C THE PUBLIC FINANCES

The latest projections for the public finances show that the Government is firmly on track to meet its strict fiscal rules over the economic cycle, using cautious assumptions and in the cautious case, while meeting its international and public spending commitments:

- **the average current budget since the start of the present cycle in 1999-2000 is comfortably in surplus, ensuring the Government is on track to meet the golden rule; and**
- **public sector net debt is projected to be low and stable throughout the next five years, comfortably meeting the sustainable investment rule, and at between 31 and 34 per cent of GDP, the lowest in the G7.**

In the short term, the full operation of the automatic stabilisers means that fiscal policy is supporting monetary policy in maintaining economic stability during a period of global uncertainty. In the medium term, the public finances return towards the Budget 2002 profile as economic growth strengthens. The use of cautious assumptions and the 'stress test' against the cautious case help to ensure that the public finances are sound and sustainable, despite the continuing international uncertainty and global economic weakness.

INTRODUCTION

C1 Chapter 2 describes the Government's fiscal policy framework and shows how the projections of the public finances are consistent with meeting the fiscal rules. This chapter explains the latest outturns and the fiscal projections in more detail. It includes:

- five-year projections of the current budget and public sector net debt, the key aggregates for assessing performance against the golden rule and the sustainable investment rule respectively;
- projections of public sector net borrowing, the fiscal aggregate relevant to assessing the impact of fiscal policy on the economy;
- projections of the cyclically-adjusted fiscal balances; and
- detailed analyses of the outlook for government receipts and expenditure.

C2 The fiscal projections continue to be based on deliberately cautious key assumptions audited by the National Audit Office (NAO).

MEETING THE FISCAL RULES

C3 Table C1 shows five-year projections for the current budget and public sector net debt, the key aggregates for assessing performance against the golden rule and the sustainable investment rule respectively. Outturns and projections of other important measures of the public finances, including net borrowing and the cyclically-adjusted fiscal balances, are also shown.

C4 As explained in Chapter 2, the Government's provisional view is that the current economic cycle started in 1999-2000. Based on the assumptions used in these projections, the economy will next return to trend levels, ending the current cycle, in 2005-06.

Table C1: Summary of public sector finances

	Per cent of GDP							
	Outturns		Estimate	Projections				
	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Fairness and prudence								
Surplus on current budget	2.2	1.0	–1.1	–0.8	–0.1	0.2	0.4	0.6
Average surplus since 1999-2000	2.2	1.8	1.1	0.7	0.6	0.5	0.5	0.5
Cyclically-adjusted surplus on current budget	1.7	0.9	–0.5	0.2	0.5	0.4	0.4	0.6
Long-term sustainability								
Public sector net debt – end year	31.2	30.2	30.9	32.2	32.7	33.2	33.5	33.8
Core debt	31.3	30.3	30.4	30.9	30.9	31.2	31.6	32.0
Net worth[1]	21.3	26.2	22.9	21.7	20.0	18.5	18.0	17.0
Primary balance	3.8	1.8	–0.6	–0.8	–0.4	–0.3	–0.1	–0.1
Economic impact								
Net investment	0.5	1.0	1.2	1.7	2.0	2.1	2.1	2.2
Public sector net borrowing (PSNB)	–1.7	0.0	2.3	2.5	2.1	1.9	1.7	1.6
Cyclically-adjusted PSNB	–1.2	0.1	1.7	1.5	1.5	1.7	1.7	1.6
Financing								
Central government net cash requirement	–3.7	0.3	2.0	3.2	2.4	2.1	2.2	1.9
Public sector net cash requirement	–3.9	0.3	2.1	2.9	2.3	1.9	2.0	1.7
European commitments								
Treaty deficit[2]	–1.7	0.0	2.3	2.4	2.1	1.9	1.7	1.7
Cyclically-adjusted Treaty deficit[2]	–1.2	0.1	1.7	1.5	1.4	1.7	1.7	1.7
Treaty debt ratio[3]	39.8	37.9	38.0	39.0	39.4	39.6	39.9	40.1
Memo: Output gap	0.9	–0.2	–1.1	–1.4	–0.7	–0.1	0.0	0.0

[1] *At end-December; GDP centred on end-December.*

[2] *General government net borrowing on a Maastricht basis.*

[3] *General government gross debt.*

The golden rule

C5 The projections show that the Government is firmly on track to meet the golden rule. Over the period of this cycle, from 1999-2000 to 2005-06, the current budget is comfortably in surplus. Similarly, the average surplus on the current budget is positive since the start of the cycle and throughout the projection period. The same is true were the current cycle thought to have started in 1997-98. The cyclically-adjusted surplus, which allows underlying or structural trends in the indicators to be seen more clearly by removing the estimated effects of the economic cycle, temporarily shows a deficit in 2002-03, before returning to surplus for the rest of the projection period.

C6 Following a deficit of 3 per cent of GDP in 1996-97, current budget surpluses of more than 2 per cent were recorded in 1999-2000 and 2000-01 and of around 1 per cent of GDP in 2001-02. Largely as a result of cyclical and other temporary factors, the current budget moves into a deficit of 1.1 per cent of GDP in 2002-03, before gradually returning to surplus in 2005-06 and reaching a surplus of 0.6 per cent of GDP by 2007-08.

The sustainable investment rule

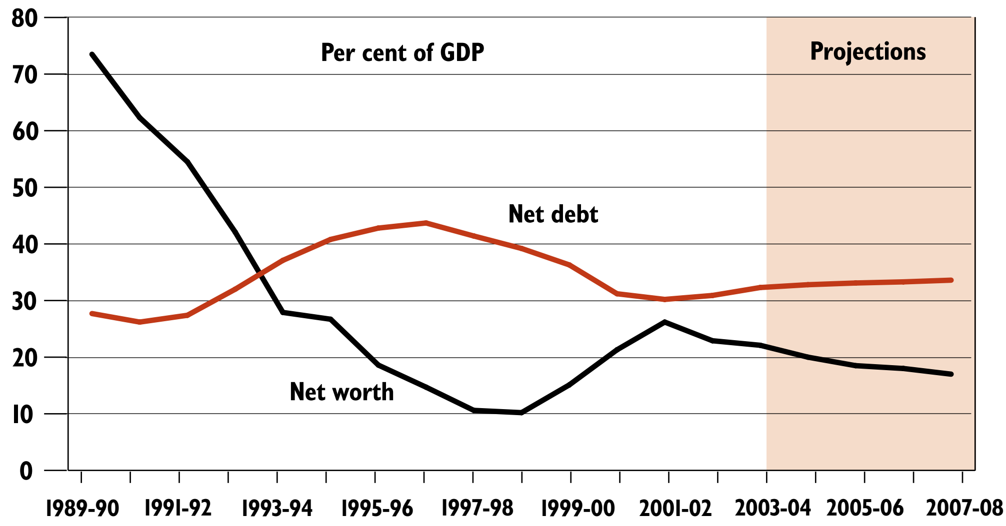
C7 The sustainable investment rule is also comfortably met over this economic cycle. In 1996-97, public sector net debt stood at 44 per cent of GDP. The tough decisions on taxation and expenditure taken by the Government, including the decision to use the proceeds from the auction of spectrum licences to repay debt, reduced net debt to around 30 per cent of GDP by the end of 2001-02. It is now projected to grow slowly, but to remain below 34 per cent of GDP, as the Government borrows modestly to fund increased investment in public services. The projections for core debt, which exclude the estimated impact of the economic cycle, increase more slowly to 32 per cent of GDP.

Net worth

C8 Net worth is the approximate stock counterpart of the current budget balance. Current budget surpluses of over 2 per cent of GDP in recent years increased net worth to 26.2 per cent of GDP in 2001-02. Modest declines are projected for later years. At present, net worth is not used as a key indicator of the public finances, mainly as a result of the difficulties involved in measuring accurately many government assets and liabilities.

C9 Chart C1 shows public sector net debt and net worth as a per cent of GDP from 1989-90 to 2007-08.

Chart C1: Public sector net debt and net worth



Net investment

C10 As a result of decisions taken in the 2002 Spending Review, public sector net investment is projected to rise steadily to $2^1/_4$ per cent of GDP in 2007-08. These increases are sustainable and fully consistent with the Government's long-term approach and the fiscal rules, since net debt is being held at a stable and prudent level, well below 40 per cent of GDP.

Net borrowing

C11 This increase in net investment, together with the new projections for the current budget, mean that public sector net borrowing is expected to increase to a maximum of $2^1/_2$ per cent of GDP in 2003-04, helping monetary policy maintain economic stability while the economy is below trend, before decreasing to around $1^1/_2$ per cent of GDP in later years as the economy moves back to trend. Cyclically-adjusted public sector net borrowing is around $1^3/_4$ per cent of GDP or lower in every year from 2003-04.

Financing **C12** The central government net cash requirement was 0.3 per cent of GDP in 2001-02. It is projected to increase in 2002-03 and subsequent years, mirroring the profile of net borrowing.

European commitments **C13** Table C1 also shows the Treaty measures of deficit and debt used for the purposes of the Excessive Deficit Procedure – Article 104 of the Treaty. Both the reference levels of 3 per cent of GDP for the deficit and 60 per cent of GDP for gross debt are achieved throughout the projection period.

CHANGES TO THE FISCAL BALANCES

C14 Table C2 compares the latest estimates for the main fiscal balances with those in the Pre-Budget Report and in Budget 2002.

Table C2: Fiscal balances compared with Budget 2002 and the 2002 Pre-Budget Report

	Outturn	Estimate[1]			Projections		
	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Surplus on current budget (£ billion)							
Budget 2002	10.6	3.2	7	9	7	9	–
Effect of revisions and forecasting changes	–3.0	–7.9	–12	–7	–3	–1	–
Effect of discretionary changes	–	–1.0	1	0	1	1	–
PBR 2002	7.7	–5.7	–5	3	5	8	10
Effect of revisions and forecasting changes	2.3	–4.1	–4	–3	–1	–1	0
Effect of discretionary changes	–	–1.9	0	–1	–1	–1	–1
Budget 2003	**9.9**	**–11.7**	**–8**	**–1**	**2**	**6**	**9**
Net borrowing (£ billion)							
Budget 2002	1.3	11.2	13	13	17	18	–
Effect of changes in current surplus	3.0	8.9	12	6	2	1	–
Effect of changes in net investment	–3.1	–0.1	0	0	0	0	–
PBR 2002	1.2	20.1	24	19	19	19	20
Effect of changes in current surplus	–2.3	6.0	4	4	3	2	1
Effect of changes in net investment	0.7	–2.1	–1	1	1	0	0
Budget 2003	**–0.4**	**24.0**	**27**	**24**	**23**	**22**	**22**
Cyclically-adjusted surplus on current budget (per cent of GDP)							
Budget 2002[2]	1.0	0.5	0.6	0.7	0.6	0.7	–
PBR 2002	0.7	0.2	0.3	0.6	0.5	0.6	0.7
Budget 2003	**0.9**	**–0.5**	**0.2**	**0.5**	**0.4**	**0.4**	**0.6**
Cyclically-adjusted net borrowing (per cent of GDP)							
Budget 2002[2]	0.2	0.9	1.2	1.2	1.4	1.4	–
PBR 2002	0.2	1.2	1.5	1.3	1.5	1.5	1.5
Budget 2003	**0.1**	**1.7**	**1.5**	**1.5**	**1.7**	**1.7**	**1.6**

[1] *The 2002-03 figures were projections in Budget 2002 and PBR 2002.*

[2] *The 2001-02 figures were estimates in Budget 2002.*

C15 In the Pre-Budget Report, receipts for 2002-03 were revised down significantly – mainly as a result of the effects of the global economic downturn. An explanation of the impact of the slowdown on different taxes was included in the Pre-Budget Report.

C16 As explained in Chapter B, the short-term outlook for the world economy has weakened further since the Pre-Budget Report. This has had important implications for the fiscal projections. Table C2 shows that, since the Pre-Budget Report, the current budget has been revised down from a deficit of £5.7 billion to a deficit of £11.7 billion in 2002-03, including provision of £3 billion to meet the cost of the war in Iraq, and from a deficit of £5 billion to a deficit of £8 billion in 2003-04. It also shows that net borrowing has been revised up since the Pre-Budget Report, from £20.1 billion to £24 billion in 2002-03 and from £24 billion to £27 billion in 2003-04. However, the tough decisions on taxation and spending taken by the Government over the course of the last Parliament to reduce debt to low and stable levels, means that even after these revisions, the Government remains on track to meet its strict fiscal rules.

C17 The underlying strength of the fiscal position means that the changes in the fiscal balances in 2003-04 are consistent with the Government's aim of allowing the automatic stabilisers to support monetary policy in maintaining economic stability while the economy is below trend. This interaction between the economic cycle and the public sector finances also explains why there is little difference between the cyclically-adjusted balances in 2003-04 from the Pre-Budget Report projections.

FORECAST DIFFERENCES AND RISKS

C18 The fiscal balances represent the difference between two large aggregates of expenditure and receipts, and forecasts are inevitably subject to wide margins of uncertainty. Over the past ten years, the average absolute difference between year-ahead forecasts of net borrowing and subsequent outturns has been around 1 per cent of GDP. This difference tends to grow as the forecast horizon lengthens. A full account of differences between the projections made in Budget 2000 and Budget 2001 and the subsequent outturns is provided in the *End of year fiscal report*, which was published alongside the Pre-Budget Report.

C19 There are both upside and downside risks to the economic outlook. On the upside, the various uncertainties currently affecting the global economy could dissipate more quickly, and confidence recover more sharply, than anticipated. This would, in turn, help support a stronger than expected improvement in UK economic prospects.

C20 A period of prolonged uncertainty, accompanied by continued volatility in financial markets, weaker equity prices and higher oil prices poses the clearest downside risk to G7 activity. The Government will remain vigilant in the face of these risks. The public finance projections will continue to be based on cautious assumptions, including those for equity prices and the trend rate of growth, and to be 'stress tested' against the cautious case, described in paragraph C23, which builds in a margin for safety in the public finances. The Government remains on track to meet its strict fiscal rules over the economic cycle, including in the cautious case.

C21 Short-term forecasts of the public finances are critically dependent on the path of the economy, as most tax revenues and some public expenditure – notably social security – vary directly with the economic cycle. Earlier work[1] suggested that if GDP growth were one percentage point higher or lower than assumed over the coming year, net borrowing might be lower or higher by 0.4 per cent of GDP in the first year and by a further 0.3 per cent of GDP the following year. These figures are now closer to 0.5 and 0.2 per cent respectively, as the introduction of the corporation tax instalment system has reduced the lag between profits and tax receipts. However, not all cycles will conform exactly to these parameters, notably

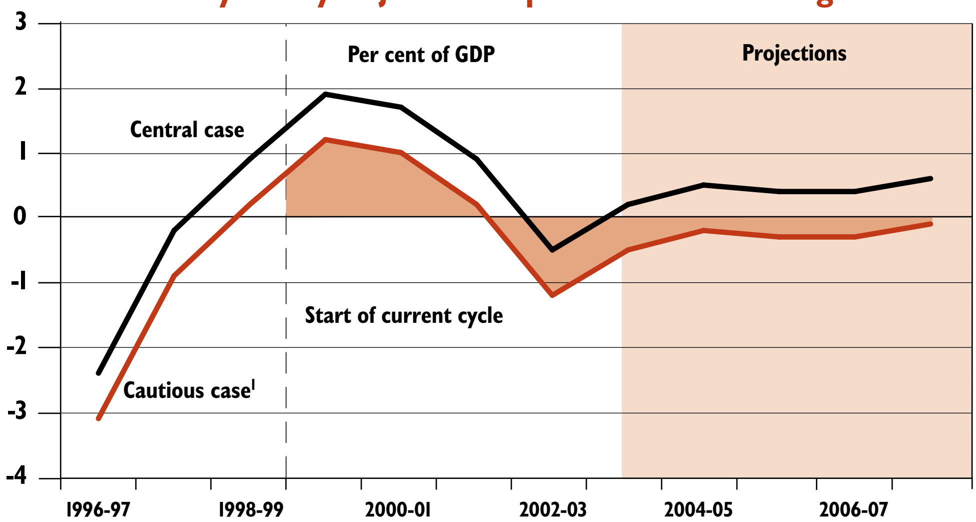
[1] *Fiscal policy: public finances and the cycle*, HM Treasury, March 1999.

because the estimates are based on historical data (since which time both the state of the economy and the tax regime have changed) and because cycles differ in respects other than magnitude.

C22 Projected differences in short-term growth forecasts may have only a temporary effect on the public finances. For a given path of trend output, higher or lower growth in the short term will be followed by lower or higher growth later on, and the public finances may be little affected on average over the cycle.

C23 However, changes in the estimated cyclical position of the economy in relation to its trend – the output gap – will have a permanent effect on prospects. For this reason, the public finances projections are 'stress tested' against an alternative cautious case, in which the level of trend output is assumed to be 1 percentage point lower than the Government's central view. This scenario would imply that a greater proportion of any projected surplus on the current budget was due to the cyclical strength of the economy – a 1 per cent larger positive output gap reduces the structural surplus on the current budget by about 0.7 per cent of GDP per year. This is illustrated in Chart C2. Even in this cautious case, the cyclically-adjusted current budget is estimated to have been comfortably in surplus over the past four years. The impact of the temporary fall in receipts means that it is projected to move into a modest deficit over the short term, before returning towards balance by the end of the projection period. The average cyclically-adjusted current budget is in surplus in the cautious case over the economic cycle, meeting the 'stress test' of the golden rule.

Chart C2: Cyclically-adjusted surplus on current budget



[1] *Cautious case assumes trend output one percentage point lower in relation to actual output than in the central case.*

ASSUMPTIONS

C24 The fiscal projections are based on the following assumptions:

- the economy follows the path described in Chapter B. In the interests of caution, the fiscal projections continue to be based on the deliberately prudent and cautious assumption of trend output growth of 2½ per cent a year up to 2006-07, ¼ percentage point lower than the Government's neutral view. Beyond 2006-07, projections by the Government Actuary imply a slowdown in the growth in the population of working age, due to demographic effects. The Government's neutral view of trend output growth is reduced to 2½ per cent in 2007-08, and so, to maintain a cautious approach, an assumption of 2¼ per cent is used in the public finance projections in that year, still ¼ percentage point lower than the Government's neutral view;

- there are no tax changes beyond those announced in or before this Budget and the indexation of rates and allowances. Consistent with the *Code for fiscal stability*, the forecast does not take account of measures that cannot be costed accurately, including the Graduate Contributions scheme, described further in Chapter 3;

- firm Departmental Expenditure Limits (DEL) as set out in the 2002 Spending Review up to 2005-06, but adjusted for the impact of policy decisions and DEL/AME reclassifications;

- Annually Managed Expenditure (AME) programmes through to 2005-06 have been reviewed and further additions made for new spending measures announced in this Budget. Following usual practice, the Government has decided to reset the AME margin to £1 billion in 2003-04, £2 billion in 2004-05 and £3 billion in 2005-06;

- prior to spending plans being set in the next Spending Review, assumed real growth in DEL after 2005-06 is in line with the economic growth assumption used for the public finances, supplemented by an addition to allow for the five-year health settlement of the difference between planned health growth and health's long-term average growth of 3.6 per cent. Other current spending in AME is forecast to grow from 2005-06 onwards at 1¾ per cent in real terms in line with its recent trend; and

- within these aggregates, net investment is forecast to increase from 2 per cent of GDP in 2005-06 towards an assumption of 2¼ per cent in 2007-08, while remaining consistent with the sustainable investment rule.

Table C3: Economic assumptions for the public finance projections

	Percentage changes on previous year						
	Outturn	Estimate	Projections				
	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Output (GDP)	1¾	2	2¼	3¼	3	2½	2¼
Prices							
RPIX	2¼	2¼	3	2½	2½	2½	2½
GDP deflator	2½	3	2¾	2½	2½	2½	2½
RPI[1] (September)	1¾	1½	2¾	2¾	3	2½	2½
Rossi[2] (September)	1¾	1¼	2	2¼	2	2	2
Money GDP[3] (£ billion)	1005	1056	1108	1173	1239	1301	1363

[1] *Used for revalorising excise duties in current year and uprating income tax allowances and bands and certain social security benefits in the following year.*

[2] *RPI excluding housing costs, used for uprating certain social security benefits.*

[3] *Not seasonally adjusted.*

C25 The key assumptions underlying the fiscal projections are audited by the National Audit Office (NAO) under the three-year rolling review process. Details of the audited assumptions are given in Box C1. The rolling review for Budget 2003[2] covers the assumptions relating to privatisation proceeds, interest rates and tobacco anti-smuggling measures. In addition, the Comptroller and Auditor General was asked to examine a change to the assumption dealing with tobacco revenues, and the revenue impact of a new direct taxation and national insurance contributions compliance and enforcement package.

C26 The Comptroller and Auditor General concluded that the privatisation proceeds assumption was reasonable and not incautious in operation, and that it remains a reasonable and cautious one to use for the purposes of projecting the public finances. Similarly, he concluded that the convention for interest rates was reasonable and cautious over the rolling review period. For the tobacco assumption, he concluded that the fiscal projections over the rolling review period were cautious as tobacco revenues have been greater than forecast.

The new tobacco assumption

C27 The tobacco assumption used in previous forecasts was developed at a time when cigarette smuggling was increasing and all the indications were that, with no action, this trend would continue. At the time it was not clear what the impact of the tobacco strategy would be in mitigating the trend because many of the elements were untried in a UK context. For this reason, a cautious assumption was adopted which involved for forecasting purposes:

- taking as a base a hypothetical assumed rise in smuggling in the absence of a strategy; and
- subtracting from this only the more certain of the expected impacts of the strategy.

[2] *Audit of Assumptions for Budget 2003*, 9 April 2003.

C28 The situation in 2003 is different. The strategy has now been in place for three years. After a long period of decline, UK duty paid consumption has recently stablised. The growth in smuggling has been halted and recent data suggests it is now in decline. In light of this evidence, the NAO audited a revised tobacco assumption for the Pre-Budget Report[3]. However, the Government considers that continued application of this assumption would still result in unduly pessimistic projections of revenue from tobacco duties. In particular, it would result in significant increases in the projected smuggled share of the cigarette market, from 21 per cent in 2001-02 to 28 per cent by 2005-06, despite HM Customs and Excise's target to reduce the share to 17 per cent.

C29 In addition, continuing with the existing assumption would mean that the future change in the smuggling share would continue to be driven by the assumed change in the share in the absence of an anti-smuggling strategy at all. As time passes it becomes much more difficult and less relevant to assess what would have happened without the strategy, making this approach increasingly unsatisfactory.

C30 As a result of these recent trends in smuggling and the success of HM Customs and Excise's strategy, a new assumption has been adopted for Budget 2003, under which the underlying market share of smuggled cigarettes will be set at least equal to the latest published outturn, which currently stands at 21 per cent. The new assumption is intended to be more closely aligned with observed trends in the smuggled market share and HM Customs and Excise's targets to reduce it. The Comptroller and Auditor General has audited the new assumption and concluded that it currently represents a reasonable approach and is cautious to the extent that no account is taken of expected further reductions in the smuggled market share. The impact of applying this new assumption on the projections of tobacco receipts is an extra £¾ billion a year by 2005-06 and £1¼ billion a year by 2007-08.

Inland Revenue compliance and enforcement package

C31 As described in Chapter 5, Budget 2003 launches a new compliance and enforcement package for direct tax and national insurance contributions. An additional £66 million is being provided to the Inland Revenue over the next three years to support implementation of the package. The package is expected to produce £1.6 billion in total additional revenue over the next 3 years, but in line with the Government's cautious approach to the public finances a lower figure of under £1.4 billion over three years with the annual figure rising to just over £0.6 billion in 2005-06 has been included in the forecast. The Comptroller and Auditor General has audited the projections and concluded that they are based on a reasonable approach and incorporate caution.

[3] *Audit of Assumptions for the 2002 Pre-Budget Report*, National Audit Office, 27 November 2002.

Box C1: Key assumptions audited by the NAO

• Privatisation proceeds[1,6,11]	Credit is taken only for proceeds from sales that have been announced.
• Trend GDP growth[1,6,9]	$2\frac{1}{2}$ per cent a year to 2006-07 and $2\frac{1}{4}$ per cent in 2007-08.
• UK claimant unemployment[1,4,7,9]	Rising slowly to 1.03 million in 2005-06, from recent levels of 0.93 million, consistent with the average of independent forecasts.
• Interest rates[1,6,7,11]	3-month market rates change in line with market expectations (as of 28 March).
• Equity prices[2,7]	FTSE All-Share index rises from 1778 (close 28 March) in line with money GDP.
• VAT[2,7,10]	Ratio of underlying VAT to consumption falls by 0.05 percentage points a year.
• GDP deflator and RPI[2,7]	Projections of price indices used to plan public expenditure are consistent with RPIX.
• Composition of GDP[3,8]	Shares of labour income and profits in national income are broadly constant in the medium term.
• Funding[3,8]	Funding assumptions used to project debt interest are consistent with the forecast level of government borrowing and with financing policy.
• Oil prices[5,10]	$26.6 a barrel in 2003, the average of independent forecasts, and then constant in real terms.
• Tobacco[6,10,11]	The underlying market share of smuggled cigarettes will be set at least at the latest published outturn. For Budget 2003, a share of 21 per cent has been used in all forecast years. This is in line with the most recently published outturn figure for 2001-02 and takes account of the indications from duty receipts for 2002-03 that the smuggled share in this year is likely to be lower than 21 per cent.
• Inland Revenue compliance and enforcement package[11]	Only direct and some preventive effects are allowed for.

[1] Audit of Assumptions for the July 1997 Budget Projections, 19 June 1997 (HC3693).
[2] Audit of Assumptions for the Pre-Budget Report, 25 November 1997 (HC361).
[3] Audit of Assumptions for the Budget, 19 March 1998 (HC616).
[4] Audit of the Unemployment Assumption for the March 1999 Budget Projections, 9 March 1999 (HC294).
[5] Audit of the Oil Price Assumption for the Pre-Budget Report, November 1999 (HC873).
[6] Audit of Assumptions for the March 2000 Budget, 21 March 2000 (HC348).
[7] Audit of Assumptions for the Pre-Budget 2000 Report, 8 November 2000 (HC959).
[8] Audit of Assumptions for the March 2001 Budget, 7 March 2001 (HC304).
[9] Audit of Assumptions for the April 2002 Budget, 17 April 2002 (HC760).
[10] Audit of Assumptions for the 2002 Pre-Budget Report, 27 November 2002 (HC109).
[11] Audit of Assumptions for Budget 2003, 9 April 2003 (HC627).

FISCAL AGGREGATES

C32 Tables C4 and C5 provide more detail on the projections for the current and capital budgets.

Table C4: Current and capital budgets

	£ billion						
	Outturn	Estimate	Projections				
	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Current budget							
Current receipts	389.9	397.1	428	460	493	522	550
Current expenditure	366.6	395.0	422	447	475	500	524
Depreciation	13.4	13.8	14	15	16	17	18
Surplus on current budget	**9.9**	**–11.7**	**–8**	**–1**	**2**	**6**	**9**
Capital budget							
Gross investment	27.3	30.5	37	42	45	48	52
Less asset sales	–4.3	–4.5	–4	–4	–4	–4	–4
Less depreciation	–13.4	–13.8	–14	–15	–16	–17	–18
Net investment	9.6	12.2	19	23	25	27	31
Net borrowing	**–0.4**	**24.0**	**27**	**24**	**23**	**22**	**22**
Public sector net debt – end year	**311.4**	**333.8**	**367**	**394**	**421**	**446**	**472**
Memos:							
Treaty deficit[1]	–0.4	24.0	27	24	24	23	24
Treaty debt[2]	381.1	401.1	433	462	491	519	547

[1] *General government net borrowing on a Maastricht basis.*
[2] *General government gross debt.*

C33 The current budget surplus is equal to public sector receipts minus public sector current expenditure and depreciation. The current budget is expected to show deficits from 2002-03 before returning to surplus in 2005-06 and remaining in surplus throughout the rest of the projection period. These temporary deficits are consistent with allowing the automatic stabilisers to operate fully over the economic cycle, while continuing to meet the golden rule.

C34 Underlying the projections of the current budget are steady increases in the ratios of public sector receipts and current expenditure to GDP, shown in Table C5, largely reflecting measures announced in Budget 2002 and the 2002 Spending Review. By 2005-06, when the current cycle ends under the assumptions used in these projections, the accumulated total surplus over this economic cycle will be £32 billion.

C35 Table C4 also shows that net investment is projected to more than double, from £12.2 billion in 2002-03 to £31 billion in 2007-08, as the Government seeks to rectify historical under-investment in public infrastructure. These increases are sustainable and fully consistent with the Government's long-term approach and the fiscal rules, as debt is being held at less than 34 per cent of GDP throughout the projection period, well within the 40 per cent limit set by the sustainable investment rule, as shown in Table C5.

Table C5: Current and capital budgets

	Per cent of GDP						
	Outturn	Estimate	Projections				
	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Current budget							
Current receipts	38.8	37.6	38.6	39.2	39.8	40.1	40.4
Current expenditure	36.5	37.4	38.1	38.1	38.4	38.4	38.5
Depreciation	1.3	1.3	1.3	1.3	1.3	1.3	1.3
Surplus on current budget	**1.0**	**–1.1**	**–0.8**	**–0.1**	**0.2**	**0.4**	**0.6**
Capital budget							
Gross investment	2.7	2.9	3.3	3.6	3.6	3.7	3.8
Less asset sales	–0.4	–0.4	–0.3	–0.3	–0.3	–0.3	–0.3
Less depreciation	–1.3	–1.3	–1.3	–1.3	–1.3	–1.3	–1.3
Net investment	1.0	1.2	1.7	2.0	2.1	2.1	2.2
Net borrowing	**0.0**	**2.3**	**2.5**	**2.1**	**1.9**	**1.7**	**1.6**
Public sector net debt – end year	**30.2**	**30.9**	**32.2**	**32.7**	**33.2**	**33.5**	**33.8**
Memos:							
Treaty deficit[1]	0.0	2.3	2.4	2.1	1.9	1.7	1.7
Treaty debt ratio[2]	37.9	38.0	39.0	39.4	39.6	39.9	40.1

[1] *General government net borrowing on a Maastricht basis.*
[2] *General government gross debt.*

RECEIPTS

C36 This section looks in detail at the projections for public sector tax receipts. It begins by looking at the main determinants of changes in the overall projections since the Pre-Budget Report, before looking in detail at changes in the projections of individual tax receipts. Finally, it provides updated forecasts for the tax-GDP ratios.

Changes in total receipts since the Pre-Budget Report

C37 Table C6 provides a detailed breakdown of the main factors that have led to changes in the overall projections since the Pre-Budget Report.

Table C6: Changes in current receipts since the 2002 Pre-Budget Report

	£ billion					
	Estimate	Projections				
	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Effect on receipts of changes in:						
Assumptions audited by the NAO	–0.1	1	1	1	2	2
of which:						
Equity price assumption	*0.0*	*0*	*–1*	*–1*	*–1*	*–1*
Tobacco assumption	*0.0*	*0*	*1*	*1*	*1*	*1*
Inland Revenue compliance and enforcement package	*0.0*	*0*	*1*	*1*	*1*	*1*
Financial company profits	0.0	–1	–1	0	0	0
Other economic determinants	–0.8	–1	–2	–1	–1	0
Other	–1.8	–1	–1	–1	0	0
Total before policy changes	–2.7	–2	–3	0	0	1
Discretionary changes since PBR 2002	0.0	0	0	1	1	1
Total change	**–2.7**	**–2**	**–2**	**1**	**1**	**2**

C38 Changes to tax determinants that are projected using assumptions audited by the NAO add around £2 billion per year to current receipts by the end of the projection period, compared with the Pre-Budget Report. As described in paragraphs C27 to C31, this is mainly the result of the new assumption regarding the level of tobacco smuggling, and the Inland Revenue compliance and enforcement package.

C39 The revenue impacts of these new assumptions are partly offset by changes in equity prices since the Pre-Budget Report, which reduce receipts by around £½ billion from 2003-04 onwards. Under the audited assumption, equity prices increase in line with money GDP from the existing level of the FTSE All-Share Index, 1778 in these projections compared with the Pre-Budget Report starting point of 1963, a fall of 9 per cent. The impact on receipts of the recent stock market increases over the past week have therefore not been incorporated into the forecast published today.

C40 Also included in the audited assumptions line is the impact of changes in the oil price forecast. The audited oil price assumption is based on the average of independent forecasts for 2003 ($26.6), as this is lower than the high average levels seen over the last three months, which partially reflected uncertainty over events in the Middle East. This is $1½ a barrel higher than assumed in the Pre-Budget Report and leads to slightly higher tax revenues.

C41 As set out in Chapter B, growth in real GDP is expected to be lower in 2003 and this, coupled with recent changes in the composition of GDP in particular lower wages and salaries, has adverse effects on tax receipts in 2003-04 and 2004-05. In later years, the impacts are much smaller as the economy moves back to trend.

C42 The remaining change to current receipts in 2002-03 is explained by other factors. In particular, lower than expected taxes on income and wealth, and stamp duties. From 2003-04 onwards, these impacts are partly offset by higher forecasts of business rates receipts, and lower income tax tax credits, although the latter has little impact on the overall fiscal balances as they are largely matched by increases in the public expenditure element of the tax credits, and by higher council tax receipts, which reflect the convention of forward projections based on the average of recent years' council tax increases.

Tax-by-tax analysis

C43 Table C7 shows the changes to the projections of individual taxes since Budget 2002 and the Pre-Budget Report for 2002-03 and 2003-04. Table C8 contains updated projections for the main components of public sector receipts for 2001-02, 2002-03 and 2003-04.

Table C7: Changes in current receipts by tax since Budget 2002 and the 2002 Pre-Budget Report

	£ billion			
	Budget 2002		PBR 2002	
	2002-03	2003-04	2002-03	2003-04
Income tax (gross of tax credits)	–4.2	–3.9	–0.8	–0.9
Non-North Sea corporation tax[1]	–3.7	–5.8	0.1	0.0
Less tax credits[2]	0.6	–1.7	0.1	0.4
North Sea revenues	–0.4	–1.0	0.1	0.2
Capital taxes[3]	–0.1	–0.6	–0.3	–0.4
Stamp duty	–0.6	–0.8	–0.6	–0.7
Value added tax	–0.3	0.0	–0.9	–0.7
Excise duties[4]	–0.6	–0.8	–0.3	0.1
Social security contributions	–0.6	–0.3	–1.2	–1.0
Other taxes and royalties[5]	0.9	1.7	0.8	0.8
Net taxes and social security contributions	**–9.1**	**–13.2**	**–3.1**	**–2.2**
Other receipts and accounting adjustments	–1.0	0.0	0.4	0.2
Current receipts	**–10.1**	**–13.3**	**–2.7**	**–2.0**

[1] *National Accounts measure: gross of enhanced and payable tax credits.*
[2] *Includes enhanced company tax credits.*
[3] *Capital gains tax and inheritance tax.*
[4] *Fuel, alcohol and tobacco duties.*
[5] *Includes council tax and money paid into the National Lottery Distribution Fund, as well as other central government taxes.*

Table C8: Current receipts

		£ billion	
	Outturn 2001-02	Estimate 2002-03	Projection 2003-04
Inland Revenue			
Income tax (gross of tax credits)	110.2	113.3	122.1
Corporation tax[1]	32.1	29.6	30.8
Tax credits[2]	–2.3	–3.4	–4.5
Petroleum revenue tax	1.3	1.0	1.5
Capital gains tax	3.0	1.7	1.2
Inheritance tax	2.4	2.4	2.4
Stamp duties	7.0	7.6	7.9
Social security contributions	63.2	64.3	74.5
Total Inland Revenue (net of tax credits)	**216.9**	**216.5**	**235.8**
Customs and Excise			
Value added tax	61.0	63.6	66.6
Fuel duties	21.9	22.1	23.0
Tobacco duties	7.8	8.1	8.0
Spirits duties	1.9	2.3	2.4
Wine duties	2.0	1.9	1.9
Beer and cider duties	3.1	3.1	3.1
Betting and gaming duties	1.4	1.3	1.3
Air passenger duty	0.8	0.8	0.8
Insurance premium tax	1.9	2.1	2.2
Landfill tax	0.5	0.5	0.7
Climate change levy	0.6	0.8	0.9
Aggregates levy	0.0	0.2	0.3
Customs duties and levies	2.0	1.9	1.9
Total Customs and Excise	**104.9**	**108.8**	**113.1**
Vehicle excise duties	4.2	4.6	4.8
Oil royalties	0.5	0.5	0.0
Business rates[3]	18.0	18.7	18.6
Council tax	15.3	16.6	18.6
Other taxes and royalties[4]	9.9	10.8	11.9
Net taxes and social security contributions[5]	**369.7**	**376.5**	**402.9**
Accruals adjustments on taxes	0.6	–0.3	3.6
Less own resources contribution to European Communities (EC) budget	–3.6	–2.5	–2.5
Less PC corporation tax payments	–0.1	–0.1	–0.1
Tax credits[6]	0.9	1.1	0.6
Interest and dividends	4.5	4.1	4.0
Other receipts[7]	17.9	18.2	19.8
Current receipts	**389.9**	**397.1**	**428.3**
Memo:			
North Sea revenues[8]	5.2	5.0	4.7

[1] *National Accounts measure: gross of enhanced and payable tax credits.*
[2] *Includes enhanced company tax credits.*
[3] *Includes district council rates in Northern Ireland paid by business.*
[4] *Includes money paid into the National Lottery Distribution Fund.*
[5] *Includes VAT and 'traditional own resources' contributions to EC budget. Cash basis.*
[6] *Excludes Children's Tax Credit and other tax credits that score as a tax repayment in the National Accounts.*
[7] *Includes gross operating surplus and rent; net of oil royalties.*
[8] *Consists of North Sea corporation tax, petroleum revenue tax and royalties.*

Income tax **C44** Income tax receipts in 2002-03 are expected to be around £0.8 billion lower than forecast in the Pre-Budget Report. Much of this is the result of downward revisions to wages and salaries in the current financial year reflecting lower growth in private sector average earnings. In addition, self assessment tax receipts due at the end of January, which relate to tax liabilities in 2001-02, were also lower than expected. Full details on the shortfall will not be available until later in the year, however, early indications are that it may partly reflect lower than expected income from dividend payments.

C45 Income tax receipts in 2003-04 have been revised down by similar amounts, although this revision is also due to lower tax revenues from interest receipts as a result of the lower interest rate forecast that is audited by the NAO. As a result of these developments, income tax as a per cent of GDP is slightly lower than in the Pre-Budget Report projection in every year.

Non-North Sea corporation tax **C46** Non-North Sea corporation tax receipts in 2002-03 are estimated to be around £26 billion, slightly higher than the Pre-Budget Report projection. After 2002-03 there have been a number of changes to the determinants of Non-North Sea corporation tax. Profits of non-financial companies have been revised downwards slightly in 2003-04 and 2004-05, but then recover. The lower equity price assumption has a negative impact on projected corporation tax on gains. Financial companies' profits are assumed to recover more slowly than was the case in the Pre-Budget Report, reflecting the ongoing uncertainty in financial markets, but to rise to similar levels by 2005. The overall forecast for corporation tax as a per cent of GDP is broadly as published in the Pre-Budget Report.

Tax credits **C47** The tables in this section show the amounts of tax credits classified as negative tax in line with OECD Revenue Statistics guidelines. The public expenditure amounts are included in Table C11. In the Pre-Budget Report, the estimated split of total tax credits between that scored as tax and that scored as public expenditure was revised, with the negative tax element about £2 billion a year higher from 2003-04 onwards. These revisions were balanced by changes in the public expenditure element of tax credits, such that there was no overall impact on the fiscal balances. Further revisions to this split account for much of the changes in Budget 2003.

North Sea revenues **C48** North Sea revenues in 2002-03 are estimated to be £5 billion, broadly in line with the Pre-Budget Report projection. In 2003-04, the Budget projection is £0.2 billion higher than was anticipated at the time of the Pre-Budget Report and there are slightly larger increases in subsequent years. Higher oil prices explain most of these increases. The oil price assumed in these projections is based on the average of independent forecasts for 2003, which is $26.6 per barrel, compared with $25.1 per barrel in the Pre-Budget Report.

Capital taxes **C49** Receipts from capital taxes in 2002-03 are expected to be around £0.3 billion lower than projected in the Pre-Budget Report, largely as a result of lower capital gains taxes. These receipts relate to gains realised in 2001-02, and are therefore not a result of recent movements in asset prices. Information on the tax liability underlying the gains realised in 2002-03 will become available in 2004.

C50 The reduction in the capital taxes forecast from 2003-04 onwards is largely explained by the reduction in the equity price forecast, along with new information on the composition of assets liable for inheritance tax.

Stamp duty

C51 Stamp duty receipts in 2002-03 are estimated to be around £0.6 billion lower than forecast in the Pre-Budget Report, as a result of lower revenues from land and property transactions. This partly reflects lower than expected volumes of residential transactions and prices. Downward revisions to the projected levels of these tax determinants, along with lower forecasts for commercial prices explain most of the downward revisions to revenues in future years.

C52 Although equity prices were lower than expected at the time of the Pre-Budget Report in 2002-03, higher trading volumes have meant that revenues from stamp duty on shares are broadly in line with expectations. This pattern is expected to continue throughout the projection period.

Social security contributions

C53 Receipts from social security contributions in 2002-03 are expected to be around £1.2 billion lower than projected in the Pre-Budget Report. This is partly a result of lower wages and salaries, but also because personal pension rebates have been higher than expected. These two factors also explain much of the revision in 2003-04. Measured as a per cent of GDP, receipts remain slightly below their Pre-Budget Report levels in later years.

VAT receipts

C54 VAT receipts in 2002-03 are estimated to have been £63.6 billion, around £0.9 billion lower than projected in the Pre-Budget Report. This is largely because of lower than expected receipts in recent months. The forecast of VAT revenues from 2003-04 onwards continues to be governed by an assumption that is audited by the NAO, which stipulates that the ratio of VAT to consumers' expenditure should decline gradually, by 0.05 percentage points a year, after the effects of VAT policy decisions are taken into account. Therefore, the shortfall in 2002-03 automatically depresses receipts in future years. However, this is partly offset by the Budget forecast of higher consumers' expenditure growth from 2003-04 onwards and the VAT measures described in Chapter A. Therefore, VAT receipts are expected to be around £0.7 billion a year lower than their Pre-Budget Report levels from 2003-04 onwards.

Excise duties

C55 Excise duties in 2002-03 are estimated to be around £0.3 billion lower than forecast in the Pre-Budget Report, and around £0.1 billion higher in 2003-04. Fuel duty receipts were around £0.2 billion lower than forecast in the Pre-Budget Report in 2002-03. This is mainly because the later than usual date of the Budget means that the additional receipts associated with the forestalling of road fuel duties will now be received in the early part of 2003-04. This timing issue decreases receipts in 2002-03 by around £0.2 billion with an offsetting increase in 2003-04. This increase in 2003-04 is offset by the fuel duty measure described in Chapter A, and higher oil prices that are assumed to increase pump prices and decrease demand. Alcohol duty receipts are broadly as forecast in the Pre-Budget Report.

C56 Tobacco duty receipts in 2002-03 are slightly lower than projected in the Pre-Budget Report as a result of downward revisions to the level of overall consumption. However, from 2003-04 onwards, receipts are expected to be higher than in the Pre-Budget Report. This is the result of the revised assumption regarding the levels of tobacco smuggling discussed in paragraphs C27 to C30, which has been audited by the NAO to ensure that it remains reasonable and cautious.

Other receipts

C57 Receipts from business rates in 2002-03 are estimated to be £0.7 billion higher than forecast in the Pre-Budget Report. This reflects new information on in year receipts. Other receipts in 2003-04 have also been revised up by similar amounts, largely as a result of higher council tax receipts, which reflect the convention of forward projections based on the average of recent years' council tax increases.

Tax-GDP ratio

C58 Table C9 shows projections of receipts from major taxes as a per cent of GDP, and Table C10 sets out current and previous projections of the overall tax-GDP ratio.

Table C9: Current receipts as a proportion of GDP

	Per cent of GDP						
	Outturn	Estimate			Projections		
	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Income tax (gross of tax credits)	11.0	10.7	11.0	11.2	11.4	11.6	11.7
Non-North Sea corporation tax[1]	2.9	2.5	2.5	2.9	3.2	3.3	3.4
Tax credits[2]	–0.2	–0.3	–0.4	–0.4	–0.4	–0.4	–0.3
North Sea revenues[3]	0.5	0.5	0.4	0.4	0.4	0.4	0.4
Value added tax	6.1	6.0	6.0	6.0	6.0	5.9	5.9
Excise duties[4]	3.6	3.5	3.5	3.4	3.3	3.2	3.2
Social security contributions	6.3	6.1	6.7	6.9	6.8	6.9	6.9
Other taxes and royalties[5]	6.7	6.6	6.6	6.7	6.8	6.9	7.0
Net taxes and social security contributions[6]	**36.8**	**35.6**	**36.3**	**37.1**	**37.6**	**37.9**	**38.2**
Accruals adjustments on taxes	0.1	0.0	0.3	0.2	0.2	0.1	0.2
Less EC transfers	–0.4	–0.2	–0.2	–0.2	–0.2	–0.1	–0.1
Tax credits[7]	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Other receipts[8]	2.2	2.1	2.1	2.1	2.1	2.1	2.1
Current receipts	**38.8**	**37.6**	**38.6**	**39.2**	**39.8**	**40.1**	**40.4**
Memo:							
Current receipts (£ billion)	389.9	397.1	428	460	493	522	550

[1] *National Accounts measure: gross of enhanced and payable tax credits.*
[2] *Tax credits scored as negative taxation in net taxes and social security contributions.*
[3] *Includes oil royalties, petroleum revenue tax and North Sea corporation tax.*
[4] *Fuel, alcohol and tobacco duties.*
[5] *Includes council tax and money paid into the National Lottery Distribution Fund, as well as other central government taxes.*
[6] *Includes VAT and 'own resources' contributions to EC budget. Cash basis.*
[7] *Tax credits scored as negative taxation in net taxes and social security contributions but as expenditure in the National Accounts.*
[8] *Mainly gross operating surplus and rent, excluding oil royalties.*

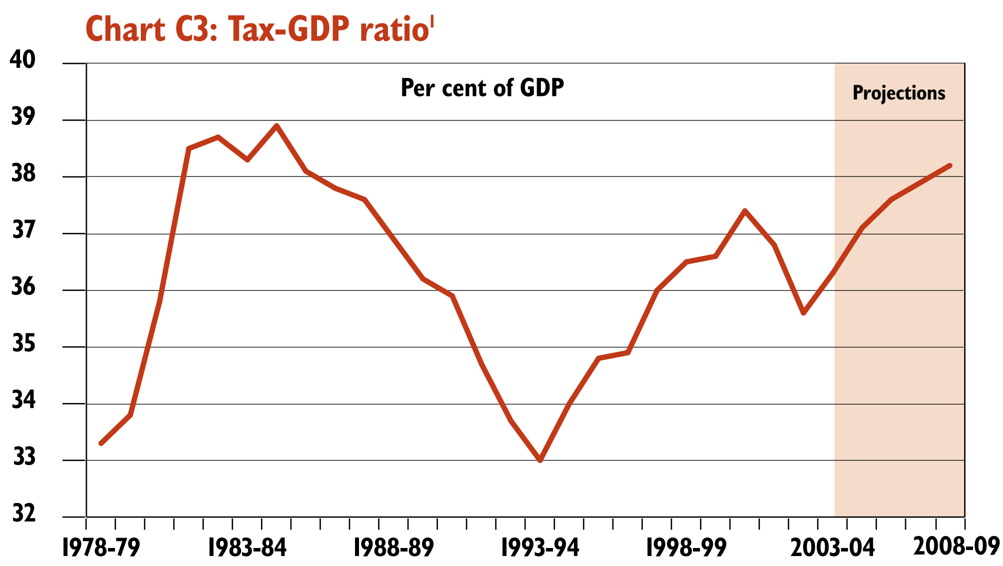
Table C10: Net taxes and social security contributions[1]

	Per cent of GDP						
	Outturn[2]	Estimate[3]			Projections		
	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Budget 2002	37.0	36.7	37.6	38.1	38.3	38.3	–
PBR 2002	37.1	36.3	37.0	37.7	38.2	38.4	38.6
Budget 2003	**36.8**	**35.6**	**36.3**	**37.1**	**37.6**	**37.9**	**38.2**

[1] *Cash basis. Uses OECD definition of negative tax personal tax credits. Net of enhanced company tax credits.*
[2] *The 2001-02 figures were estimates in Budget 2002.*
[3] *The 2002-03 figures were projections in Budget 2002 and PBR 2002.*

C59 Table C10 shows that the tax-GDP ratio is now expected to fall to 35.6 per cent of GDP in 2002-03, compared with the Pre-Budget Report projection of 36.3 per cent and the Budget 2002 projection of 36.7 per cent. Similarly, the tax-GDP ratio is expected to be well below the Pre-Budget Report and Budget 2002 projections throughout the projection period.

C60 Chart C3 shows the tax-GDP ratio from 1978-79 to 2007-08.



[1] *Net taxes and social security contributions as defined in Table C10.*

PUBLIC EXPENDITURE

C61 Table C11 shows projections for public expenditure up to 2005-06, the last year covered by the 2002 Spending Review. The projections cover the whole of the public sector, using the National Accounts aggregate Total Managed Expenditure (TME). TME is split into Departmental Expenditure Limits (DEL) – firm three year limits for departments' programme expenditure – and Annually Managed Expenditure (AME) – expenditure that is not easily subject to firm multi-year limits.

Table C11: Total Managed Expenditure 2001-02 to 2005-06

			£ billion		
	Outturn	Estimate		Projections	
	2001-02	2002-03	2003-04	2004-05	2005-06
Departmental Expenditure Limits					
Resource Budget	215.8	241.6	249.1	263.8	283.5
Capital Budget	18.0	20.7	25.1	26.8	29.1
Less depreciation	–9.6	–18.3	–10.4	–11.1	–11.8
Total Departmental Expenditure Limits	**224.1**	**244.0**	**263.8**	**279.5**	**300.7**
Annually Managed Expenditure					
Social security benefits[1]	101.1	105.5	111.0	116.7	121.9
Tax credits[1]	8.7	9.8	11.7	12.1	12.5
Housing Revenue Account subsidies	4.5	4.3	4.3	4.0	4.1
Common Agricultural Policy	3.7	2.6	2.3	2.3	2.3
Net public service pensions[2]	10.1	3.5	0.2	0.1	–0.1
National Lottery	1.7	1.9	2.2	1.9	1.5
Non-cash items in AME	23.4	27.9	25.2	26.4	27.5
Other departmental expenditure	0.2	2.3	2.2	1.8	1.9
Net payments to EC institutions[3]	0.8	2.3	2.3	3.0	3.4
Locally financed expenditure	19.8	20.7	23.0	24.6	26.1
Central government gross debt interest	22.1	20.8	21.8	23.2	24.3
Public corporations' own-financed capital expenditure	1.5	2.2	2.6	2.7	2.7
Total AME before margin and accounting adjustments	**197.7**	**203.8**	**208.9**	**218.9**	**228.2**
AME margin	0.0	0.0	1.0	2.0	3.0
Accounting adjustments[4]	–32.2	–26.7	–18.0	–15.7	–15.4
Annually Managed Expenditure	**165.5**	**177.0**	**191.9**	**205.2**	**215.8**
Total Managed Expenditure	**389.6**	**421.0**	**455.7**	**484.7**	**516.5**
of which:					
Public sector current expenditure	366.6	395.0	422.3	446.5	475.2
Public sector net investment	9.6	12.2	18.9	23.0	25.4
Public sector depreciation	13.4	13.8	14.4	15.2	15.9

[1] *For 2001-02 to 2004-05, child allowances in Income Support and Jobseekers' Allowance, which, from 2003-04, are paid as part of the Child Tax Credit, have been included in the tax credits line and excluded from the social security benefits line. This is in order to give figures on a consistent definition over the forecast period.*

[2] *Net public service pensions expenditure is reported under FRS17 accounting requirements.*

[3] *Net payments to EC institutions exclude the UK's contribution to the cost of EC aid to non-Member States (which is attributed to the aid programme).*

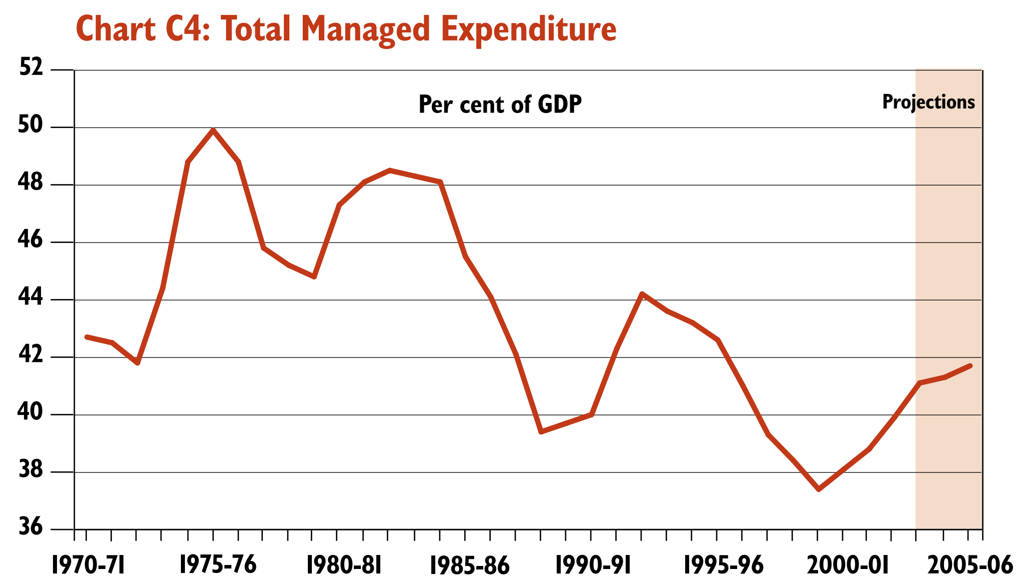
Net payments therefore differ from the UK's net contribution to the EC Budget, latest estimates for which are (in £ billion):

2001-02	2002-03	2003-04	2004-05	2005-06
1.5	3.1	3.2	3.7	4.0

The trended forecast for 2002-03 is £3.0 billion.

[4] *Excludes depreciation.*

C62 Chart C4 shows TME as a per cent of GDP from 1970-71 to 2005-06.



C63 The 2002 Spending Review was the first to be conducted on a full resource basis. Resource accounting and budgeting (RAB) replaces the previous approach of planning and controlling public expenditure on a cash basis and applies the best financial and disclosure practices of commercial accounting to central government finances. Resource budgeting was introduced in two stages, and prior to the 2002 Spending Review budgets were set on a 'near cash' basis – a hybrid of resource budgeting and the previous cash management system.

C64 From 2003-04 onwards, departmental budgets will be controlled on a full resource budgeting basis, which means that the full economic cost of departmental activity will be recognised in budgets. Table C12 shows DEL in terms of resource and capital budgets. These figures have been adjusted to reflect classification changes since the Pre-Budget Report. These include: the reduction in the cost of capital charge that, under RAB, reflects the opportunity and financing costs of capital; and changes to the discount rate applied to future liabilities, as agreed with the independent Financial Reporting Advisory Board (FRAB). Both of these changes are TME neutral.

C65 Defence estimated outturn in 2002-03 has increased by £9.5 billion since the Pre-Budget Report. The majority of this increase is a result of changes arising from the quinquennial revaluation of its asset base in line with Generally Accepted Accounting Practice, the continued implementation of the asset management plan following on from the Strategic Defence Review and recognition of future liabilities. These items are all non-cash and TME neutral. An additional allocation of £1 billion was also made from the special reserve.

Table C12: Departmental Expenditure Limits – resource and capital budgets

	£ billion				
	Outturn	Estimate		Plans	
	2001-02	2002-03	2003-04	2004-05	2005-06
Resource Budget					
Education and Skills[1]	17.0	20.6	22.0	23.7	25.6
Health[1]	52.1	57.4	63.0	68.7	74.9
of which: NHS	*50.9*	*55.1*	*60.8*	*66.5*	*72.7*
Transport	4.4	6.0	7.3	7.5	8.4
Office of the Deputy Prime Minister	2.7	4.1	4.8	5.2	5.4
Local government	36.9	37.4	41.0	44.1	48.0
Home Office	10.3	11.3	11.7	11.6	12.4
Lord Chancellor’s departments	3.1	3.3	3.1	3.4	3.5
Attorney General's departments	0.4	0.5	0.5	0.5	0.5
Defence[2]	32.3	41.4[3]	30.8	31.5	32.3
Foreign and Commonwealth Office	1.4	1.6	1.7	1.5	1.6
International Development	3.2	3.6	3.6	3.8	4.5
Trade and Industry	5.4	4.6	4.7	4.9	5.4
Environment, Food and Rural Affairs	2.7	2.7	2.7	2.7	2.8
Culture, Media and Sport	1.2	1.3	1.4	1.5	1.5
Work and Pensions	6.2	7.5	8.0	8.0	8.2
Scotland[4]	16.0	17.3	18.4	19.4	20.6
Wales[4]	8.2	9.1	9.8	10.4	11.1
Northern Ireland Executive[4]	5.7	6.2	6.4	6.7	7.1
Northern Ireland Office	1.0	1.2	1.1	1.1	1.1
Chancellor's departments	4.1	4.6	4.6	4.7	4.9
Cabinet Office	1.5	1.7	1.8	1.8	1.9
Invest to Save Budget	0.0	0.0	0.0	0.0	0.0
Capital Modernisation Fund	0.0	0.0	0.0	0.0	0.0
Reserve	0.0	0.0	0.7	1.2	1.7
Unallocated special reserve[5]	0.0	2.0	0.0	0.0	0.0
Allowance for shortfall[6]	0.0	–3.8	0.0	0.0	0.0
Total Resource Budget DEL	**215.8**	**241.6**	**249.1**	**263.8**	**283.5**
Capital Budget					
Education and Skills	2.1	2.6	3.3	3.8	4.3
Health	1.8	2.1	3.0	3.5	4.5
of which: NHS	*1.7*	*2.0*	*2.9*	*3.4*	*4.4*
Transport	2.4	3.0	3.3	3.6	3.3
Office of the Deputy Prime Minister	1.8	1.5	1.9	2.0	2.1
Local government	0.1	0.2	0.3	0.3	0.3
Home Office	0.6	0.9	1.1	1.1	1.1
Lord Chancellor's departments	0.1	0.1	0.1	0.1	0.1
Attorney General's departments	0.0	0.0	0.0	0.0	0.0
Defence	5.8	6.3	6.1	6.4	7.0
Foreign and Commonwealth Office	0.1	0.1	0.1	0.1	0.1
International Development	0.0	0.0	0.0	0.0	0.0
Trade and Industry	0.1	0.4	0.5	0.2	0.2
Environment, Food and Rural Affairs	0.3	0.4	0.3	0.3	0.3
Culture, Media and Sport	0.0	0.1	0.1	0.1	0.1
Work and Pensions	0.1	0.2	0.0	0.2	0.1
Scotland[4]	1.4	2.0	2.0	2.2	2.3
Wales[4]	0.5	0.8	0.8	0.9	1.0
Northern Ireland Executive[4]	0.4	0.6	0.4	0.5	0.5
Northern Ireland Office	0.0	0.1	0.1	0.1	0.1
Chancellor's departments	0.2	0.4	0.3	0.3	0.3
Cabinet Office	0.2	0.2	0.6	0.2	0.2
Invest to Save Budget	0.0	0.0	0.0	0.0	0.0
Capital Modernisation Fund	0.0	0.0	0.0	0.0	0.0
Reserve	0.0	0.0	0.8	0.8	1.1
Allowance for shortfall[6]	0.0	–1.2	0.0	0.0	0.0
Total Capital Budget DEL	**18.0**	**20.7**	**25.1**	**26.8**	**29.1**
Depreciation	**–9.6**	**–18.3**	**–10.4**	**–11.1**	**–11.8**
Total Departmental Expenditure Limits	**224.1**	**244.0**	**263.8**	**279.5**	**300.7**
Total education spending	49.4	53.6	58.6	62.9	68.5

[1] *From 2003-04 onwards this includes employer contributions for cost of pension increases.*
[2] *Cost of capital charge and provisions discount rate classification changes have only been applied to the Ministry of Defence figures from 2003-04 onwards.*
[3] *One-off increase in defence non-cash expenditure in line with agreed asset management policy.*
[4] *For Scotland and Wales and Northern Ireland, the split between current and capital budgets is decided by the respective executives.*
[5] *This is the remaining contingency provision for costs of military operations in Iraq after an allocation of a preliminary £1 billion to Ministry of Defence from the £3 billion total.*
[6] *In 2001-02 and 2002-03, DEL is controlled on a near-cash basis (see Table C13). The numbers have been translated onto a Stage 2 basis, for comparison purposes. They have been adjusted since PBR 2002 to take account of changes to non-cash, classification changes and other items that have no impact on total public spending. From 2003-04, DEL will be controlled fully on a Stage 2 basis.*

C66 In 2001-02 and 2002-03, departmental expenditure was controlled on a 'near cash' basis. Table C13 shows outturns and plans on this basis. Both tables have been updated since the Pre-Budget Report to reflect transfers between departments and programmes, additions and allocations from central funds and reclassifications.

C67 At the Pre-Budget Report planned DEL for 2002-03 on a 'near cash' basis was £231.4 billion. Since then £2.3 billion has been added to total planned DEL reflecting the addition to the special reserve and classification changes, giving a total planned DEL of £233.7 billion. As Table C13 shows, in 2002-03 total DEL spending remains within plans. In line with previous practice, an allowance for shortfall of £4.0 billion, representing estimates of the likely underspend beneath departmental estimates, is made.

Table C13: Departmental Expenditure Limits on a 2000 Spending Review basis – resource and capital budgets

	£ billion	
	Outturn 2001-02	Estimate 2002-03
Resource Budget		
Education and Skills	16.5	20.0
Health	48.7	54.5
of which: NHS	*47.5*	*52.3*
Transport	2.7	3.1
Office of the Deputy Prime Minister	1.3	1.8
Local government	36.9	37.4
Home Office	9.7	10.4
Lord Chancellor's departments	2.9	3.1
Attorney General's departments	0.4	0.5
Defence	18.5	20.2
Foreign and Commonwealth Office	1.3	1.4
International Development	3.2	3.4
Trade and Industry	3.5	3.8
Environment, Food and Rural Affairs	2.7	2.2
Culture, Media and Sport	1.0	1.2
Work and Pensions	6.2	7.4
Scotland[1]	14.2	16.1
Wales[1]	7.5	8.5
Northern Ireland Executive[1]	4.7	5.7
Northern Ireland Office	1.0	1.1
Chancellor's departments	3.8	4.2
Cabinet Office	1.3	1.4
Invest to Save Budget	0.0	0.0
Capital Modernisation Fund	0.0	0.0
Reserve	0.0	0.0
Unallocated special reserve[2]	0.0	2.0
Allowance for shortfall	0.0	–3.1
Total Resource Budget DEL	**188.1**	**206.3**
Capital Budget		
Education and Skills	2.5	3.2
Health	1.9	2.2
of which: NHS	*1.8*	*2.1*
Transport	4.3	5.6
Office of the Deputy Prime Minister	2.6	3.2
Local government	0.1	0.2
Home Office	0.8	1.1
Lord Chancellor's departments	0.1	0.1
Attorney General's departments	0.0	0.0
Defence	5.9	6.3
Foreign and Commonwealth Office	0.1	0.1
International Development	0.0	0.0
Trade and Industry	0.5	1.0
Environment, Food and Rural Affairs	0.5	0.6
Culture, Media and Sport	0.1	0.1
Work and Pensions	0.2	0.2
Scotland[1]	2.2	2.0
Wales[1]	0.9	1.1
Northern Ireland Executive[1]	0.5	0.5
Northern Ireland Office	0.0	0.1
Chancellor's departments	0.2	0.4
Cabinet Office	0.2	0.2
Invest to Save Budget	0.0	0.0
Capital Modernisation Fund	0.0	0.0
Reserve	0.0	0.0
Allowance for shortfall	0.0	–0.9
Total Capital Budget DEL	**23.7**	**27.3**
Total Departmental Expenditure Limits	**211.8**	**233.7**
Total education spending	49.4	53.6

[1] *For Scotland and Wales and Northern Ireland, the split between current and capital budgets is decided by the respective executives.*

[2] *This is the remaining contingency provision for costs of military operations in Iraq after an allocation of a preliminary £1 billion to the Ministry of Defence from the £3 billion total.*

C68 Table C14 shows changes in DEL and AME components since the Pre-Budget Report. It has also been updated to incorporate reclassifications including between DEL and AME as well as between current and capital DEL, and the reduction in DEL brought about by the reallocation of the Capital Modernisation Fund (CMF) and measures announced in this Budget. Net public service pensions figures are now reported on a Financial Reporting Standard 17 (FRS17) basis. This means that the measure of expenditure for this component has changed from being a cash record of flows in and out of the schemes to one that records the movements in the liability of the various pension schemes, including the accruing costs as members serve additional years. Additional non-cash costs are also now included in the non-cash items in AME line. This change is neutral on TME but does mean that meaningful comparisons between the net public service pensions, non-cash items in AME and the accounting adjustments lines shown in Table C11 and in the Pre-Budget Report cannot be made and these lines have therefore been excluded from this table.

C69 As described in Chapter 6, the Government has made a special reserve allocation of £3 billion to ensure that resources are available to cover the full cost of the UK's military obligations in Iraq, of which £1 billion has already been allocated to the Ministry of Defence budget. The full amount of the provision has been allocated to 2002-03, although it is not yet clear when these costs will fall. In the light of continuing uncertainty, and in order to protect committed investment while responding prudently to heightened global risks, the Government has decided to make no further allocations from the CMF. Instead, the unallocated CMF funding will contribute towards the rebuilding of the AME margin to ensure that the public spending projections include a prudent and cautious safety margin against unexpected events.

C70 Total DEL spending in 2002-03, net of depreciation, is now estimated to be around £2.7 billion higher than in the Pre-Budget Report. £2.2 billion of this is due to the further allocations to the special reserve of £2 billion and a £0.2 billion increase in capital DEL from reclassified PFI projects. The remainder reflects changes in non-cash items, other than depreciation, which are then removed in the AME accounting adjustments and are therefore TME neutral. DEL changes in later years are due to reclassifications and other switches between DEL and AME and between resource and capital DEL.

Table C14: Changes to Total Managed Expenditure since the 2002 Pre-Budget Report

	£ billion				
	Outturn	Estimate		Projections	
	2001-02	2002-03	2003-04	2004-05	2005-06
Departmental Expenditure Limits					
Resource Budget	2.7	11.4	–3.3	–3.2	–3.2
Capital Budget	–0.1	–0.6	–0.1	–0.8	–1.0
Less depreciation	0.0	–8.1	0.7	0.4	0.4
Total Departmental Expenditure Limits[1]	**2.6**	**2.7**	**–2.7**	**–3.7**	**–3.9**
Annually Managed Expenditure					
Social security benefits	-0.2	0.6	0.9	1.0	0.9
Tax credits	0.1	–0.2	0.0	–0.2	–0.2
Housing Revenue Account subsidies	0.0	0.0	0.1	–0.2	–0.1
Common Agricultural Policy	–0.1	0.2	0.0	–0.1	–0.2
National Lottery	0.0	–0.1	0.0	0.0	0.0
Other departmental expenditure	–0.5	0.8	1.6	0.7	1.1
Net payments to EC institutions	0.0	0.7	0.1	0.0	0.0
Locally financed expenditure	–0.4	–0.2	0.7	1.2	1.4
Central government gross debt interest	–0.1	0.1	0.3	–0.6	0.4
Public corporations' own-financed capital expenditure	–0.4	–0.4	–0.2	0.1	0.1
AME margin	0.0	–0.1	–0.8	1.5	2.5
Annually Managed Expenditure	**–4.9**	**–1.5**	**3.6**	**6.7**	**8.8**
Total Managed Expenditure	**–2.3**	**1.2**	**0.9**	**3.0**	**4.9**
of which:					
Public sector current expenditure	–3.0	3.7	1.8	2.2	3.9
Public sector net investment	0.7	–2.1	–0.7	1.1	1.3
Public sector depreciation	0.0	–0.3	–0.3	–0.3	–0.3

[1] *DEL in 2001-02 and 2002-03 is controlled on a 'near cash' basis as set out in paragraph C67.*

C71 Forecasts of individual AME programmes were reviewed in the Pre-Budget Report and have been reviewed again for this Budget. In addition, and following usual practice, the Government has decided to reset the AME margin to £1 billion in 2003-04, £2 billion in 2004-05 and £3 billion in 2005-06.

C72 The main economic assumptions underpinning AME projections are set out in Box C1 and Table C3. In particular, it is assumed that UK claimant unemployment will increase slightly, in line with the average of independent forecasts, from its recent level of 0.93 million (the average of the three months ending in March 2003) to 1.03 million in 2005-06.

C73 Higher forecasts for inflation – which affects the uprating of benefits – and claimant unemployment have increased the social security expenditure forecast since the Pre-Budget Report by around £½ billion from 2004-05. New interim population projections based on the 2001 Census have also had an upward effect of around £0.2 billion from 2004-05, largely because of an increase in the forecast growth of the pensioner population. In addition, the additional funding for pensioners and other social security payments announced in this Budget add a further £0.2 billion in the last two years.

C74 Locally financed expenditure is also higher at the end of the projection period, and reflects the convention of forward projections based on the average of recent years' council tax increases. However, this has a broadly neutral impact on the fiscal balances as it is matched by additional resources raised at the local level.

C75 With the exception of 2004-05, central government gross debt interest payments are higher than at the Pre-Budget Report. This reflects higher borrowing and higher forecasts for inflation, affecting the accrued uplift on index-linked gilts, offset by lower market expectations for interest rates. In 2004-05 the forecast for inflation is lower than at the Pre-Budget Report and this, in combination with lower interest rates, more than offsets the effects of higher borrowing.

C76 The main accounting adjustments, which consist of those items within TME but outside DEL and AME main programmes, are shown in Table C15. Accounting adjustments also reflect the impact on DEL of a fall in the cost of capital charge made to departments. This change is TME neutral and constitutes a reduction in non-cash spending in DEL and a corresponding reduction in AME of the accounting adjustment that removes non-cash spending.

Table C15: Accounting adjustments

	£ billion				
	Outturn	Estimate		Projections	
	2001-02	2002-03	2003-04	2004-05	2005-06
Removal of non-cash spending in DEL[1]	–11.2	–10.0	–6.6	–6.9	–7.3
Financial transactions in DEL	–1.6	–1.5	–1.9	–1.4	–1.4
Removal of non-cash spending in AME	–29.4	–27.1	–23.6	–24.7	–25.6
Financial transactions in AME	0.1	–0.4	–0.1	0.7	0.6
Adjustments for public corporations	3.3	3.1	3.6	3.6	3.8
Central government non-trading capital consumption	8.3	8.5	9.0	9.4	9.9
VAT refunded on general government expenditure	7.6	8.8	9.8	10.6	11.6
EC contributions	–6.1	–4.2	–4.5	–4.2	–4.1
Tax credits	0.9	1.3	0.8	0.8	0.9
Intra-general government debt interest	–3.0	–3.6	–2.5	–2.8	–2.8
Other accounting adjustments	–1.1	–1.7	–2.0	–0.7	–0.9
Total accounting adjustments	**–32.2**	**–26.7**	**–18.0**	**–15.7**	**–15.4**

[1] *Excluding depreciation in resource DEL.*

C77 Table C16 shows public sector capital expenditure from 2001-02 to 2005-06.

Table C16: Public sector capital expenditure

	£ billion				
	Outturn	Estimate		Projections	
	2001-02	2002-03	2003-04	2004-05	2005-06
Capital Budget DEL	18.0	20.7	25.1	26.8	29.1
Locally financed expenditure	1.2	1.3	1.5	1.8	1.7
National Lottery	0.9	0.9	1.2	1.1	0.8
Public corporations' own-financed capital expenditure	1.5	2.2	2.6	2.7	2.7
Other capital spending in AME	1.3	0.9	2.9	5.1	5.9
AME margin	0.0	0.0	0.1	0.8	1.1
Public sector gross investment[1]	**23.0**	**26.0**	**33.4**	**38.2**	**41.3**
Less depreciation	13.4	13.8	14.4	15.2	15.9
Public sector net investment	**9.6**	**12.2**	**18.9**	**23.0**	**25.4**
Proceeds from the sale of fixed assets[2]	4.3	4.5	3.8	3.8	3.8

[1] *This and previous lines are all net of sales of fixed assets.*

[2] *Projections of total receipts from the sale of fixed assets by public sector.*

C78 Table C17 shows estimated receipts from loans and sales of assets from 2001-02 to 2005-06. The figures for sales of financial assets include proceeds of £0.1 billion for the sale of a stake in QinetiQ (formerly the Defence Evaluation and Research Agency) in the first quarter of 2003. The total proceeds of the Public Private Partnership (PPP) will be £0.2 billion, including receipts in 2001-02 and those due in future years.

Table C17: Loans and sales of assets

	Outturn	Estimate		Projections	
£ billion	2001-02	2002-03	2003-04	2004-05	2005-06
Sales of fixed assets					
Central government	0.9	1.0	1.0	1.0	1.0
Local authorities	3.4	3.5	2.8	2.8	2.8
Total sales of fixed assets	**4.3**	**4.5**	**3.8**	**3.8**	**3.8**
Total loans and sales of financial assets	**–1.8**	**–2.6**	**–2.1**	**–1.4**	**–1.5**
Total loans and sales of assets	**2.5**	**1.9**	**1.6**	**2.4**	**2.2**

PRIVATE FINANCE INITIATIVE

C79 Under the Private Finance Initiative (PFI) the public sector purchases services from a private sector partner. In addition to requiring capital investment to be undertaken by the private sector, the ability of the private sector partner to be innovative and manage risks appropriately allocated to it can result in a specified level of service at a price that represents value for money.

C80 The PFI has now become one of the established methods of delivering many public services that require significant investment in capital asssets. Projects have been approved in such diverse areas as schools, colleges, hospitals, local authorities, defence and property management since May 1997. Approval of a PFI scheme depends on value-for-money based on an assessment of the lifetime costs of both providing and maintaining the underlying asset and the running costs of delivering the required service.

C81 The Government is committed to developing PFI and other partnership arrangements with the private sector to further enhance the delivery of public services, ensure value for money for the public sector and to ensure the delivery of a higher sustainable level of public sector investment. The Government wants to exploit all commercial potential and spare capacity in public sector assets through a sensible balance of risk and reward.

C82 Table C18 shows a breakdown by department of the estimated public sector investment resulting from signed contracts and Table C19 shows those expected to reach preferred bidder stage within the next three years.

C83 Under PFI, the public sector contracts for services facilities availability and management not assets. Capital investment is only one of the activities undertaken by the private sector in order to supply these services. The figures in Tables C18 and C19, therefore, do not reflect the total value of the contracts.

Table C18: Departmental estimate of capital spending by the private sector (signed deals)

		£ million	
		Projections	
	2003-04	2004-05	2005-06
Education and Skills[1]	0	0	0
Health	338	210	89
Transport[2]	6 624	552	370
Local government[3,4]	1 940	2 330	2 700
Home Office	186	150	46
Lord Chancellor's department	52	6	11
Defence	175	0	0
Foreign and Commonwealth Office	5	5	5
Trade and Industry	6	2	0
Environment, Food and Rural Affairs	3	0	0
Work and Pensions	14	22	0
Scotland	381	330	1
Wales	43	34	0
Northern Ireland Executive	13	3	0
Chancellor's departments	49	24	11
Cabinet Office	12	4	0
Total	**9 841**	**3 672**	**3 233**

[1] *Excludes private finance activity in education institutions classified to the private sector. Schools projects funded through Revenue Support Grant are included in the local government figures.*
[2] *Includes the capital expenditure for Tubelines (part of the London Underground Limited Public Private Partnerships (LUL PPP) contracts) in 2003-04. Such investments that are found to be on balance sheet also score as public sector net investment.*
[3] *Figures represent spending on projects supported by central government through Revenue Support Grant.*
[4] *PFI activity in local authority schools is included in the local government line.*
Source: Office of Government Commerce.

Table C19: Estimated aggregated capital value of projects at preferred bidder stage

		£ million	
		Projections	
	2003-04	2004-05	2005-06
Health	145	197	193
Transport[1]	10 759	32	11
Home Office	26	17	0
Lord Chancellor's department	19	19	0
Defence	1 364	1 393	0
Scotland	9	48	16
Wales	96	0	0
Northern Ireland Executive	31	33	0
Total	**12 449**	**1 739**	**220**

[1] *The 2003-04 figure includes the estimated capital value of the LUL PPP contracts not yet signed over the next 15 years.*
Source: Office of Government Commerce.

C84 Table C20 shows a forecast of the estimated payments for services flowing from new private investment in signed projects over the next 25 years. Actual expenditure will depend on the details of the payment mechanism for each contract. Payments may be lower than estimated due to deductions from the service payments caused by the supplier's failure to meet the required performance standards. In addition, variances may occur due to changes in the service requirements agreed during the course of the contracts. Payments may also vary as a result of the early termination of a contract triggering contractual arrangements for compensation on termination.

Table C20: Estimated payments under PFI contracts – April 2003 (signed deals)[1]

	£ billion		
	Projections		
2003-04	5.4	2016-17	4.8
2004-05	5.7	2017-18	4.1
2005-06	5.8	2018-19	3.6
2006-07	6.0	2019-20	3.4
2007-08	6.0	2020-21	3.6
2008-09	5.8	2021-22	3.2
2009-10	5.8	2022-23	3.1
2010-11	5.6	2023-24	3.1
2011-12	5.3	2024-25	3.1
2012-13	5.1	2025-26	3.0
2013-14	5.0	2026-27	1.6
2014-15	4.9	2027-28	1.3
2015-16	4.8	2028-29	1.2

[1] *The figures between 2003-04 and 2016-17 include estimated payments for the Tubelines LUL PPP contracts. These contracts contain periodic reviews every 7.5 years and therefore the service payments are not fixed after 2009-10.*

Source: Office of Government Commerce.

Box C2: Transparency in reporting liabilities and contingent liabilities

The United Kingdom is one of the few countries in the world in which the Government has a statutory requirement to report its liabilities, assets and all other key financial information in the same way as private sector companies. Since 1997, the Government has introduced a series of reforms to ensure greater transparency and increased availability of information about national and departmental finances.

The *Code for fiscal stability* commits the Government to apply best-practice accounting methods in the production of its accounts. In 2000, the Government introduced new legislation that requires departmental accounts to follow Generally Accepted Accounting Practices (UK GAAP), adapted as necessary for the public sector context. In line with these statutory requirements, departments now produce full resource accounts.

The UK has an extremely transparent system for reporting liabilities, including contingent liabilities:

- **departmental resource accounts include full disclosure of all actual and contingent liabilities. These accounts are independently audited and laid before Parliament; and**
- **departmental contingent liabilities that are reportable to Parliament, either under statute or because they are above £100,000 and outside the course of normal business, are drawn together in the Supplementary Statements to the Consolidated Fund and National Loan Funds accounts.**

The Government is committed to further improvements. In particular, it is working towards the production of Central Government Accounts (CGA) as part of the staged approach to preparing Whole of Government Accounts (WGA). Both CGA and WGA represent a significant step forward by making available, for the first time, consolidated accounts information about central government and, subsequently, the public sector as a whole. One of the benefits of CGA and WGA will be consolidated information on contingent liabilities.

FINANCING REQUIREMENT

C85 Table C21 presents projections of the net cash requirement by sector, giving details of financial transactions that do not affect net borrowing (the change in the sector's net financial indebtedness) but do affect its financing requirement. The large difference in accounts receivable/payable between 2002-03 and 2003-04 is due to a combination of factors affecting differences between cash and accrued receipts and spending.This is partly a result of the cash and accrual implications of the national insurance contribution measures announced in Budget 2002. These increase accrued receipts by more than cash receipts – reducing public sector net borrowing by more than the public sector net cash requirement.

Table C21: Public sector net cash requirement

£ billion

	2002-03				2003-04			
	General government				General government			
	Central government	Local authorities	Public corporations	Public sector	Central government	Local authorities	Public corporations	Public sector
Net borrowing	**24.5**	**–0.7**	**0.1**	**24.0**	**27.2**	**–0.1**	**0.2**	**27.3**
Financial transactions								
Net lending to private sector and abroad	2.7	–0.1	0.0	2.6	2.2	–0.1	0.0	2.1
Cash expenditure on company securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Accounts receivable/payable	–1.0	0.0	0.0	–1.0	4.7	–0.1	0.0	4.7
Adjustment for interest on gilts	–1.5	0.0	0.0	–1.5	–1.0	0.0	0.0	–1.0
Miscellaneous financial transactions	–1.7	0.0	0.1	–1.6	0.0	0.0	–0.7	–0.7
Own account net cash requirement	23.0	–0.8	0.2	22.5	33.2	–0.3	–0.5	32.4
Net lending within the public sector	–1.6	1.5	0.1	0.0	2.1	–0.3	–1.9	0.0
Net cash requirement[1]	**21.4**	**0.7**	**0.3**	**22.5**	**35.3**	**–0.5**	**–2.3**	**32.4**

[1] *Market and overseas borrowing for local government and public corporation sectors.*

C86 In order to comply with the *Code for fiscal stability,* the *Provisional Debt Management Report 2003-04* (PDMR) was published on 20 March 2003 in advance of Budget 2003. As well as updating the financing arithmetic for 2002-03, it also outlined provisional financing plans for 2003-04. The forecasts for both years' financing arithmetic were based on the public finance forecasts published in the Pre-Budget Report. For 2003-04, the provisional net financing requirement was £51.3 billion. This was to be met by gross gilts issuance of £40 billion and a £9.8 billion adjustment in the net short-term debt position.

C87 Table C22 updates the financing arithmetic for both 2002-03 and 2003-04 in line with the new forecasts for the public finances. The forecast for the central government net cash requirement for 2002-03 is £21.4 billion, an increase of £2.7 billion from the Pre-Budget Report forecast. Additionally, there have been changes to the level of the Debt Management Office's (DMO's) buy-backs of near maturity stock, their cash deposit at the Bank of England (BoE) and National Savings and Investments' (NS&I's) net contribution. Overall, this means that the net financing requirement for 2002-03 has been revised to £38.3 billion. This was met by gross gilts sales in 2002-03 of £26.3 billion and a net short-term debt adjustment of £12 billion. These changes have resulted in an end-March 2003 level for the DMO's net cash position of £4.5 billion, £2.3 billion lower than forecast in the PDMR.

C88 The forecast for the central government net cash requirement for 2003-04 is £35.3 billion, an increase of £5.1 billion from the forecast published in the PDMR. The net financing requirement is forecast to be £54.8 billion, an increase of £5 billion from the forecast published in the PDMR .

C89 In order to meet this financing requirement, the DMO's remit has been revised such that:

- gross gilt sales have been increased by £7.4 billion to £47.4 billion; and
- net-short term debt sales have decreased by £2.4 billion to £7.4 billion.

C90 Full details of these measures and complete financing tables for 2002-03 and 2003-04 can be found in the *Debt and Reserves Management Report 2003-04*, which is being published alongside this Budget.

Table C22: Financing requirement forecast

	£ billion						
	2002-03					2003-04	
	Mar-2002 Original remit[1]	Apr-2002 Budget remit	Nov-2002 Pre-Budget Report	Mar-2003 PDMR[2]	Apr-2003 Budget	Mar-2003 PDMR[2]	Apr-2003 Budget
Central government net cash requirement	**13.6**	**13.5**	**18.7**	**18.7**	**21.4**	**30.2**	**35.3**
Gilt redemptions	17.2	17.0	17.0	17.0	17.0	21.1	21.1
Debt buy-backs	0.0	0.0	0.3	0.3	0.4	0.0	0.0
Gross financing requirement	**30.8**	**30.5**	**36.0**	**36.0**	**38.8**	**51.3**	**56.4**
Less assumed net NS&I's contribution	–1.5	–1.5	–1.0	0.2	0.7	1.5	1.5
Less change in DMO's cash balance at BoE	0.0	–0.1	–0.1	–0.1	–0.2	0.0	0.1
Net financing requirement	**32.3**	**32.1**	**37.1**	**35.9**	**38.3**	**49.8**	**54.8**
Financed by							
Gross gilt sales	**23.0**	**22.4**	**26.2**	**26.4**	**26.3**	**40.0**	**47.4**
Changes in short term debt	**9.3**	**9.7**	**10.9**	**9.5**	**12.0**	**9.8**	**7.4**

Note: Figures may not sum due to rounding.

[1] The Debt and Reserves Management Report 2002-03 was published on 14 March 2002 in advance of Budget 2002 to comply with the Code for fiscal stability.

[2] The Provisional Debt Management Report 2003-04 was published on 20 March 2003 in advance of Budget 2003 to comply with the Code for fiscal stability.

ANALYSIS BY SUBSECTOR AND ECONOMIC CATEGORY

C91 Table C23 shows a breakdown of general government transactions by economic category for 2001-02 to 2005-06. Table C24 shows a more detailed breakdown for public sector transactions by sub-sector and economic category for 2002-03 and 2003-04.

Table C23: General government transactions by sub-sector

	£ billion				
	Outturn	Projections			
	2001-02	2002-03	2003-04	2004-05	2005-06
Current receipts					
Taxes on income and wealth	145.1	143.5	152.9	168.8	184.8
Taxes on production and imports	136.1	143.3	149.1	157.3	166.3
Other current taxes	18.3	19.8	22.0	23.7	25.7
Taxes on capital	2.4	2.4	2.4	2.7	2.8
Social contributions	63.1	63.6	76.2	80.8	85.1
Gross operating surplus	8.3	8.5	9.0	9.4	9.9
Rent and other current transfers	2.2	2.0	1.6	1.7	1.7
Interest and dividends from private sector and abroad	4.0	3.5	3.4	3.9	4.1
Interest and dividends from public sector	7.2	7.0	7.6	7.8	8.0
Total current receipts	**386.6**	**393.7**	**424.1**	**456.0**	**488.5**
Current expenditure					
Current expenditure on goods and services	196.4	212.7	232.0	247.3	264.2
Subsidies	6.0	7.7	7.6	8.6	9.9
Net social benefits	124.1	129.6	136.3	142.9	149.2
Net current grants abroad	–1.9	0.5	–0.2	–0.9	–1.6
Other current grants	19.4	23.2	23.4	23.7	26.9
Interest and dividends paid	22.4	21.2	22.2	23.5	24.6
AME margin	0.0	0.0	0.9	1.2	1.9
Total current expenditure	**366.5**	**395.0**	**422.2**	**446.3**	**475.0**
Depreciation	8.3	8.5	9.0	9.4	9.9
Surplus on current budget	**11.8**	**–9.8**	**–7.0**	**0.3**	**3.6**
Capital expenditure					
Gross domestic fixed capital formation	12.4	14.5	19.7	22.6	24.6
Less depreciation	–8.3	–8.5	–9.0	–9.4	–9.9
Increase in inventories	0.0	0.5	0.1	0.3	0.3
Capital grants (net) within public sector	1.3	1.4	0.6	0.6	0.6
Capital grants to private sector	6.9	7.0	9.8	10.6	11.4
Capital grants from private sector	–0.9	–0.9	–1.1	–1.0	–1.0
AME margin	0.0	0.0	0.1	0.8	1.1
Net investment	**11.4**	**14.0**	**20.1**	**24.5**	**27.1**
Net borrowing[1]	–0.4	23.8	27.1	24.2	23.5
of which:					
Central government net borrowing	–0.5	24.5	27.2	23.0	23.0
Local authority net borrowing	0.1	–0.7	–0.1	1.3	0.5

[1] *Although this is based on the ESA95 definition of general government net borrowing (GGNB), the forecasts are identical to GGNB calculated on a Maastricht definition.*

Table C24: Public sector transactions by sub-sector and economic category

	£ billion			
	2002-03			
	General government			
	Central government	Local authorities	Public corporations	Public sector
Current receipts				
Taxes on income and wealth	143.5	0.0	–0.1	143.5
Taxes on production and imports	143.1	0.1	0.0	143.3
Other current taxes	3.2	16.6	0.0	19.8
Taxes on capital	2.4	0.0	0.0	2.4
Social contributions	63.6	0.0	0.0	63.6
Gross operating surplus	4.7	3.8	9.2	17.7
Rent and other current transfers	2.0	0.0	0.6	2.6
Interest and dividends from private sector and abroad	2.8	0.7	0.6	4.1
Interest and dividends from public sector	6.2	0.8	–7.0	0.0
Total current receipts	**371.6**	**22.1**	**3.4**	**397.1**
Current expenditure				
Current expenditure on goods and services	130.3	82.5	0.0	212.7
Subsidies	6.6	1.1	0.0	7.7
Net social benefits	117.0	12.6	0.0	129.6
Net current grants abroad	0.5	0.0	0.0	0.5
Current grants (net) within public sector	78.4	–78.4	0.0	0.0
Other current grants	23.2	0.0	0.0	23.2
Interest and dividends paid	20.8	0.3	0.1	21.3
AME margin	0.0	0.0	0.0	0.0
Total current expenditure	**376.9**	**18.0**	**0.1**	**395.0**
Depreciation	4.7	3.8	5.2	13.8
Surplus on current budget	**–10.0**	**0.2**	**–1.9**	**–11.7**
Capital expenditure				
Gross domestic fixed capital formation	5.9	8.7	4.6	19.1
Less depreciation	–4.7	–3.8	–5.2	–13.8
Increase in inventories	0.5	0.0	0.0	0.5
Capital grants (net) within public sector	7.3	–5.9	–1.4	0.0
Capital grants to private sector	5.9	1.1	0.3	7.3
Capital grants from private sector	–0.4	–0.5	0.0	–0.9
AME margin	0.0	0.0	0.0	0.0
Net investment	**14.5**	**–0.5**	**–1.8**	**12.2**
Net borrowing	**24.5**	**–0.7**	**0.1**	**24.0**

Table C24: Public sector transactions by sub-sector and economic category

	£ billion			
	2003-04			
	General government			
	Central government	Local authorities	Public corporations	Public sector
Current receipts				
Taxes on income and wealth	152.9	0.0	–0.1	152.8
Taxes on production and imports	148.9	0.1	0.0	149.1
Other current taxes	3.4	18.6	0.0	22.0
Taxes on capital	2.4	0.0	0.0	2.4
Social contributions	76.2	0.0	0.0	76.2
Gross operating surplus	4.9	4.0	10.5	19.5
Rent and other current transfers	1.6	0.0	0.7	2.3
Interest and dividends from private sector and abroad	2.7	0.7	0.6	4.0
Interest and dividends from public sector	5.1	2.5	–7.6	0.0
Total current receipts	**398.2**	**26.0**	**4.2**	**428.3**
Current expenditure				
Current expenditure on goods and services	139.7	92.3	0.0	232.0
Subsidies	6.4	1.1	0.0	7.6
Net social benefits	123.4	12.9	0.0	136.3
Net current grants abroad	–0.2	0.0	0.0	–0.2
Current grants (net) within public sector	85.3	–85.3	0.0	0.0
Other current grants	23.4	0.0	0.0	23.4
Interest and dividends paid	21.8	0.3	0.1	22.3
AME margin	0.9	0.0	0.0	0.9
Total current expenditure	**400.7**	**21.4**	**0.1**	**422.3**
Depreciation	4.9	4.0	5.5	14.4
Surplus on current budget	**–7.5**	**0.5**	**–1.4**	**–8.4**
Capital expenditure				
Gross domestic fixed capital formation	9.0	10.7	4.5	24.2
Less depreciation	–4.9	–4.0	–5.5	–14.4
Increase in inventories	0.1	0.0	0.0	0.1
Capital grants (net) within public sector	7.3	–6.7	–0.6	0.0
Capital grants to private sector	8.6	1.2	0.3	10.1
Capital grants from private sector	–0.4	–0.7	0.0	–1.1
AME margin	0.1	0.0	0.0	0.1
Net investment	**19.7**	**0.4**	**–1.2**	**18.9**
Net borrowing	**27.2**	**–0.1**	**0.2**	**27.3**

HISTORICAL SERIES

Table C25: Historical series of public sector balances, receipts and debt

Per cent of GDP

	Public sector current budget	Public sector net borrowing	Cyclically adjusted public sector net borrowing	Public sector net cash requirement	General government net borrowing[1]	Net taxes and social security contributions	Public sector current receipts	Public sector net debt[2]	General government gross debt[3]	Public sector net worth[4]
1970-71	6.7	–0.6	–0.8	1.2	–2.1		43.3			
1971-72	4.2	1.1	0.5	1.4	–0.7		41.4			
1972-73	2.0	2.8	2.7	3.6	2.2		39.0			
1973-74	0.3	4.9	5.7	5.9	4.4		39.5			
1974-75	–1.1	6.6	7.2	9.0	4.1		42.3	52.1	60.4	
1975-76	–1.6	7.0	6.5	9.3	4.8		42.9	53.9	58.7	
1976-77	–1.2	5.5	4.8	6.4	4.1		43.3	52.4	59.1	
1977-78	–1.4	4.3	3.8	3.7	3.6		41.5	49.0	57.1	
1978-79	–2.6	5.0	4.8	5.2	4.3	33.3	40.2	47.1	56.2	
1979-80	–1.9	4.1	4.0	4.7	3.0	33.8	40.7	43.9	51.8	
1980-81	–3.0	4.9	2.9	5.2	3.8	35.8	42.4	46.1	52.9	
1981-82	–1.4	2.3	–1.7	3.3	3.3	38.5	45.8	46.1	51.7	
1982-83	–1.5	3.0	–1.1	3.2	3.1	38.7	45.5	44.8	50.4	
1983-84	–2.0	3.8	0.6	3.2	3.8	38.3	44.5	45.3	50.4	
1984-85	–2.2	3.7	1.0	3.1	3.3	38.9	44.4	45.2	50.3	
1985-86	–1.2	2.4	0.9	1.6	2.6	38.1	43.1	43.4	49.5	
1986-87	–1.4	2.1	1.9	0.9	2.3	37.8	42.0	41.1	48.9	
1987-88	–0.3	1.0	2.1	–0.7	1.3	37.6	41.1	36.8	46.5	75.8
1988-89	1.7	–1.3	1.2	–3.0	–0.9	36.9	40.7	30.6	40.6	81.8
1989-90	1.4	–0.2	2.5	–1.3	0.3	36.2	39.9	27.7	35.5	73.5
1990-91	0.4	1.0	2.6	–0.1	1.4	35.9	39.0	26.2	33.3	62.3
1991-92	–1.9	3.8	3.2	2.3	3.7	34.7	38.6	27.4	34.4	54.5
1992-93	–5.6	7.6	5.5	5.9	7.4	33.7	36.6	32.0	40.6	42.1
1993-94	–6.2	7.8	5.4	7.1	7.8	33.0	35.8	37.1	45.9	27.9
1994-95	–4.8	6.3	4.9	5.3	6.5	34.0	36.9	40.8	49.4	26.7
1995-96	–3.4	4.8	4.1	4.3	5.0	34.8	37.8	42.8	51.9	18.6
1996-97	–3.0	3.7	3.1	2.9	3.9	34.9	37.4	43.7	52.1	14.7
1997-98	–0.2	0.8	0.8	0.1	0.9	36.0	38.5	41.4	49.1	10.6
1998-99	1.2	–0.5	–0.2	–0.8	–0.5	36.5	38.8	39.2	46.3	10.2
1999-00	2.2	–1.7	–1.4	–0.9	–1.7	36.6	39.1	36.3	43.2	15.1
2000-01	2.2	–1.7	–1.2	–3.9	–1.7	37.4	39.8	31.2	39.8	21.3
2001-02	1.0	0.0	0.1	0.3	0.0	36.8	38.8	30.2	37.9	26.2

[1] *UK National Accounts definition.*
[2] *At end-March; GDP centred on end-March.*
[3] *Maastricht measure from 1993.*
[4] *At end-December; GDP centred on end-December.*

Table C26: Historical series of government expenditure

	£ billion (2001-02 prices)				Per cent of GDP			
	Public sector current expenditure	Public sector net investment	Public sector gross investment[1]	Total Managed Expenditure	Public sector current expenditure	Public sector net investment	Public sector gross investment[1]	Total Managed Expenditure
1970-71	161.9	30.4	49.7	211.6	32.6	6.1	10.0	42.7
1971-72	169.3	26.8	46.6	215.9	33.3	5.3	9.2	42.5
1972-73	177.0	25.8	46.6	223.6	33.1	4.8	8.7	41.8
1973-74	194.5	29.0	52.3	246.8	35.0	5.2	9.4	44.4
1974-75	215.1	30.6	55.6	270.7	38.8	5.5	10.0	48.8
1975-76	219.8	30.0	55.3	275.1	39.9	5.5	10.0	49.9
1976-77	225.9	24.5	50.6	276.5	39.9	4.3	8.9	48.8
1977-78	222.5	16.6	42.7	265.2	38.4	2.9	7.4	45.8
1978-79	229.2	14.5	41.1	270.3	38.4	2.4	6.9	45.2
1979-80	234.9	13.4	40.5	275.3	38.2	2.2	6.6	44.8
1980-81	241.7	10.8	38.1	279.9	40.8	1.8	6.4	47.3
1981-82	252.7	5.5	32.7	285.4	42.6	0.9	5.5	48.1
1982-83	258.5	9.1	35.5	293.9	42.7	1.5	5.9	48.5
1983-84	266.7	11.2	37.5	304.2	42.3	1.8	5.9	48.3
1984-85	274.2	9.9	34.8	309.0	42.6	1.5	5.4	48.1
1985-86	274.1	8.3	30.6	304.7	41.0	1.2	4.6	45.5
1986-87	278.1	5.0	27.5	305.6	40.1	0.7	4.0	44.1
1987-88	281.8	4.8	25.6	307.4	38.6	0.7	3.5	42.1
1988-89	275.4	2.7	24.3	299.7	36.2	0.4	3.2	39.4
1989-90	277.2	9.3	31.0	308.2	35.7	1.2	4.0	39.7
1990-91	279.0	11.2	30.1	309.1	36.1	1.4	3.9	40.0
1991-92	295.8	14.2	30.2	325.9	38.4	1.8	3.9	42.3
1992-93	310.5	15.5	30.4	340.9	40.3	2.0	3.9	44.2
1993-94	320.8	12.7	27.3	348.1	40.1	1.6	3.4	43.6
1994-95	332.0	12.5	27.6	359.6	39.9	1.5	3.3	43.2
1995-96	337.1	12.0	27.3	364.4	39.4	1.4	3.2	42.6
1996-97	340.5	6.0	20.2	360.7	38.7	0.7	2.3	41.0
1997-98	337.9	5.4	19.1	356.9	37.2	0.6	2.1	39.3
1998-99	337.7	6.5	20.0	357.7	36.2	0.7	2.1	38.4
1999-00	342.3	4.6	17.9	360.2	35.6	0.5	1.9	37.4
2000-01	357.3	5.3	18.7	376.0	36.2	0.5	1.9	38.1
2001-02	366.6	9.6	23.0	389.6	36.5	1.0	2.3	38.8

[1] *Net of sales of fixed assets.*

CONVENTIONS USED IN PRESENTING THE PUBLIC FINANCES

FORMAT FOR THE PUBLIC FINANCES

The June 1998 Economic and Fiscal Strategy Report (EFSR), set out a new format for presenting the public finances that corresponded more closely to the two fiscal rules. The three principle measures are:

- **the surplus on current budget (relevant to the golden rule);**
- **public sector net borrowing; and**
- **the public sector net debt ratio (relevant to the sustainable investment rule).**

These measures are based on the National Accounts and are consistent with the European System of Accounts 1995 (ESA95). Estimates and forecasts of the public sector net cash requirement (formerly called the public sector borrowing requirement) are still shown in the FSBR, but they are given less prominence.

The fiscal rules are similar to the criteria for deficits and debt laid down in the Treaty but there are important definitional differences:

- **UK fiscal rules cover the whole public sector, whereas the Treaty deficit and debt only includes general (i.e. central and local) government;**
- **the fiscal rules apply over the whole economic cycle, not year to year;**
- **the current budget excludes capital spending, which is included in the Treaty deficit measure; and**
- **the UK debt measure is net of liquid assets, whereas the Treaty measure uses gross debt.**

From February 2000 the Treaty deficit moved to being reported on an ESA95 basis.

NATIONAL ACCOUNTS

The **National Accounts** record most transactions, including most taxes (although not corporation tax), on an accruals basis, and impute the value of some transactions where no money changes hands (for example, non-trading capital consumption). The principle measures drawn from the National Accounts are described below.

The **current budget** (formerly known as the current balance) measures the balance of current account revenue over current expenditure. The definition of the current budget presented in this chapter is very similar to the National Accounts concept of net saving. It differs only in that it includes taxes on capital (mainly inheritance tax) in current rather than capital receipts.

Public sector net borrowing (formerly known as the financial deficit in the UK National Accounts) is the balance between expenditure and income in the consolidated current and capital accounts. It differs from the public sector net cash requirement in that it is measured on an accruals basis and because certain financial transactions (notably net lending and net acquisition of other financial assets, which affect the level of borrowing but not the public sector's net financial indebtedness) are excluded from public sector net borrowing but included in the public sector net cash requirement.

General government net borrowing, which excludes net borrowing of public corporations, is the most internationally comparable measure of the budget deficit. It was established as the European Commission's reported measure under the Maastricht Treaty, although its definition has since been slightly modified to depart from that in ESA95.

PUBLIC SECTOR CURRENT RECEIPTS

Net taxes and social security contributions (NTSSC) is a measure of net cash payments made to UK government and differs in several respects from the National Accounts measure of total **public sector current receipts (PSCR)**. A reconciliation between the two aggregates is given in the lower half of Table C8. The main adjustments are:

- accruals adjustments, mainly on income tax, national insurance contributions and VAT, are added to change the basis of figures from cash to National Accounts accruals;
- some tax payments that are collected by the government, but then paid to the EC, are subtracted as they do not score as government receipts in the National Accounts;
- tax paid by public corporations is also subtracted, as it has no impact on overall public sector receipts;
- an adjustment is made for tax credits. In NTSSC, all tax credits are scored as negative tax to the extent that they are less than or equal to the tax liability of the household, and as public expenditure where they exceed the liability, in line with OECD Revenue Statistics guidelines. Although the Office for National Statistics (ONS) have adopted this treatment for the Working Tax Credit and Child Tax Credit, due to be introduced in April 2003, they have continued to treat the Working Families' Tax Credit (WFTC), the Disabled Person's Tax Credit (DPTC) and enhanced and payable company tax credits entirely as public expenditure in the National Accounts. Those parts of WFTC, DPTC and company tax credits that offset tax liability in NTSSC are added back into current receipts in Table C8; and
- interest and other non-tax receipts, which are excluded from NTSSC, are added. This excludes oil royalties, as they are already included in NTSSC, even though the National Accounts treat them as non-tax receipts.

TOTAL MANAGED EXPENDITURE

Public expenditure is measured across the whole of the public sector using the aggregate **Total Managed Expenditure (TME)**. TME is the sum of public sector current expenditure, public sector net investment and public sector depreciation. These aggregates are based on National Accounts definitions defined under ESA95.

Public sector current expenditure is the sum of expenditure on pay, and related costs, plus spending on goods and services, and current grants made to the private sector. Current expenditure is net of receipts from sales of goods and services.

Public sector capital expenditure is shown in Table C16. It includes:

- gross domestic fixed capital formation (i.e. expenditure on fixed assets such as schools and hospitals, roads, computers, plant and machinery and intangible assets) net of receipts from sales of fixed assets (e.g. council houses and surplus land);
- grants in support of capital expenditure in the private sector; and
- the value of the physical increase in stocks (for central government, primarily agricultural commodity stocks).

Public sector net investment: in Table C1 nets off depreciation of the public sector's stock of fixed assets.

Public sector depreciation: is the annual charge that is made in relation to the reduction in value of the public sector's capital assets over a particular financial year.

For budgeting purposes, TME is further split into:

Departmental Expenditure Limits (DEL) are firm three-year spending limits for departments. In general DEL will cover all running costs and all programme expenditure except that spending that is included in departmental Annually Managed Expenditure due to it not being reasonably subject to close control over the three year period. DEL has distinct resource and capital budgets, as shown in Table C13.

Annually Managed Expenditure (AME) is spending that cannot be reasonably subject to firm multi-year limits. AME components are shown in Table C11 and are defined as follows:

Social security benefits in AME expenditure covers contributory, non-contributory and income-related benefits for children, people of working age and pensioners. Broadly, benefits are paid in respect of retirement, unemployment, incapacity or disability, caring responsibilities and bereavement, as well as housing costs for all groups. Some expenditure on housing-related benefits is, however, covered by the Housing Revenue Account subsidies and locally financed expenditure categories.

Tax credits scored as expenditure includes spending on the Working Families' Tax Credit and Disabled Person's Tax Credit and that element of the Working Tax Credit and the Child Tax Credit that is classified as public expenditure under National Accounts definitions. For 2001-02 to 2004-05, expenditure related to the child allowances in Income Support and Jobseekers' Allowance, which, from 2003-04, are paid as part of the Child Tax Credit, have been included in the tax credit line rather than in the social security benefits line in order to present figures on a consistent definition over the period shown.

Housing Revenue Account subsidies relates to two main areas of public expenditure: Housing Benefit paid to tenants of local authority-owned social housing; and subsidy to meet deficits on local authority Housing Revenue Accounts as part of a national redistributive system.

Common Agriculture Policy expenditure comprises direct payments to farmers and market price supports (intervention purchases and export refunds).

Net public service pensions. The main unfunded public service pension schemes, following FRS17, report any increase in liabilities accrued in the period less contributions received from employers, employees and inward transfers. This line does not include an amount for the unwinding of the discount rate on the liability (which scores elsewhere in AME). For some small unfunded schemes, information is not available on an FRS17 basis, and these schemes report the difference between the cash paid out during the year and any contributions received.

National Lottery expenditures relate to the distribution of the money received from the National Lottery for good causes. Funds are drawn down by Distributor Bodies and directed towards Lottery funded projects.

Non-cash items in AME. Under the 2002 Spending Review resource budgeting regime, a department's spending budget includes certain items that do not have a cash component at the time when the expense is recorded. Examples include depreciation, cost of capital charges and provisions.

Other departmental expenditure aggregates all other expenditure made by departments that is not seperately identified in the AME table.

Net Payments to EC (European Communities) institutions is the balance between the UK's gross contribution to the EC Budget minus the UK abatement and public sector receipts from the EC Budget (net contribution to EC budget). For domestic public expenditure planning purposes part of the UK's contribution to the EC budget is attributed to the overseas aid programme and excluded from the net payments to EC institutions figures.

Locally financed expenditure consists of local authority self-financed expenditure (LASFE) and Scottish spending financed by local taxation (non-domestic rates and, if and when levied, the Scottish variable rate of income tax). LASFE is the difference between total local authority expenditure, including most gross debt interest but net of capital receipts, and central government support to local authorities (i.e. Aggregate External Finance (AEF), specific grants and credit approvals).

Central government debt interest is shown gross – only interest paid within the public sector is netted off. All other receipts of interest and dividends are included in current receipts. The capital uplift on index-linked gilts is also scored here as interest at the time it accrues as is the amortisation of discounts on gilts at issue.

Public corporations' own-financed capital expenditure. This is the amount of capital expenditure by public corporations that is not financed by general government.

AME margin is an unallocated margin on total AME spending and is included as a measure of caution against AME expenditure exceeding its forecast levels.

The **accounting adjustments** include various items within TME but outside DEL, which are not shown separately in Table C11. The definition of each line is as follows:

Removal of non-cash spending in DEL[4] *and AME* pertain to a number of non-cash expenditure items recorded as DEL and AME expenditure that are not consistent with TME defined under a National Accounts basis.

Financial transactions in DEL and in AME are deducted. This is because TME measures the current and capital expenditure of the public sector, as defined in the National Accounts. This excludes expenditure on the acquisition of financial assets since in the National Accounts these are classified as financial transactions, not capital expenditure. Departmental budgets include the net acquisition of certain types of financial assets. These are assets acquired for policy purposes rather than cash flow management and typically refer to transactions in shares and lending to businesses and individuals.

[4] Excluding depreciation in resource DEL.

Adjustments for public corporations. Under the 2002 Spending Review, departments' budgets score transactions with their public corporations. These adjustments remove those transactions and move the scoring of public corporations' spending onto a National Accounts basis.

Central government non-trading capital consumption (i.e. depreciation) as measured by ONS for National Accounts is added.

VAT refunded on general government expenditure is added back and covers refunds obtained by central government departments, local authorities and certain public corporations. DEL and AME programme expenditure are measured net of these refunds, while TME is recorded with VAT paid.

EC contribution deducts traditional own resources (i.e. payments of Customs duties and agricultural and sugar levies) and VAT contributions to European Community, which are included in the net payments to EC institutions line in AME but excluded from TME.

Tax credits are only added back if they score as public expenditure under National Accounts conventions but are not included as expenditure in AME. This includes Mortgage Interest Relief, Life Assurance Premium Relief, Private Medical Insurance Premium Relief, Vocational Training Relief (part up to 1998-99; all from 1999-2000), Working Families' Tax Credit and Disabled Person's Tax Credit (from 1999-2000) and the Research and Development Tax Credit (from 2001-02).

Intra-general government debt interest is deducted as it removes intra-public sector debt interest and dividend payments and receipts, which are included elsewhere in DEL and AME. The reason for this is that TME is consolidated public sector expenditure; so it records only those distributive transactions that are paid outside the public sector. Payments of grants and interest that are within the public sector do not score in TME. So it is necessary to deduct any interest payments to the public sector included in DEL or the debt interest figures in AME in other AME.

Other accounting adjustments shows other adjustments and includes, among others, the deduction of grants paid to local authorities by non-departmental public bodies classified to the central government sector, loan and debt write-offs and loan guarantees.

DEBT AND WEALTH

Public sector net debt is approximately the stock analogue of the public sector net cash requirement. It measures the public sector's financial liabilities to the private sector and abroad, net of short-term financial assets such as bank deposits and foreign exchange reserves.

General government gross debt, the Treaty debt ratio, is the measure of debt used in the European Union's Excessive Deficit Procedure. As a general government measure, it excludes the debt of public corporations. It measures general government's total financial liabilities before netting off short-term financial assets.

Public sector net worth represents the public sector's overall net balance sheet position. It is equal to the sum of the public sector's financial and non-financial assets less its total financial liabilitites. The estimates of tangible assets are subject to wide margins of error, because they depend on broad assumptions, for example about asset lives, which may not be appropriate in all cases. The introduction of resource accounting for central government departments will lead in time to an improvement in data quality, as audited information compiled from detailed asset registers becomes available.