and that resources tied up in assets could be (re)deployed elsewhere. Thus departments are required to make assets work for them. Holding capital is no longer a free good as under the previous cash regime.

2.13 The improved information provided by RAB is already making a difference to public sector management, even though full resource budgeting is not yet in place. The National Asset Register is one example. For the first time, departments have a clear view of the nature and value of all their asset holdings. Crucially, this information is open to full public scrutiny and is based on audited data. Box 2.2 gives more details about the National Asset Register.

Box 2.2: The National Asset Register (NAR)

The NAR, first published in 1997, contained summary information on the assets owned by all government departments and their sponsored bodies. The NAR was an international landmark in transparency and accountability in government.

The Government published an updated version of the Register in 2001, which again broke new ground. The Register now includes asset valuations and each department's entry includes a comprehensive description of all significant changes since 1997. The updated Register therefore demonstrates progress made in the last three years in the Government's management of its assets. The National Asset Register is now a vital part of the Government's drive to improve efficiency in the public sector, enabling more informed decisions about the holding, acquisition and disposal of assets.

RAB plays a central role in providing the information contained in the National Asset Register. Under RAB, departments are required to maintain asset registers, to revalue their assets annually, and to have their accounts audited by the National Audit Office.

2.14 The 2002 Spending Review will build on significant achievements to date. The more effective use of assets was an important part of both the 1998 Comprehensive Spending Review and the 2000 Spending Review, and the emerging resource-based information played an important part in decision making. A summary of what has been achieved to date so far is set out in Box 2.3.

Box 2.3: Improvements in asset management

The National Asset Register and Departmental Investment Strategies – both of which are underpinned by RAB information – are already contributing to better management of assets within Government, freeing up scarce resources for much needed investment elsewhere.

The National Asset Register revealed that in 1999-2000 alone, some £1.3 billion worth of surplus assets were disposed of. Under the rules introduced by the Government in the 1998 Comprehensive Spending Review, these receipts can be recycled by departments for other investment.

Examples of good practice on asset management include:

- **the Ministry of Defence disposed of surplus assets worth over £230 million in 1999-2000, and, as part of the Strategic Defence Review, plans to dispose of estate worth a total of £700 million by April 2002;**
- **the Foreign and Commonwealth Office has developed a series of Key Performance Indicators (KPI) for its overseas estate. This measures performance of individual properties and enables identification of assets that are not performing optimally; and**
- **through the Wider Markets Initiative, a number of public bodies are making better use of their assets by engaging in commercial services. Examples include: the Royal Parks Agency, which, through a partnership company has developed an extensive range of commercial activities based on the Royal Parks in London; and British Waterways, which has negotiated a public-private partnership that allows a private company to use canals to lay fibre optic cables with capacity then sold to telecommunications companies.**

BETTER INCENTIVES AND INFORMATION

Better incentives for management

2.15 The move to full resource budgeting in the 2002 Spending Review will improve the incentives for public service managers in a wide range of policy and management issues, and increase the quality of information available to them on which to base decisions.

Asset utilisation and disposal

2.16 Because of the important changes resource budgeting brings to the treatment of capital, it plays a particularly significant role in terms of providing better incentives for managing new investment and existing assets.

2.17 From 2003-04, the first year of the 2002 Spending Review, holding assets will incur a charge in department's main budgets. This means that departmental plans will have to justify the continued funding of continued asset holdings and relate them to the delivery of key government objectives. This will increase the incentives to dispose of those no longer needed. Moreover, as departments will also incur a charge for using up capital – depreciation – there will be new incentives to drive down the capital costs, to improve the quality of maintenance and to extend the useful life of assets where it is cost-effective to do so.

2.18 But the benefits of RAB in terms of incentives go well beyond asset management. The resource budgeting system has incentives built-in to reward good decision taking, allowing resources to be redeployed into priority areas.

Management of provision

2.19 One further example is the treatment of provisions. Provisions are obligations for future spending as a result of past events. Examples within Government include provisions for retirement costs within the civil service, and a range of compensation liabilities, for example for clinical negligence in hospitals or compensation for former miners.

2.20 Under a cash-based system, departments are required to stay within annual cash limits, which can provide an incentive to try to delay payments. Resource budgeting, which counts the full cost of the liability when it emerges, removes this distortion and provides an incentive to discharge the liability cost-effectively, as savings can be redirected elsewhere.

Box 2.4: How resource budgeting provides better incentives – some examples

The following hypothetical examples illustrate the way in which the features of the resource budgeting framework above, would change the way managers of public resources take decisions.

- **managing liabilities – a department might lose or decide not to contest a court case over employment rights which will cost the Government money over many years. Under cash budgeting, the department could have done this, and then paid out the consequences from its budget when they occurred as non-discretionary costs, perhaps in small amounts each year over a long period. But resource budgeting means that when this liability is incurred, i.e. the legal decision is taken, a provision is created, which hits the department's budget immediately. This means the department must take the full cost of the case into account immediately and these costs are visible to Government, Parliament and the public. Moreover, as compensation payments materialise, the Department has an incentive to reduce the costs of administering the payments and the level of payment. Any increase will force the department to absorb further costs while any saving can be redirected to other areas of spending.**

- **managing payments – under the cash system, a department's procurement programme would have counted against their budget when the bill was paid. This could have been some time after the bill was received or even in a different financial year from when the asset came into use. The true cost of acquiring the asset relative to other pressures in each year would not have been properly reflected. Under resource budgeting, the cost is recognised on the balance sheet and in the department's investment budget at each stage that the department incurs costs until the asset comes into use. As well as allowing a department to better judge its priorites, it also shows the full cost of overruns and of writing off projects.**

- **estate management – under the cash system, a department could have invested in two buildings in the same town. The costs of those investments would have hit their budget in the year(s) they were bought or built. Then, each year they continued to own these two buildings, they would only have had to budget for the costs of keeping them running. Under resource budgeting, the department will be budgeting each year for the costs of the depreciation of those buildings, and paying a cost of capital charge, effectively for tying up public money in expensive fixed assets. The department's managers now have a choice: do they need these two buildings relatively close together? If not, they could sell one, reinvest the proceeds in the other, and turn the amount of their budget they have to devote to depreciation and the cost of capital charge each year into service improvements at the one remaining building. In this way, resource budgeting makes the choices about holding onto assets versus investing that resource in the operating costs of services, more real for managers.**

Managing cash and stock

2.21 The information provided in resource accounts allows departments to see exactly the average time taken to meet their payment obligations. Improvements can be measured year – on – year and the information is publicly available in audited accounts. Resource budgeting also means there is no longer any benefit for departments in delaying payments to stay within cash limits in a single financial year as the cost of running services is measured when the resource is used. This means departments now have better incentives to manage working capital.

Commercial freedoms for publicly owned companies

2.22 The Government retains ownership of a number of companies, which, whilst not always operating in fully competitive markets, have considerable commercial potential. Examples include the Patent Office, Ordnance Survey and British Waterways Board.[3] Resource budgeting requires the Government to generate a rate of return, as in a shareholder relationship. If this return is made, the company is free to reinvest additional profits for future benefits.

2.23 Some hypothetical practical examples of how resource budgeting provides better incentives for good decision taking are set out in Box 2.4.

High quality information

2.24 The high quality financial information in resource accounts – which are required to be prepared in line with best practice in the rest of the economy – provides the Government, Parliament and the public with far superior information on the delivery of public services and how it has been spent.

2.25 This is of benefit to policy makers and managers at all levels. At a macro level, RAB supports the operation of the Government's fiscal policy by providing clear rules on the definition of capital spending and a better measure of depreciation in central government.[4]

2.26 At a micro level, RAB provides the Government with a better measure of the true cost of providing individual services. This will assist the Government in ensuring that resources are allocated to priority services in line with the Government's objectives. New resource based information is already assisting departments, for example, in delivering Public Service Agreements and Service Delivery Agreements, the high – level, outcome-focused goals which departments agree during the course of spending reviews. Some examples of the way in which departments are already using resource-based information to improve management are listed in Box 2.5.

2.27 The ways in which the quality of information is improved by resource based information include:

- performance against targets for meeting payment obligations, as resource accounts show clearly how quickly on average departments are paying bills;
- departments which engage in lending or loan guarantees, for example the Department of Trade and Industry in respect of industrial assistance, can see clearly the level of bad debt, which is charged as a cost to their department;
- the balance sheet shows the level of assets under development, and the level of overall use of assets through depreciation relative to new investment; and
- information on an accruals basis shows the level of prepayments already made and activities which have taken place but not yet paid for, allowing departments more effectively to manage cashflow.

[3] This does not apply to a small number of large publicly-owned companies which are classified as self-financing public corporations, such as Consignia and the Royal Mint. These are not controlled directly within departments' budgets.

[4] For a fuller account of the improved fiscal information provided by RAB, see paragraph 4.7 to 4.17.

2.28 Some examples of the way in which departments are already using resource-based information to improve management are listed in Box 2.5.

Box 2.5: Better information for management

Departments are already identifying benefits to their operations by using the better information provided by a resource-based approach to management. For example:

- **To provide a more transparent link between costs and outputs and outcomes, HM Customs and Excise has asked lead Directors to prepare resource accounts for specific PSA/SDA targets before determining the best allocation of the resources given to the Department in the 2000 Spending Review. The department has also developed a comprehensive set of management accounts, bringing together information on operational performance, expenditure and staff deployment and progress on significant projects. The department's Management Committee uses these accounts, which are updated on a monthly basis, to monitor progress and guide any necessary action.**
- **The Ministry of Defence uses resource-based information as part of a balanced scorecard to enable the Royal Navy Board to monitor performance. The four dimensions of the scorecard are output, resources, process and development. These are derived from the high level Naval Strategic Plan and are linked to a risk analysis which identifies critical areas for attention. The scorecard is colour-coded for ease of presentation and identifies any individual aspects requiring attention.**
- **The Foreign and Commonwealth Office's capital budgets for strategic new investments in the diplomatic estate, security and IT used to be held by small specialist strategy units at the centre of the department. The Department is now considering devolving the resource costs of the estate to front-line budget holders.**

A step change in accountability and transparency

2.29 Better information is also available to Parliament and the public on how departments have managed taxpayers's resources. Resource accounts provide similar information for departments to that which companies are required to produce under company law, as well as providing additional information analyzing how different resources have been used. This, combined with the additional information of government performance now available through departments' annual reports on progress against their PSA targets, greatly increases the transparency of government activities.

2.30 All departments' accounts, which are audited by the National Audit Office, now contain for the first time the equivalent of the main financial statements used in commercial accounts, prepared in line with accounting practices used in the private sector. These are:

- the equivalent of a profit and loss statement, showing the level of resources consumed by a department in the year in question. This is known as the **operating cost statement**, reflecting the fact that most central government activities are not profit making;
- **a balance sheet**, showing the assets and liabilities of the department; and
- **a cash flow statement**, showing inflows and outflows from the department during an accounting period.

2.31 Like commercial accounts, resource accounts also require the disclosure of additional information relevant to the Government. The notes to the accounts must include disclosures on the composition and remuneration of the management board, risks where future expenditure may be incurred (contingent liabilities), and a detailed breakdown of assets.

2.32 But resource accounts go further. In addition to the private sector style information described above, resource accounts contain two further statements reflecting both Parliamentary control of expenditure and the policy objectives of departments. These are:

- **a statement of resource outturn**, comparing what Parliament has approved with the actual spending that has taken place; and
- **an analysis of resources by objective**, showing how departmental resources have been split between the main objectives of the department.

Parliament's role in approving spending

2.33 Parliament's fundamental role in giving legal authority to government spending plans continues under resource budgeting and indeed is enhanced by it. Under RAB, departments' spending plans are submitted annually to Parliament for approval. One important feature is that in resource based Parliamentary Estimates, Parliament continues to vote a cash requirement for departments, as well as their overall resource request. This illustrates that, as with any business, an accruals-based system of accounting and budgeting should not mean losing control over cash. Departments have to submit a supplementary request for further resources or cash, with Treasury approval, if they wish to exceed these legally binding limits.

Independent standard setting

2.34 The information in resource accounts forms the basis of both Parliamentary and Treasury control of expenditure under resource-based supply and budgeting. It is therefore vital that there are clearly understood rules for managing public money under RAB.

2.35 To this end, the Government has established an independent group of experts, the Financial Reporting Advisory Board (FRAB), to advise the Treasury on the resource accounting policies. The requirement to consult the FRAB was placed on a statutory footing in the Government Resources and Accounts Act 2000, introduced by the Government to facilitate the switch to RAB. The work of the FRAB is summarised in Box 2.6

Box 2.6: The Financial Reporting Advisory Board

Credibility and transparency are of crucial importance in any system of standard-setting for accounting for public expenditure. The Financial Reporting and Advisory Board (FRAB) provides an independent element in that system.

The Government Resources and Accounts Act, passed in 2000, requires that government to follows, as far as is practicable, the accounting standards used in the private sector as required by the Companies Act. The FRAB's statutory function is to advise the Treasury on how this should be done. It therefore reviews changes proposed to the Government's Resource Accounting Manual (RAM), which Departments are required to follow in preparing their resource accounts. The FRAB reports to Parliament annually on its activities and highlights any departure form UK Generally Accepted Accounting Practice in the RAM, together with its views on any such departures.

The FRAB includes representatives from the Accounting Standards Board, which sets accounting standards for the private sector, the National Audit Office, the Audit Commission, Government Departments and other public bodies, the Office for National Statistics and the academic sector. The Treasury is also represented.

2.36 The move to RAB is leading to significant improvements in the quality of Government financial management. Departments have taken and are continuing to take significant steps to improve the level of financial skills within their organisations. Many have recruited qualified accountants externally and/or engaged private sector expertise to support the preparation of resource accounts. Some are also sponsoring existing members of staff who are pursuing professional financial and accountancy qualifications. Box 2.7 gives two examples.

Box 2.7: Improvements in financial management in departments

The introduction of RAB presented the Ministry of Defence, as the largest asset holder within government with a significant challenge. In response, the department has developed and implemented a comprehensive training programme to support the introduction of RAB, covering professional and vocational, general awareness, business processes and systems. A Finance Training Committee – chaired at Director General level – meets biannually to co-ordinate the provision of training.

The introduction of RAB presented the Department of Trade and Industry (DTI) with the challenge of training not only their key financial personnel in headquarters, but also Finance Officers and staff in government offices, and in its agencies. In response, the department developed a number of awareness and theory-based courses, in conjunction with its supplier of finance training; and its management accounting system operator has provided systems training. To date the department has trained over 1,000 staff from all parts of the business in both these areas. In addition, DTI is sponsoring a number of staff undertaking professional financial qualifications.

2.37 The introduction of RAB, along with the other major reforms to the spending control framework, places the UK at the forefront of improvements in public sector management. With the introduction of full resource budgeting in the 2002 Spending Review, the benefits of RAB outlined in this chapter will become more and more apparent. Chapter 3 sets out in more detail how the next Review will operate.

3 How resource budgeting works

This chapter of the paper:

- **describes briefly the overall framework for controlling spending and improving the quality of public services within the context of the Government's fiscal rules; and**
- **sets out how the move to resource budgeting in the 2002 Spending Review complements that framework, covering what changes and what stays the same.**

The public spending framework

3.1 Since taking office in 1997 the Government have introduced a number of major reforms to the public spending control framework, to foster improvements in service delivery through increased investment, underpinned by a sustainable fiscal position.

3.2 The main changes have been:

- **fiscal Rules** – to ensure that public spending is sustainable and affordable, spending plans are set in accordance with the requirements of the **Code for Fiscal Stability** and must meet the strict fiscal rules set by the Government. The **Golden Rule** states that over the course of the economic cycle, the Government can borrow only to invest, whilst the **sustainable investment rule** requires that public debt should be held at a stable and prudent level;
- **three-year budgeting** – so that departments can plan with certainty over a reasonable time period, spending plans are now set on a three year basis. Firm departmental budgets are set for three years. These are called **Departmental Expenditure Limits (DELs)**. Other expenditure, which cannot be managed on a three year basis is treated as **Annually Managed Expenditure (AME)**. Some examples of AME expenditure include social security, debt interest and Common Agricultural Policy payments;
- **End Year Flexibility** – to avoid the wasteful end-year surges evident in the past, departments can now carry over in full underspends from previous years;
- **separate capital budgets** - there is a separate Departmental Expenditure Limit for capital, which protects long-term investment plans from current pressures. Departments prepare **investment strategies**, setting out how they will use this allocation to improve the stock of public capital; and
- **focus on outcomes** – departments, through their **Public Service Agreements** (PSAs) and **Service Delivery Agreements** (SDAs), agree to deliver specified outcomes and outputs in return for their resources.

Resource Budgeting and the control framework

3.3 These changes complement the move to resource budgeting by encouraging:

- a longer term approach to planning consistent with a sound fiscal strategy;
- a strong emphasis on good quality public investment and the better utilisation of existing assets;
- a focus on the outcomes achieved by public spending, not inputs; and
- transparency in presenting spending information.

3.4 The key aspects of this framework remain unchanged by the introduction of resource budgeting. In particular, for the period covered by the 2002 Spending Review, 2003-04 to 2005-06:

- the definition and measurement of the fiscal rules remain unchanged[5];
- the DEL and AME structure, with separate budgets for resource consumption and new capital investment, remains in place; and
- PSAs will continue to be negotiated alongside expenditure allocations.

3.5 Of course the inclusion of new costs within departments' budgets for the first time in the 2002 Spending Review means that there are changes in the nature of the expenditure departments are managing within the framework of DEL and AME. This inevitably has consequences for the presentation of public expenditure data. Chapter 4 of this paper analyses this in full by restating the existing spending plans set out in the 2000 Spending Review on a full resource budgeting basis, explaining the changes.

Timetable for implementing resource budgeting

3.6 The RAB framework has been carefully developed to fit in with the wider frameworks for outcome focused public management and Parliamentary control of expenditure. In fact, the full implementation of resource budgeting brings to a conclusion a long term programme of reform initiated by the previous Government in 1994 with cross-party support.[6]

3.7 RAB is already operational. In 2001-02, for the first time, Parliament voted departments' Estimates on a resource basis, and their accounts will be presented on the same basis. This follows the approval from the Committee of Public Accounts[7] and the Treasury Committee to discontinue the old cash-based system, in line with the original RAB project timetable.

3.8 2001-02 is also the first full year of resource budgeting. However, to allow departments additional time to develop expertise in monitoring and controlling accruals based expenditure within the context of three year spending limits, Ministers decided in December 1999 to introduce resource budgeting in two stages.

3.9 In Stage 1, spanning the years covered by the 2000 Spending Review (2001-02 to 2003-04), the main new costs introduced by RAB are treated as part of AME, and are therefore not controlled by departments alongside their other expenditure in the three year DEL. As a result these new costs were not included in the presentation of departmental settlements in the 2000 Review.

The 2002 Spending Review

3.10 In order to realise the full benefits of RAB as soon as possible, the Government intends now to proceed as planned with the full implementation of resource budgeting in the 2002 Spending Review, which will set plans for the years 2003-04 to 2005-06.

3.11 This means that departments' main budget for current expenditure, the **resource DEL**, will include, for the first time charges for:

- **depreciation** – the cost of using assets;
- **a cost of capital charge** – the cost of holding assets, normally levied at 6 per cent of net assets; and
- **provisions** – committed future expenditure, such as compensation payments.

[5] Paragraph 4.7 to 4.17 explains this in more detail.

[6] *Better accounting for the taxpayer's money*, Cm2626, July 1994.

[7] 29th report, 1999-2000

3.12 On the capital side, there are further changes:

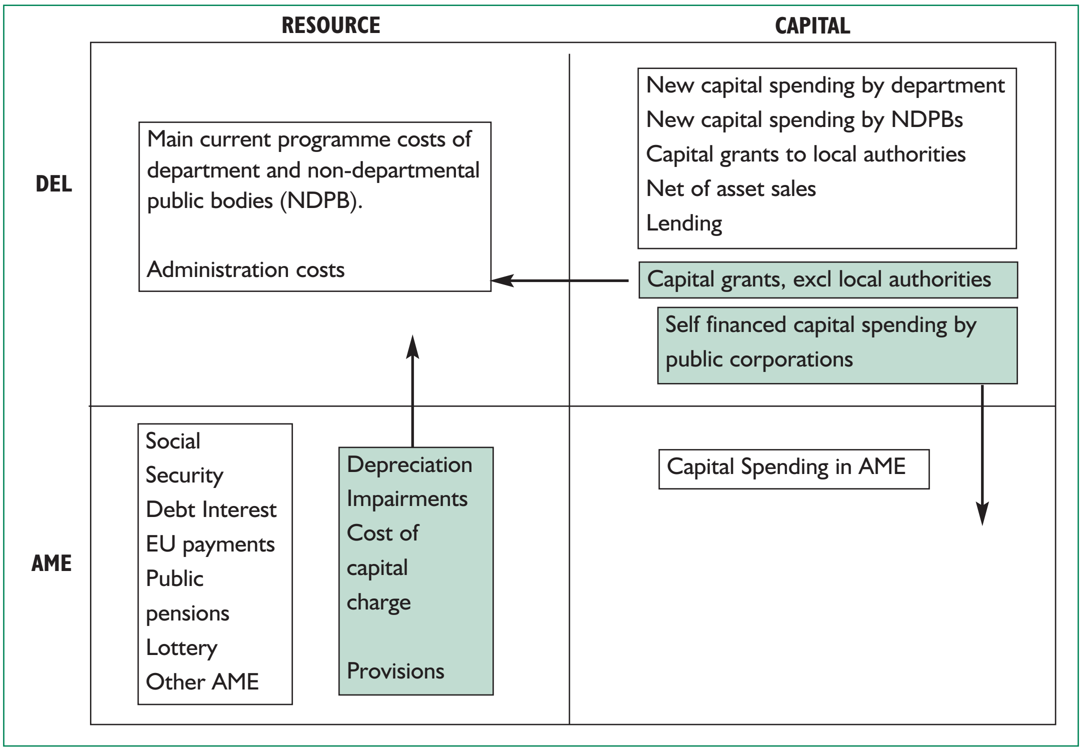
- grants paid to the private sector – for example, to universities – will be managed through the resource budget instead of the capital budget. This reflects the fact that under RAB, spending is only treated as capital if it creates an asset on the Government's balance sheet; and

- so as to reflect the more commercial budgeting relationship for public corporations under RAB, investment by public corporations financed by their own resources will no longer count as part of the parent department's capital DEL.

3.13 So in the 2002 Spending Review, the apparatus for controlling departmental spending remains broadly in line with the system for three year planning introduced by the Government in the 1998 Comprehensive Spending Review. However, the inclusion of new items in DEL, or the transfer between resource and capital DELs as a result of the move to resource budgeting will mean some changes to the way in which the data is presented.

3.14 Table 3.1 illustrates these points, mapping out the main potential changes in departments' budgets. This helps to explain the changes in data that are the focus of Chapter 4. The outcome of the 2002 Spending Review will be presented on both the existing and new RAB model to ease comparison to prevent confusion.

Table 3.1: Changes in budgetary control in the 2002 Spending Review



4 CHANGES TO SPENDING DATA

By including new costs in department' budgets in order to reflect their full economic cost, resource budgeting changes the way departmental spending data is presented.

This chapter analyses the impact of these changes on the data by restating the 2000 Spending Review plans in full resource terms. The aim is to familiarise users of expenditure statistics with the new method of presentation in advance of the publication of the 2002 Spending Review. The new budgeting framework will apply to departments from 2003-04. The tables contained in this chapter are in broadly the same format as those that will be published in Spending Review documentation.

Among the main points of interest are:

- **there is no impact on the Government's adherence to the fiscal rules, which continue to be measured on a basis consistent with the internationally recognised national accounts;**
- **plans will be shown on the old and new basis so it will be clear what the changes will be and why they happen;**
- **budgets for some services, notably defence, are considerably higher than previously measured under cash. This reflects the inclusion in departmental budgets of the cost of the department's extensive asset base. Consequently, health and education growth rates for spending programmes change slightly; and**
- **data for some departments can be lumpy, reflecting the nature of activity measured in accruals terms. For example, the Department for the Environment, Food and Rural Affairs shows a provision for £1.5 billion for foot and mouth related activities in 2000-01. Under cash these costs would have been more spread out and much would have scored in 2001-02. This is in line with best practice accounting, showing the costs as soon as they are apparent to government.**

4.1 Table 3.1 summarises the various changes in budgetary treatment of expenditure, introduced by the move to full resource budgeting. This chapter explains the practical effect of these changes and restates existing spending plans in full resource budgeting terms. The data in this chapter is based on conversions of the existing plans by departments and the Treasury in advance of next year's Spending Review. The data is at this stage **provisional** and further adjustments may be made to reflect the latest information. Nonetheless this data is unlikely to change fundamentally between now and the Spending Review.

What is being measured?

4.2 At a departmental level, the main focus of presentation continues to be the Departmental Expenditure Limit. As Table 3.1 illustrates, the resource DEL shows departmental current spending, with the new accruals items, whilst the capital DEL represents, in the main, the additions to departments' capital stock in the period, net of asset sales.

4.3 Table 4.1 a and Table 4.1 b illustrate by category of change, the aggregate changes in the resource and capital DEL budgets for all departments as a result of the change to full resource budgeting.

Table 4.1: Changes in Departmental Expenditure Limits

Table 4.1a: Changes in Departmental Expenditure Limits – Resource Budget

£bn	2000–01	2001–02	2002–03	2003–04
Resource DEL, existing basis	**170.8**	**187.6**	**200.3**	**211.9**
changes				
depreciation & impairments	8.7	9.0	10.1	10.7
cost of capital charge[8]	10.6	10.5	10.7	11.2
changes in provisions[9]	3.0	0.1	0.5	0.7
capital grants	2.6	3.8	4.4	6.5
other changes	1.6	1.3	1.1	1.0
sum of all changes	*26.5*	*24.7*	*26.8*	*30.1*
Resource DEL, new basis	**197.5**	**212.3**	**227.0**	**242.0**

[8] excludes cost of capital charge on the roads network, which continues to be measured as part of AME.

[9] excludes changes in nuclear decommissioning liabilities, which continue to be measured as part of AME.

Table 4.1b: Changes in Departmental Expenditure Limits – Capital Budget

£bn	2000–01	2001–02	2002–03	2003–04
Capital DEL, existing basis	**20.1**	**24.9**	**28.3**	**33.2**
changes				
capital grants	–2.5	–3.8	–4.4	–6.4
public corporations' self financed investment	–1.1	–1.1	–1.1	–1.1
other changes	–0.5	–0.5	–0.5	–0.5
sum of all changes	*–4.2*	*–5.5*	*–5.9*	*–8.1*
Capital DEL, new basis	**15.9**	**19.4**	**22.4**	**25.1**

Table 4.1c: Changes in Departmental Expenditure Limits – Total Budget

£bn	2000–01	2001–02	2002–03	2003–04
Total DEL, existing basis	**190.9**	**212.5**	**228.6**	**245.1**
changes				
changes in resource DEL	26.5	24.7	26.8	30.1
changes in capital DEL	–4.2	–6.0	–5.9	–8.1
less depreciation and impairments	–8.7	–9.0	–10.1	–10.7
total changes (net)	*13.6*	*10.3*	*10.7*	*11.3*
Total DEL, new basis	**204.5**	**222.6**	**239.3**	**256.4**

4.4 As can be seen from these figures, departmental spending in Resource DEL increases by some £30 billion in 2003-04 alone. This is explained by the following:

- the Resource DEL now includes over £20 billion of charges for holding or using capital, as well as changes in departments' provisions;
- grants which amount to some £6.5 billion in 2003-04, and are used to fund capital outside the public sector, have been switched from the capital DEL to the resource DEL to reflect the fact that these funds do not purchase assets over which the Government has ownership; and

- the capital DEL is reduced further by the transfer to AME of some £1 billion of capital expenditure financed by public corporations. This is in line with the more commercial system that has been introduced which allows public companies from 2003-04 to reinvest additional profits over and above the required return to the sponsoring department.

Total Departmental Expenditure Limits

4.5 In the past it has been the practice to add DELs together to give a single number for a department or group of departments. However, the inclusion of capital consumption costs – depreciation and impairments – in the resource DEL means that continuing simply to add the DELs together would be misleading. This is because capital would be counted twice – once when the new investment is made, and again as it is depreciated over its useful life.

4.6 Therefore, in order to provide a single number for total departmental expenditure, total Departmental Expenditure Limits are calculated net of depreciation and impairments. This is the best measure of total annual spending under resource budgeting as it reflects what is being put into running services, plus net investment. The two DELs, on a gross basis, remain separate controls on departmental spending.

RAB AND FISCAL POLICY

4.7 These changes in Departmental Expenditure Limits do not affect the Government's key fiscal measures. The Government's measurement of its success in adhering to its fiscal strategy, underpinned by strict fiscal rules, therefore also remains unchanged. This part of the paper explains the relationship between resource budgeting and the fiscal measures.

Measures of total spending

4.8 The Government's preferred measure of aggregate spending is Total Managed Expenditure (TME). TME is a measure drawn from the national accounts, which are prepared according to internationally recognised standards and are used *inter alia* for international comparisons. TME forms the expenditure side of net borrowing, which is the Government's preferred measure of its fiscal stance.

4.9 TME can be split into Public Sector Current Expenditure (PSCE), Public Sector Net Investment (new capital investment less depreciation), and depreciation. These measures of total spending are central to delivering the Government's objectives of providing fiscal stability and improving the public infrastructure. Box 4.1 explains how this works in more detail.

Box 4.1: Meeting the Golden Rule and the Government's target for investment

The two key spending aggregates used to measure success in delivering increased investment underpinned by fiscal stability are Public Sector Current Expenditure (PSCE) and Public Sector Net Investment (PSNI). Together with depreciation, these aggregates give Total Managed Expenditure (TME), the Government's preferred measure of total spending.

PSCE plus depreciation make up the expenditure side of the current balance. This is used to measure success against the Golden Rule, which requires that the current budget balances over the course of the economic cycle.

PSNI measures the total new capital investment in the economy funded by government, less depreciation. It therefore provides a measure of the net improvement in the capital stock funded by government. The Government set a target to double public sector net investment by 2003-04 in the 2000 Spending Review.

RAB and fiscal measures

4.10 These fiscal and expenditure aggregates are not affected by the introduction of resource budgeting, as they are determined in accordance with independent international standards and compiled in the national accounts. They will continue to be the basis on which the Government formulates and measures fiscal policy and performance in the period covered by the 2002 Spending Review.

4.11 There are, however, some differences between the way in which RAB (which generally uses accounting policies based on practice in the private sector) and national accounts, (which are based on the framework for national accounting followed by member states of the European Union) classify expenditure. This means, for example, that some spending within the Resource DEL, the control on departmental current expenditure, does not affect Public Sector Current Expenditure. Instead it may count toward Public Sector Net Investment or not at all. There is nothing new about this; departments' budgets already contain some spending which is controlled in budgets but does not affect overall public expenditure. One such example is lending.

4.12 The main differences between what is controlled in DEL under RAB, and national accounts treatment are:

- national accounts do not include a cost of capital charge on net assets, as actual debt interest is scored;
- unlike in RAB, where provisions are recorded in the budget, national accounts do not include commitments for future expenditure such as liabilities for compensation or clean up;
- under RAB, only spending which creates an asset on the Government's balance sheet is considered capital expenditure. National accounts also treat as capital, government grant funded investment elsewhere in the economy;
- national accounts do not classify expenditure on single-use military equipment as investment, whereas RAB does.

The key fiscal tables - expenditure

4.13 Because of these differences, there will be, in the 2002 Spending Review, a series of reconciling adjustments between DEL, programme spending in AME and the fiscal aggregates.

4.14 These adjustments will be the only main change to the presentation of the aggregate spending tables shown routinely in Financial Statement and Budget Reports, pre-Budget Reports and the Public Expenditure Statistical Analysis. Tables 4.2 to 4.4 show the relationship between DEL and AME in resource terms, and, in succession, Total Managed Expenditure, Public Sector Current Expenditure and Public Sector Net Investment. The totals are therefore in line with those in the 2001 Pre-Budget Report Annex B illustrating that the move to resource budgeting has no effect on the key expenditure aggregates.[10]

[10] There may be some small differences reflecting changes in forecasts.

Table 4.2: Total Managed Expenditure

£bn	2000–01	2001–02	2002–03	2003–04
Departmental Expenditure Limits				
Resource budget DEL	197.5	212.3	227.0	242.0
Capital budget DEL	15.9	19.4	22.4	25.1
Resource and net capital	**204.5**	**222.6**	**239.3**	**256.4**
Annually Managed Expenditure				
Departmental AME:				
Social security benefits	99.2	105.5	109.3	115.1
Housing Revenue Account subsidies	3.2	4.6	4.4	4.2
Common Agricultural Policy	2.7	4.5	2.7	2.8
Export Credits Guarantee Department	1.2	0.9	0.6	0.6
Net public service pensions	4.9	5.3	5.4	5.8
National Lottery	1.9	2.1	2.2	2.3
Other programme expenditure	0.2	0.2	0.0	–0.1
Public corporations own-financed capital expenditure	2.4	2.2	2.5	2.2
Non-cash items in AME	4.8	4.7	5.1	5.3
Total departmental AME	**120.5**	**130.0**	**132.2**	**138.2**
Other AME:				
Net Payments to EC institutions	3.7	0.7	2.1	2.3
Locally financed expenditure	18.3	19.3	20.2	21.2
CG debt interest	26.1	22.2	21.4	23.2
Accounting and other adjustments	–9.5	–1.3	0.8	1.5
Total other AME	38.5	40.9	44.5	48.2
AME Margin	–	0.2	2.2	1.5
Annually Managed Expenditure	**159.0**	**171.1**	**178.9**	**187.9**
Total Managed Expenditure	**363.5**	**393.7**	**418.2**	**444.3**
of which:				
Public Sector Current Expenditure	344.5	367.6	389.4	411.1
Public Sector Net Investment	6.3	12.9	14.8	18.6
Depreciation (national accounts)	12.7	13.2	14.0	14.6

Table 4.3: Public Sector Current Expenditure

£bn	2000–01	2001–02	2002–03	2003–04
Resource budget:				
in Departmental Expenditure Limits	197.5	212.3	227.0	242.0
in Departmental AME	110.8	119.3	122.9	128.5
Total resource budget	**308.3**	**331.6**	**349.9**	**370.5**
less capital spending in resource budget				
Capital grants	–2.6	–3.8	–4.4	–6.5
Current spending in budgets	**305.7**	**327.8**	**344.5**	**364.0**
Other current spending in AME:				
Net Payments to EC institutions	3.7	0.7	2.1	2.3
Locally financed current expenditure	16.5	17.5	18.4	19.5
CG debt interest	26.1	22.2	21.4	23.2
AME Margin (current)	–	0.2	2.2	1.5
Accounting and other adjustments	–7.5	–0.8	–0.2	0.6
Public Sector Current Expenditure	**344.5**	**367.6**	**389.4**	**411.1**

Table 4.4: Public Sector Net Investment

£bn	2000–01	2001–02	2002–03	2003–04
Capital budget:				
in Departmental Expenditure Limits	15.9	19.4	22.4	25.1
in Departmental AME	5.7	5.5	4.5	4.2
Total capital budget	**21.6**	**25.0**	**26.9**	**29.3**
Capital spending in resource budget				
Capital grants	2.6	3.8	4.4	6.5
Other capital spending in AME:				
Locally financed capital expenditure	1.8	1.8	1.8	1.8
Accounting and other adjustments	–7.0	–4.6	–4.3	–4.4
Public sector gross investment	**19.0**	**26.0**	**28.8**	**33.2**
less Depreciation (national accounts)	12.7	13.2	14.0	14.6
Public sector net investment	**6.3**	**12.9**	**14.8**	**18.6**

Improvements to fiscal management information

4.15 Resource accounts at present do not extend on a consistent basis beyond central government departments. This means we do not have consistent data for much of the rest of the public sector – particularly local government – to complement the better information provided for central government by resource accounting. This will change with the arrival of Whole of Government Accounts (WGA), which the Government aims to publish for the first time for the financial year 2005-06.

4.16 WGA, will over time, improve fiscal planning by allowing the Government to use an audited public sector balance sheet to pay more attention to measures of public sector net wealth. Box 4.2 describes the WGA project in more detail.

Box 4.2: Whole of Government Accounts

Whole of Government Accounts (WGA) will be commercial-style accounts covering the whole of the public sector. Like departmental resource accounts, WGA will be produced on an accruals basis using private sector accounting standards, adapted where necessary for government. Government will be treated as if it was a single entity by eliminating all significant transactions between public sector entities.

WGA will provide better quality and more transparent information to assist with the development of fiscal policy, to facilitate better management of public services and to help with the more effective distribution of resources. In particular, WGA will provide audited data to underpin the operation of the Golden Rule, and allow the public sector balance sheet to be used in fiscal management.

4.17 In the meantime, RAB information will increasingly provide better information for measurement and planning. For example, the Office for National Statistics, who compile the national accounts, have signaled their intention to use data from resource accounts in compiling depreciation estimates for central government data in due course. This change, and any subsequent changes in estimation as a result of better information arising from RAB, will be reflected in restatements of the national accounts when they are made.

RAB AND DEPARTMENTAL SPENDING TOTALS

Spending plans for individual departments

4.18 The next sets of tables list the existing and restated figures for each department, and the difference brought about by the move to resource budgeting. In tables 4.5, 4.6 and 4.7, which show the resource, capital and total DELs for each department respectively:

- Table a is the existing basis;
- Table b is the new basis under resource budgeting; and
- Table c shows the difference.

4.19 These tables are the standard presentation of departmental expenditure data. It will continue to be presented in this way once the move to full resource budgeting is completed. As in other publications a forward estimate of spending by key function – such as education – is given as part of the table for total DEL.

Table 4.5[1]: Changes in Departmental Expenditure Limits, Resource Budgets

Table 4.5a: Resource Budget, existing basis

£bn	2000–01	2001–02	2002–03	2003–04
Resource Budget				
Education and Skills	14.2	17.3	18.8	20.1
Health	43.6	47.9	52.4	56.6
of which: NHS	*42.8*	*46.9*	*50.5*	*54.5*
Transport and Regions	3.6	4.7	5.1	5.1
Local Government	35.3	36.9	39.0	41.6
Home Office	8.4	8.8	9.2	9.7
Lord Chancellor's departments	2.5	2.8	2.7	2.8
Attorney General's departments	0.4	0.4	0.4	0.4
Defence	18.1	18.4	18.5	18.7
Foreign and Commonwealth Office	1.1	1.2	1.1	1.1
International Development	2.4	2.7	3.0	3.2
Trade and Industry	3.0	4.1	3.7	3.3
Environment, Food and Rural Affairs	1.5	2.1	1.7	1.8
Culture, Media and Sport	1.0	1.0	1.1	1.2
Work and Pensions	5.2	5.8	6.1	6.1
Scotland	12.7	14.8	15.3	16.3
Wales	6.8	7.6	8.1	8.8
Northern Ireland Executive	4.8	5.0	5.3	5.6
Northern Ireland Office	1.1	1.0	1.1	1.0
Chancellor's Departments	3.6	4.0	4.0	4.0
Cabinet Office	1.2	1.5	1.4	1.4
Employment Opportunities Fund	0.6	0.9	0.9	1.4
Invest to Save Budget	–	0.0	0.0	0.1
Capital Modernisation Fund	–	–	–	–
Policy Innovation Fund	–	0.0	0.0	0.0
Reserve	–	1.6	1.3	1.8
Allowance for shortfall*	0.0	–3.1	0.0	0.0
Total Departmental Expenditure Limits	**170.8**	**187.6**	**200.3**	**211.9**

**It is assumed that over the year underspends in total will offset the drawdown of End Year Flexibility.*

[1] Some data in this and subsequent tables is different from the printed version, following late changes. This version is up to date.

Table 4.5b: Resource Budget, new basis

£bn	2000–01	2001–02	2002–03	2003–04
Resource Budget[1]				
Education and Skills	14.6	18.0	19.5	21.0
Health	45.2	50.5	54.6	58.9
of which: NHS	*44.4*	*49.5*	*52.7*	*56.8*
Transport and Regions	6.2	7.6	8.6	10.1
Local Government	35.3	36.9	39.0	41.6
Home Office	9.1	9.5	10.0	10.5
Lord Chancellor's departments	2.7	2.8	2.9	2.9
Attorney General's departments	0.4	0.4	0.4	0.4
Defence	29.0	29.7	31.2	32.1
Foreign and Commonwealth Office	1.3	1.4	1.3	1.4
International Development	3.0	3.1	3.4	3.7
Trade and Industry	5.1	4.3	4.5	4.6
Environment, Food and Rural Affairs	3.7	2.7	2.2	2.3
Culture, Media and Sport	1.1	1.3	1.2	1.3
Work and Pensions	5.2	5.8	6.2	6.2
Scotland	14.5	16.9	17.2	18.3
Wales	8.0	8.3	8.9	9.5
Northern Ireland Executive	6.1	6.3	6.6	7.0
Northern Ireland Office	1.0	1.1	1.1	1.0
Chancellor's Departments	3.9	4.4	4.4	4.5
Cabinet Office	1.4	1.7	1.6	1.6
Employment Opportunities Fund	0.6	0.9	0.9	1.4
Invest to Save Budget	–	0.0	0.1	0.1
Capital Modernisation Fund	–	–	–	–
Policy Innovation Fund	–	0.0	0.0	0.0
Reserve	0.0	1.6	1.3	1.8
Allowance for shortfall*	0.0	–3.1	0.0	0.0
Total Departmental Expenditure Limits	**197.5**	**212.3**	**227.0**	**242.0**
of which non-cash items in DEL:				
Depreciation & impairments	*8.3*	*9.0*	*10.1*	*10.7*
Cost of capital charges	*10.6*	*10.5*	*10.7*	*11.2*
Provisions and other charges	*3.0*	*0.1*	*0.5*	*0.7*

[1] Does not include cost of capital charges on the roads network for the Department for Transport. Local Government and the Regions or the devolved administrations. Also excludes changes in provisions for nuclear decommissioning liabilities. Both of these continue to be managed in AME.

**It is assumed that over the year underspends in total will offset the drawdown of End Year Flexibility.*

Table 4.5c: Resource Budget, changes

£bn	2000–01	2001–02	2002–03	2003–04
Resource Budget				
Education and Skills	0.4	0.6	0.7	0.9
Health	1.6	2.6	2.2	2.3
of which: NHS	*1.6*	*2.6*	*2.2*	*2.3*
Transport and Regions	2.3	2.5	3.4	5.0
Local Government	0.0	0.0	0.0	0.0
Home Office	0.7	0.7	0.7	0.8
Lord Chancellor's departments	0.1	0.1	0.1	0.1
Attorney General's departments	0.0	0.0	0.0	0.0
Defence	10.9	11.3	12.7	13.3
Foreign and Commonwealth Office	0.2	0.2	0.2	0.2
International Development	0.6	0.4	0.5	0.5
Trade and Industry	2.1	0.3	0.8	1.3
Environment, Food and Rural Affairs	2.2	0.5	0.6	0.6
Culture, Media and Sport	0.2	0.2	0.1	0.1
Work and Pensions	0.0	0.1	0.1	0.1
Scotland	1.9	2.1	1.9	2.0
Wales	1.2	0.7	0.7	0.7
Northern Ireland Executive	1.3	1.3	1.4	1.4
Northern Ireland Office	–0.1	0.1	0.1	0.1
Chancellor's Departments	0.3	0.4	0.4	0.4
Cabinet Office	0.2	0.2	0.2	0.2
Employment Opportunities Fund	0.4	0.0	0.0	0.0
Invest to Save Budget	0.0	0.0	0.0	0.0
Capital Modernisation Fund	0.0	0.0	0.0	0.0
Policy Innovation Fund	0.0	0.0	0.0	0.0
Reserve	0.0	0.0	0.0	0.0
Allowance for shortfall*	0.0	0.0	0.0	0.0
Total changes in resource DEL	**26.5**	**24.7**	**26.8**	**30.1**

**It is assumed that over the year underspends in total will offset the drawdown of End Year Flexibility.*

Table 4.6: Changes in Departmental Expenditure Limits, Capital Budgets

Table 4.6a: Capital Budget, existing basis

£bn	2000–01	2001–02	2002–03	2003–04
Education and Skills	1.6	2.9	3.0	3.9
Health	1.3	2.5	2.4	2.7
of which: NHS	*1.3*	*2.3*	*2.3*	*2.6*
Transport and Regions	5.9	7.3	8.1	10.5
Local Government	0.1	0.1	0.3	0.3
Home Office	0.5	1.1	0.9	0.8
Lord Chancellor's departments	0.1	0.1	0.1	0.1
Attorney General's departments	0.0	0.0	0.0	0.0
Defence	5.2	5.5	5.7	6.2
Foreign and Commonwealth Office	0.1	0.1	0.2	0.2
International Development	0.2	0.4	0.4	0.4
Trade and Industry	0.3	0.8	0.8	1.0
Environment, Food and Rural Affairs	0.4	0.5	0.5	0.5
Culture, Media and Sport	0.0	0.1	0.1	0.1
Work and Pensions	0.1	0.2	0.1	0.1
Scotland	2.0	2.4	2.3	2.4
Wales	0.8	0.9	1.1	1.1
Northern Ireland Executive	0.7	0.8	0.8	0.7
Northern Ireland Office	0.0	0.1	0.1	0.0
Chancellor's Departments	–0.2	0.3	0.2	0.2
Cabinet Office	0.2	0.3	0.2	0.2
Invest to Save Budget	–	0.0	0.0	0.0
Employment Opportunities Fund	0.7	0.0	0.0	0.0
Capital Modernisation Fund	–	0.3	0.9	1.2
Policy Innovation Fund	–	0.0	0.0	0.0
Reserve	–	0.0	0.3	0.5
Allowance for shortfall*	0.0	–1.8	0.0	0.0
Total capital DEL	**20.1**	**24.9**	**28.3**	**33.2**

**It is assumed that over the year underspends in total will offset the drawdown of End Year Flexibility.*

Table 4.6b: Capital Budget, new basis

£bn	2000–01	2001–02	2002–03	2003–04
Education and Skills	1.2	2.3	2.3	3.0
Health	1.3	2.4	2.4	2.7
of which: NHS	*1.3*	*2.3*	*2.3*	*2.6*
Transport and Regions	4.1	5.1	5.4	6.2
Local Government	0.1	0.1	0.3	0.3
Home Office	0.4	0.9	0.7	0.6
Lord Chancellor's departments	0.1	0.1	0.1	0.3
Attorney General's departments	0.0	0.0	0.0	0.0
Defence	5.2	5.5	5.7	6.2
Foreign and Commonwealth Office	0.1	0.1	0.1	0.1
International Development	0.2	0.4	0.4	0.4
Trade and Industry	0.0	0.3	0.2	0.3
Environment, Food and Rural Affairs	0.2	0.3	0.3	0.3
Culture, Media and Sport	0.0	0.0	0.0	0.1
Work and Pensions	0.0	0.2	0.1	0.0
Scotland	1.4	1.7	1.5	1.6
Wales	0.5	0.6	0.7	0.7
Northern Ireland Executive	0.3	0.3	0.4	0.3
Northern Ireland Office	0.0	0.1	0.1	0.0
Chancellor's Departments	–0.2	0.3	0.2	0.2
Cabinet Office	0.2	0.3	0.2	0.2
Employment Opportunities Fund	0.7	0.0	0.0	0.0
Invest to Save Budget	–	0.0	0.0	0.0
Capital Modernisation Fund	–	0.3	0.9	1.2
Policy Innovation Fund	–	0.0	0.0	0.0
Reserve	–	0.0	0.3	0.5
Allowance for shortfall*	0.0	–1.8	0.0	0.0
Total capital DEL	**15.9**	**19.4**	**22.4**	**25.1**

**It is assumed that over the year underspends in total will offset the drawdown of End Year Flexibility.*

Table 4.6c: Capital Budgets, changes

£bn	2000–01	2001–02	2002–03	2003–04
Education and Skills	–0.4	–0.6	–0.7	–0.9
Health	–0.1	–0.1	0.0	–0.1
of which: NHS	*–0.1*	*–0.1*	*0.0*	*–0.1*
Transport and Regions	–2.0	–2.2	–2.7	–4.3
Local Government	0.0	0.0	0.0	0.0
Home Office	–0.1	–0.2	–0.2	–0.2
Lord Chancellor's departments	0.0	0.0	0.0	0.0
Attorney General's departments	0.0	0.0	0.0	0.0
Defence	0.0	0.0	0.0	0.0
Foreign and Commonwealth Office	0.0	0.0	0.0	0.0
International Development	0.0	0.0	0.0	0.0
Trade and Industry	–0.3	–0.6	–0.6	–0.7
Environment, Food and Rural Affairs	–0.2	–0.2	–0.2	–0.2
Culture, Media and Sport	0.0	–0.1	0.0	0.0
Work and Pensions	0.0	0.0	0.0	0.0
Scotland	–0.6	–0.7	–0.7	–0.8
Wales	–0.2	–0.4	–0.4	–0.4
Northern Ireland Executive	–0.4	–0.4	–0.4	–0.4
Northern Ireland Office	0.0	0.0	0.0	0.0
Chancellor's Departments	0.0	–0.0	0.0	0.0
Cabinet Office	0.0	0.0	0.0	0.0
Employment Opportunities Fund	0.0	0.0	0.0	0.0
Invest to Save Budget	0.0	0.0	0.0	0.0
Capital Modernisation Fund	0.0	0.0	0.0	0.0
Policy Innovation Fund	0.0	0.0	0.0	0.0
Reserve	0.0	0.0	0.0	0.0
Allowance for shortfall*	0.0	0.0	0.0	0.0
Total changes in capital DEL	**–4.2**	**–5.5**	**–5.9**	**–8.1**

**It is assumed that over the year underspends in total will offset the drawdown of End Year Flexibility.*

Table 4.7: Changes in Departmental Expenditure Limits, Total Budgets

Table 4.7a: Total Budgets, existing basis

£bn	2000–01	2001–02	2002–03	2003–04
Education and Skills	15.8	20.3	21.8	24.0
Health	44.9	50.4	54.8	59.3
of which: NHS	*44.1*	*49.3*	*52.8*	*57.0*
Transport and Regions	9.5	12.1	13.2	15.6
Local Government	35.3	37.0	39.3	41.9
Home Office	8.9	9.9	10.1	10.5
Lord Chancellor's departments	2.6	2.9	2.8	2.9
Attorney General's departments	0.4	0.5	0.4	0.4
Defence	23.3	23.9	24.2	24.9
Foreign and Commonwealth Office	1.3	1.4	1.3	1.3
International Development	2.7	3.1	3.3	3.6
Trade and Industry	3.4	4.9	4.4	4.4
Environment, Food and Rural Affairs	1.9	2.7	2.2	2.3
Culture, Media and Sport	1.0	1.2	1.2	1.2
Work and Pensions	5.2	6.0	6.2	6.2
Scotland	14.7	17.2	17.6	18.7
Wales	7.6	8.5	9.2	9.9
Northern Ireland Executive	5.2	5.8	6.1	6.4
Northern Ireland Office	1.1	1.1	1.1	1.0
Chancellor's Departments	3.4	4.3	4.2	4.3
Cabinet Office	1.4	1.7	1.5	1.6
Employment Opportunities Fund	1.3	0.9	0.9	1.4
Capital Modernisation Fund	0.0	0.4	0.9	1.2
Invest to Save Budget	0.0	0.0	0.1	0.1
Policy Innovation Fund	0.0	0.1	0.1	0.1
Reserve	0.0	1.6	1.7	2.2
Allowance for shortfall*	0.0	–4.9	0.0	0.0
Total DEL	**190.9**	**212.5**	**228.6**	**245.1**

**It is assumed that over the year underspends in total will offset the drawdown of End Year Flexibility.*

Table 4.7b: Total Budgets, new basis

£bn	2000–01	2001–02	2002–03	2003–04
Resources and net capital				
Education and Skills	15.8	20.2	21.8	24.0
Health	46.0	52.6	56.6	61.1
of which: NHS	*45.2*	*51.5*	*54.6*	*59.0*
Transport and Regions	9.9	12.6	13.8	16.2
Local Government	35.3	37.0	39.3	41.9
Home Office	9.3	10.0	10.5	10.8
Lord Chancellor's departments	2.7	2.9	2.9	2.9
Attorney General's departments	0.4	0.4	0.4	0.4
Defence	28.3	28.9	29.5	30.4
Foreign and Commonwealth Office	1.3	1.4	1.3	1.4
International Development	2.9	3.2	3.4	3.7
Trade and Industry	5.1	4.5	4.6	4.8
Environment, Food and Rural Affairs	3.5	2.9	2.4	2.5
Culture, Media and Sport	1.1	1.3	1.2	1.3
Work and Pensions	5.7	6.0	6.2	6.2
Scotland	15.8	18.4	18.6	19.7
Wales	8.3	8.6	9.3	9.9
Northern Ireland Executive	6.0	6.3	6.7	7.0
Northern Ireland Office	1.0	1.1	1.2	1.1
Chancellor's Departments	3.5	4.5	4.4	4.4
Cabinet Office	1.5	1.8	1.7	1.8
Employment Opportunities Fund	1.3	0.9	0.9	1.4
Capital Modernisation Fund	0.0	0.4	0.9	1.2
Invest to Save Budget	0.0	0.0	0.1	0.1
Policy Innovation Fund	0.0	0.1	0.1	0.1
Reserve	0.0	1.6	1.7	2.2
Allowance for shortfall*	0.0	–4.9	0.0	0.0
Total DEL	**204.5**	**222.6**	**239.3**	**256.4**

**It is assumed that over the year underspends in total will offset the drawdown of End Year Flexibility.*

Table 4.7c: Total Budgets, changes

£bn	2000–01	2001–02	2002–03	2003–04
Resources and net capital				
Education and Skills	0.0	-0.0	0.0	0.0
Health	1.1	2.2	1.7	1.8
of which: NHS	*1.1*	*2.2*	*1.7*	*1.8*
Transport and Regions	0.4	0.5	0.6	0.6
Local Government	0.0	0.0	0.0	0.0
Home Office	0.4	0.3	0.3	0.4
Lord Chancellor's departments	0.1	0.1	0.1	0.0
Attorney General's departments	0.0	0.0	0.0	0.0
Defence	5.0	5.0	5.3	5.5
Foreign and Commonwealth Office	0.1	0.1	0.1	0.1
International Development	0.3	0.0	0.1	0.1
Trade and Industry	1.7	-0.4	0.1	0.4
Environment, Food and Rural Affairs	1.8	0.2	0.2	0.2
Culture, Media and Sport	0.1	0.1	0.1	0.1
Work and Pensions	0.0	0.0	0.0	0.0
Scotland	1.1	1.2	1.0	1.1
Wales	0.7	0.0	0.1	0.1
Northern Ireland Executive	0.7	0.6	0.6	0.7
Northern Ireland Office	-0.1	0.0	0.0	0.0
Chancellor's Departments	0.1	0.2	0.2	0.2
Cabinet Office	0.1	0.1	0.2	0.2
Employment Opportunities Fund	0.0	0.0	0.0	0.0
Capital Modernisation Fund	0.0	0.0	0.0	0.0
Invest to Save Budget	0.0	0.0	0.0	0.0
Policy Innovation Fund	0.0	0.0	0.0	0.0
Reserve	0.0	0.0	0.0	0.0
Total changes in DEL	**13.6**	**10.3**	**10.7**	**11.3**

Analysis of changes

4.20 Box 4.3 identifies and explains some of the main changes in departmental spending data.

Box 4.3: Changes in departmental spending data

Some of the key points emerging from the new data are:

- **the level of resources consumed by Defence are shown to be considerably higher than previously measured. This is because the costs of the large asset base – some £87 billion – held by the Ministry of Defence are included in budgets for the first time;**
- **the measure of spending by the Department of Health rises by nearly £2 billion per year, as capital costs on the NHS estate and provisions for clinical negligence are now fully recognised in the health budget;**
- **the figures for spending on the Department for Education and Skills remain largely unchanged, mainly because the schools estate falls within the control of local authorities and thus is not subject to capital charging;**
- **the data for the Department for Environment, Food and Rural Affairs reflects more fully the economic effect of the foot and mouth outbreak. Although most cash payments were made in 2001-02, the outbreak occurred in March 2001. As resource budgeting records expenditure when the activity first arises, total foot and mouth spending was scored in the 2000-01 financial year. This reflects best accounting practice, showing the costs to government as they arise.**

Analysis by department

4.21 The following section summarises the changes for all major Government Departments.

Education and Skills

4.22 The data for the Department for Education and Skills changes little under full resource budgeting. The costs of capital consumption are low for the department because schools appear on the balance sheets of local authorities and universities are privately owned institutions. Consequently neither are inside the boundary for resource accounting.

4.23 There are some substantial switches from the capital to the resource side of the budget, reflecting the reclassification of capital grants to the private sector. This has no effect on the total figure.

Health

4.24 The Department of Health's total DEL increases by around £2 billion in each of the years shown in the tables. This is largely because of the transfer of capital charges into DEL. It also reflects the accruals treatment of liabilities, for example in clinical negligence, whereby liabilities are recognised at the time they are incurred, not when cases are finally settled.

Transport, Local Government and the Regions

4.25 The rise in resource DEL for the Department of Transport, Local Government and the Regions of around £600 million per year reflects mainly the transfer into DEL from AME of some housing related expenditure, as well as the inclusion of costs of capital charges on the department's assets.

4.26 There is also a substantial switch from the capital to the resource DEL – some £4.8 billion in 2003-04 – which reflects the new treatment of capital grants to private sector bodies. This is primarily in the sectors of transport and housing. Another change is the reclassification of £400 million of routine roads maintenance as operating expenditure rather than investment.

4.27 The cost of capital charge on the £70 billion roads network, for which the department is responsible and which amounts to some £4 billion, is not included. Because of the size and volatility of this figure it will continue to be treated as part of AME in the 2002 Spending Review. The same applies to the roads networks managed by the devolved administrations.

4.28 There is no change in the line for local government expenditure, as resource accounting and budgeting applies only to central government.

Home Office

4.29 The Home Office DEL rises overall by some £300 to £400 million per year, mainly because of capital costs associated with the prison estate.

Defence

4.30 The Ministry of Defence is the most capital intensive of all government departments with some £87 billion of asset holdings. Consequently under resource budgeting, which measures the cost of the consumption and financing of investment, it is transparent that defence consumes a larger proportion of government resources than identified under the cash-based system of accounting and budgeting.

4.31 Overall, the defence budget, net of depreciation and impairments, is £30.4 billion in 2003-04, as opposed to £24.9 billion at present. Virtually all of this change is attributable to the increase in the resource DEL, which includes the capital consumption costs.

Foreign and Commonwealth Office

4.32 The increase in the Foreign and Commonwealth Office's DEL of around £70 million per year reflects mostly costs of capital charges on the overseas diplomatic estate.

International Development

4.33 The relatively small increase in the DEL for the Department for International Development is due largely to the cost of capital on financial assets, notably as owner of the UK's holdings in some international financial institutions such as the World Bank.

Environment, Food and Rural Affairs

4.34 The large increase of some £1.6 billion in the Department for the Environment, Food and Rural Affairs in 2000-01, reflects the changes in the treatment of pre-committed government expenditure. Payments in DEL relating to foot and mouth are largely scored in the 2000-01 financial year, when the liabilities arose, rather than 2001-02 when much of the compensation was paid out. Much foot and mouth compensation was also in AME.

4.35 In the other years covered, the small increases are attributable to the cost of capital charge on the assets of the department and its sponsored bodies, such as the Environment Agency.

Trade and Industry

4.36 The Department of Trade and Industry shows higher levels of expenditure in 1999-2000 and 2000-01. This is largely the result of a revision of provisions for coal health liabilities. Under full resource budgeting, these are recorded on an accruals basis in the resource budget part of DEL and so hit the budget in the year such movements are recognised. This does not apply to liabilities to decommission nuclear waste, which continue to be managed in AME because of their size and volatility.

Lord Chancellor's Department

4.37 The Lord Chancellor's Department's budget increases by between £60 million and £90 million in each of the years covered. This is explained by changes in provisions for legal aid commitments.

Culture, Media and Sport

4.38 The figures for the Department of Culture, Media and Sport rise by around £80 million to £90 million per year, reflecting the capital costs associated with the department's sponsored bodies, mostly museums and galleries. There are also some switches between the resource and capital budgets, arising from the new treatment of capital grants to the private sector.

Work and Pensions

4.39 The Department for Work and Pensions (DWP) brings together the former Department of Social Security with the employment programmes of the Department for Education and Employment. The resource budget does not increase greatly in 2003-04, because the department does not have an extensive asset base and therefore does not have high cost of capital charges.

Devolved Administrations

4.40 The data for the devolved administrations, which has been converted on the same basis to allow the comparisons with UK and English departments, show a rise reflecting in the main the capital costs of the wide range of services provided by the devolved administrations.

Presentation of functional spending

4.41 Government spending is allocated primarily by department, and consequently the focus of presentation is often departmental expenditure. However this does not tell the whole story, as Government services, such as education and transport, are delivered by a range of bodies, often a mixture of departments, the devolved administrations, local government and the private sector funded by Government grants.

4.42 So, since the 2000 Spending Review the Government has presented spending data for key services in functional terms. For example, the 2000 Review included plans for:

- a 5.7% average annual growth in health spending in the UK between 2000-01 and 2003-04;
- a 5.6% annual average growth in education over the same period;
- a two and a half fold increase in transport investment as part of the ten year plan for transport; and
- the first real terms planned incerase in the defence budget in over a decade.

4.43 Resource budgeting measurement changes the presentation of this data to varying degrees. The new data impacts slightly on growth rates for some individual spending programmes. Table 4.8 shows the growth in spending from 2000-01 to 2003-04 announced in the 2000 Spending Review for education and health, and how they would have looked had full resource budgeting data been used.

Table 4.8: Impact on key growth rates

	£bn		average annual
	2000-01	2003–04	growth rate
UK education spending			
2000 Review Presentation	45.9	58.1	5.6%
2002 Review Presentation (RAB basis)	46.0	58.2	5.6%
UK health spending			
2000 Review Presentation	54.2	69.0	5.7%
2002 Review Presentation (RAB basis)	55.7	71.7	5.8%

[12] As noted in the Statement of Funding Policy, the application of the Barnett formula under the second stage of resource budgeting is being discussed by the Treasury and the devolved administrations.

International comparisons

4.44 The table shows some small changes in growth rates as a result of the different measurement. The change is no more than half of one percent in any one case. In health, the growth rate rises slightly because of the increasing costs of capital, and rises in estimation for clinical negligence. The new method of presentation does not alter the rate of growth in the defence budget, the first planned increase in defence spending for a decade. In other areas the growth rate might fall slightly because of the higher starting point and the relatively stable costs of capital over the period being considered.

4.45 So although there are some small changes, the impact of the measures announced by the Government in the 2000 Spending Review remain largely unchanged.

4.46 The presentation of the 2002 Spending Review will be done on the basis shown above. When comparing over longer periods of history, cash data will be used because of the absence of resource data over a long period. The Government will make it explicit when cash as opposed to resource based data is being used.

4.47 The Government has pledged to raise the share of national income spent on education to 5.3% by 2003-04, and has said it wishes to see the level of national income spent on health, including private spending, rise towards the European average.

4.48 The outcome of the 2002 Spending Review will be presented on both the existing and new RAB model to ease comparison and prevent confusion. Like the fiscal rules, the data for spending as a proportion of GDP is compiled by the Office for National Statistics on a different basis than resource budgeting, and in line with internationally recognised standards for national accounts. This allows a proper comparison to be made with other countries, and measurement of trends in spending over longer periods of time against agreed criteria.

5 Conclusion

5.1 This paper has described why the Government is committed to the full implementation of resource budgeting, and the benefits the reform will bring to the delivery and management of public services.

5.2 This major reform continues to provide a significant challenge to all areas of central Government. Much has already been achieved, for example the improvements already evident in the management of public capital. The challenge for the future is to ensure that, following the change to full resource budgeting in the 2002 Spending Review, managers at all levels of Government use the added information intelligently and respond to the new incentives the new system provides.

5.3 Such a process of continuing improvement will be assisted if those who scrutinise the workings of Government – Parliament, independent experts and other stakeholders – see the more transparent information contained in resource accounts and budgets as an important new resource in their work.