

# Budget 2006

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**A strong and strengthening economy:  
Investing in Britain's future**

## **Economic and Fiscal Strategy Report and Financial Statement and Budget Report**

March 2006

Return to an Order of the House of Commons dated 22 March 2006

*Copy of Economic and Fiscal Strategy Report and Financial Statement and Budget Report – March 2006  
as laid before the House of Commons by the Chancellor of the Exchequer when opening the Budget.*

John Healey  
Her Majesty's Treasury  
22 March 2006

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The Economic and Fiscal Strategy Report and the Financial Statement and Budget Report contain the Government's assessment of the medium-term economic and budgetary position. They set out the Government's tax and spending plans, including those for public investment, in the context of its overall approach to social, economic and environmental objectives. After approval for the purposes of Section 5 of the European Communities (Amendment) Act 1993, these reports will form the basis of submissions to the European Commission under Article 99 (ex Article 103) and Article 104 (ex Article 104c) of the Treaty establishing the European Community.

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# OVERVIEW

The Government's economic objective is to build a strong economy and a fair society, where there is opportunity and security for all. Budget 2006, *A strong and strengthening economy: Investing in Britain's future*, presents updated assessments and forecasts of the economy and public finances, and reports on how the Government's policies are helping to deliver its long-term goals. The Budget:

- shows that the economy is stable and growing and that the Government is meeting its strict fiscal rules for the public finances;
- announces further measures to help families and children, including a commitment to increase the child element of the Child Tax Credit in line with average earnings to the end of this Parliament;
- announces that the payments into Child Trust Fund accounts at age 7 will be £250 for all children, with £500 for children from lower-income families;
- takes further steps to extend employment opportunity for all, through measures which focus help and support on those who face the greatest barriers to work;
- announces that from April 2008 every pensioner and disabled person will have free off-peak national bus travel in England;
- announces £585 million of additional resources over 2006-07 and 2007-08 to provide further support for personalised learning in schools in England;
- announces further measures to boost productivity and growth, to build on the UK's position as a leading location for inward investment, advance the science and innovation ten-year framework, and to reduce further the burden of regulation on business;
- provides £100 million to accelerate the recruitment of Police Community Support Officers;
- commits funding, in partnership with commercial sponsorship, to support the most talented British athletes to prepare for the 2012 Olympics;
- takes steps to tackle the global challenge of climate change, including reforms to vehicle excise duty and measures to encourage energy efficiency in the household and business sectors;
- introduces measures to modernise the tax system, and to tackle tax fraud and avoidance; and
- defers the inflation-based increase in main road fuel duties to 1 September 2006.

**1.1** The Government's economic objective is to build a strong economy and a fair society, where there is opportunity and security for all.

**1.2** The long-term decisions the Government has taken – giving independence to the Bank of England, new fiscal rules and a reduction in debt – have created a strong platform of economic stability. In recent years, the international economy has been affected by geopolitical uncertainty, rising oil prices, and large current account imbalances and shifting exchange rates between the US, Asia and Europe. In the UK, with low and stable inflation, interest rates set by the Monetary Policy Committee to meet the Government's symmetric inflation target, and fiscal policy supporting monetary policy over the cycle, the economy has grown continuously throughout this period. The UK economy is currently experiencing its longest unbroken expansion since quarterly records began, with GDP now having grown for 54 consecutive quarters.

**Meeting long-term global challenges**

**I.3** The global economy is undergoing a major transformation, with far-reaching and fundamental changes in technology, production and trading patterns. Faster information flows and falling transport costs are breaking geographical barriers to economic activity. The boundary between what can and cannot be traded is being steadily eroded, and the global market is encompassing ever-greater numbers of goods and services. This fast pace of change, combined with emergence of rapidly industrialising economies such as China and India and their integration into the global economy, presents new opportunities for the UK as well as new challenges. The increasing demands placed on the world's resources and environment also heightens the need to tackle the global challenge of climate change.

**I.4** A more integrated global economy increases the speed and magnitude with which global shocks and imbalances can affect the UK. The UK's strong macroeconomic framework has helped to underpin increased stability compared to earlier decades, and put the UK in a strong position to resist the inflationary pressure bought by recent sustained increases in oil prices. The UK has been experiencing an unprecedented period of economic stability since 1997, with volatility at historically low levels and now the lowest in the G7. Economic stability provides the platform for building prosperity, achieving social justice with security and opportunity for all, and maintaining investment in public services. Stability allows businesses, individuals and the Government to plan more effectively for the long term, improving the quantity and quality of investment and helping to raise productivity.

**I.5** The Government is committed to locking in stability and investing in the UK's future, enabling it to meet the challenges and rise to the opportunities of the global economy. To respond to these global challenges, this Budget sets out further reforms to reduce the regulatory burden on business; to create a world-class environment for scientific research and development; to improve the skills of the nation; to lock in the UK's track record of attracting high levels of inward investment; and to tackle the global challenges of climate change.

**I.6** Fairness must go alongside flexibility, providing security and support for those that need it and ensuring that everyone has the opportunity to fulfil their potential. The reforms of the welfare state introduced since 1997 reflect the Government's aims of eradicating child poverty, supporting families to balance their work and family life, promoting saving, and ensuring security for all in old age. The Government is also committed to a modern and fair tax system which encourages work and saving, and ensures that everyone pays their fair share of tax. The Budget announces further measures to help support families, children and pensioners, and to promote employment opportunity for all.

**I.7** This Budget describes the next steps the Government is taking to enhance its long term goals of:

- **maintaining macroeconomic stability**, ensuring the fiscal rules are met and that inflation remains low;
- **raising the sustainable rate of productivity growth**, through reforms that promote enterprise and competition, enhance flexibility and promote science, innovation and skills;
- **providing employment opportunity for all**, by promoting a flexible labour market which sustains a higher proportion of people in employment than ever before;
- **ensuring fairness**, by providing security for people when they need it, tackling child and pensioner poverty, providing opportunity for all children and young people and delivering security for all in retirement;

- **delivering world-class public services**, with extra investment alongside efficiency, reform and results; and
- **addressing environmental challenges**, such as climate change and the need for energy efficiency in response to rising oil prices.

## MAINTAINING MACROECONOMIC STABILITY

**I.8** The Government's long-term economic goal is to maintain macroeconomic stability, ensuring the fiscal rules are met at all times and that inflation remains low. Chapter 2 describes how the Government is working to achieve this goal and summarises prospects for the UK economy and public finances, full details of which are set out in Chapters B and C of the *Financial Statement and Budget Report (FSBR)*.

**The policy framework** **I.9** The Government's macroeconomic framework is based on the principles of transparency, responsibility and accountability, and is designed to ensure lasting stability so that businesses, individuals and the Government can plan effectively for the long term. The Bank of England has operational independence to meet the Government's symmetrical inflation target. Fiscal policy is underpinned by clear objectives and two strict rules which ensure sound public finances over the medium term. The fiscal rules underpin the Government's public spending framework which facilitates long-term planning and provides departments with the flexibility and incentives they need to increase the quality of public services and deliver specified outcomes.

**Economic prospects** **I.10** The UK economy is currently experiencing its longest unbroken expansion on record, with GDP now having grown for 54 consecutive quarters. The domestic stability delivered by the Government's macroeconomic framework, with volatility in the UK economy at historically low levels and the lowest in the G7, puts the UK in a strong position to respond to the global economic challenges of the next decade.

**I.11** Overall economic developments since the 2005 Pre-Budget Report have been as forecast. Economic growth has gradually increased momentum through the latter stages of 2005 and into 2006. With the outturn for 2005 and the forecast for 2006 as expected at the time of the Pre-Budget Report, the UK economy remains well placed for a pick-up in growth to above trend rates later this year and into 2007, supported by the continuing domestic stability delivered by the Government's macroeconomic framework. Overall, the Budget forecast is as set out in the 2005 Pre-Budget Report. GDP is forecast to grow by 2 to 2½ per cent in 2006, rising to above-trend rates of 2¾ to 3¼ per cent in both 2007 and 2008.

**The public finances** **I.12** The Budget 2006 projections for the public finances are broadly in line with the 2005 Pre-Budget Report and show that the Government is meeting its strict fiscal rules:

- the current budget shows an average surplus as a percentage of GDP over the current economic cycle, even using cautious assumptions, ensuring the Government is meeting the golden rule. Beyond the end of the current cycle, the current budget moves clearly into surplus including, by the end of the projection period, the cyclically-adjusted current budget in the cautious case; and
- public sector net debt is projected to remain low and stable over the forecast period, stabilising at a level below the 40 per cent ceiling set in the sustainable investment rule.

**Table 1.1: Meeting the fiscal rules**

	Per cent of GDP						
	Outturn	Estimate	Projections				
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
<b>Golden rule</b>							
Surplus on current budget	-1.6	-0.9	-0.6	0.1	0.5	0.7	0.8
Average surplus since 1997-1998	0.2	0.1	0.0	0.0	0.1	0.1	0.2
Cyclically-adjusted surplus on current budget	-1.3	-0.3	0.4	0.7	0.7	0.7	0.8
<b>Sustainable investment rule</b>							
Public sector net debt <sup>1</sup>	35.0	36.4	37.5	38.1	38.3	38.4	38.4

<sup>1</sup> Debt at end March; GDP centred on end March.

**Budget policy 1.13** Against this backdrop, and building on steps already taken, Budget 2006 announces **decisions** further decisions to lock in stability and invest in the UK's future, including:

- a commitment to increase the child element of the Child Tax Credit in line with average earnings to the end of this Parliament;
- that the further payments into Child Trust Fund accounts at age 7 will be £250 for all children, with £500 for children from lower-income families;
- £585 million of additional resources over 2006-07 and 2007-08 to provide further support for personalised learning in schools in England;
- an increase in the stamp duty land tax threshold to £125,000, exempting an additional 40,000 home buyers each year;
- the introduction of Real Estate Investments Trusts to create greater flexibility for investors;
- measures to modernise the tax system, and to tackle tax fraud and avoidance; and
- the deferral of the inflation-based increase in main road fuel duties to 1 September 2006, in response to sustained volatility in oil prices.

**1.14** Consistent with the requirements of the *Code for Fiscal Stability*, the updated public finance projections in Budget 2006 take into account the fiscal effects of these and all other firm decisions announced in the Budget. The fiscal impact of Budget policy decisions is set out in Table 1.2. Full details are provided in Chapter A of the FSBR.

**1.15** An updated analysis of long-term fiscal sustainability was published alongside the 2005 Pre-Budget Report in the *2005 Long-term public finance report*, and is updated in Annex A of the Economic and Fiscal Strategy Report. Using a range of sustainability indicators, this shows that the public finances are sustainable in the longer term, and that the UK is well placed relative to many other countries to face the challenges of an ageing population.

## MEETING THE PRODUCTIVITY CHALLENGE

**1.16** Productivity growth, alongside high and stable levels of employment, is central to long-term economic performance. In the increasingly knowledge-driven global economy, science, innovation and creativity are important drivers of productivity growth, backed up by a highly skilled workforce and a competitive and enterprising economy. The UK has

historically experienced comparatively low rates of productivity growth. However, as set out in *Productivity and the UK 6: Progress and New Evidence*, published alongside this Budget, UK performance has improved in relation to other major economies in recent years. The Government's long term goal is for the UK to continue to close the productivity gap by achieving a faster rate of growth than its main competitors.

- Action so far I.17** The Government's strategy focuses on five key drivers of productivity performance:
- **improving competition** which promotes flexible markets and increases business efficiency and consumer choice;
  - **promoting enterprise**, including through reducing the regulatory burden on business, to ensure that UK firms are well-placed to respond to opportunities in a rapidly changing global market;
  - **supporting science and innovation** which is central to success in the international economy, as global restructuring focuses developed economies toward knowledge-based and high value-added sectors;
  - **raising UK skills** to create a more flexible and productive workforce, and to meet the long-term challenge of rising skills levels in emerging markets; and
  - **encouraging investment** to increase the stock of physical capital supported by stronger, more efficient capital markets. In the global economy, attracting international capital and investment will require macroeconomic stability and a robust and efficient investment environment.

- Next steps I.18** Building on the reforms and initiatives already introduced, Budget 2006 sets out the next steps the Government is taking to strengthen the drivers of productivity growth and meet the long-term challenges of the global economy, including:
- **advancing the goals of the ten-year Science and Innovation Investment framework to maximise the impact of science funding**, including an intention to create a single health research fund of at least £1 billion per year, to simplify radically institutional research funding, to expand R&D support to mid-sized companies and introduce a package of measures to improve science teaching, raise the quality of science lessons and entitle able pupils to study three separate sciences at GCSE;
  - **measures to reduce further burdens on business**, including new commitments to reduce the administrative burden of the tax system, introducing the Hampton Review's principles into law, and a review of how the experiences of large business can be taken into account in administering the tax system;
  - **a comprehensive package of measures further to enhance the UK's position as a leading location for inward investment**, developing an ambitious strategy for marketing the UK;
    - **promoting London as the world's leading international centre for financial and business services**, with a new strategy to be developed and implemented by a high-level group representing the City's key interests by summer 2006;
    - **establishing a new International Business Advisory Council** comprising some of the world's foremost business people;

- **a programme of organisational changes to UK Trade and Investment** with the aim of a fundamental transformation of its effectiveness in marketing the UK;
- **strengthening the UK's reputation as one of the world's best locations for higher education**, by boosting support for international students to the UK, and establishing three new University Partnership Schemes;
- **building on the Government's commitment to raise skills levels** by investing in the reform of further education and training provision, and asking the Leitch Review of Skills to report specifically on how skills and employment policy can better complement each other;
- **boosting access to finance to enable early-stage companies with real growth potential to bridge the equity gap and progress through to market**, announcing a further £50 million in 2006-07 and £50 million in 2007-08 for the Enterprise Capital Funds scheme; and
- **taking forward the Government's strategy for tackling the long-term lack of supply and responsiveness of housing and property** and introducing Real Estate Investment Trusts to create greater flexibility for investors.

## INCREASING EMPLOYMENT OPPORTUNITY FOR ALL

**I.19** The Government's long-term goal is employment opportunity for all – the modern definition of full employment. It aims to ensure a higher proportion of people in work than ever before by 2010. To achieve this, each individual who wants and is able to work should be provided with the support to enable them to find work and develop skills. The Government is also determined to build a flexible labour market which allows the economy to respond quickly and efficiently to economic change, driven for example by shifting patterns of international production and trade.

**Action so far I.20** The Government's strategy for extending employment opportunity to all builds on the strong performance of the UK labour market over recent years. UK unemployment has fallen to 5.0 per cent, significantly below the EU average of 7.7 per cent, while the working age employment rate has reached 74.5 per cent. Chapter 4 describes the successful action the Government has already taken to increase employment opportunity, through:

- **delivering employment opportunity to all**, to provide everyone who is able to work with the support they need to move into work as quickly as possible;
- **extending employment opportunity** to those groups and regions which have faced the greatest barriers to work;
- **enhancing skills and mobility**, to ensure that everyone can fulfil their potential in the labour market and that business has access to the skilled workforce they need to compete in the global economy; and
- **making work pay**, through the National Minimum Wage and tax credits which create a system of support that provides greater rewards from work, improving incentives for individuals to participate in the labour market.

**Next steps I.21** Budget 2006 describes the further steps the Government is taking to build on this success and further strengthen the labour market, with a long-term vision for extending support to the inactive and those who face particular barriers to work. The Budget announces:

- **an extension of the support offered to lone parents** through ensuring that all lone parents who have claimed benefit for at least a year will be required to attend a Work Focused Interview every six months;
- **a strengthened, refocused, Fortnightly Job Review for Jobseeker's Allowance claimants, from June 2006**, to ensure that only those claimants who are able to demonstrate that they have undertaken their responsibilities to look for work are allowed to continue their claim;
- **measures to reduce anomalies in, and further simplify, housing benefit; and to tackle fraud and error in the housing benefit system;**
- **in response to the Women and Work Commission report, new funding to:**
  - **double the number of existing Skills Coaching pilots to 16 Jobcentre Plus districts** with a specific focus on helping low-skilled women return to work;
  - **increase, by 50 per cent, the number of pilots delivering level 3 skills**, with an additional pilot focused on women with low skills; and
  - **help Sector Skills Councils in industries with skills shortages test new recruitment, training and career pathways** for over 10,000 low skilled women;
- publication of *Employment Opportunity for all: analysing labour market trends in London*, alongside this Budget, examining the underlying reasons why employment rates are lower in London compared to other parts of the country, as a basis for future policy action;
- publication of the Welfare Reform Green Paper announcing national roll out of the successful Pathways to Work pilot projects by 2008 for Incapacity Benefit claimants, and consulting on replacement of the current system of incapacity benefits with a new Employment and Support Allowance;
- following the Low Pay Commission's recommendations, **the adult rate of the National Minimum Wage will rise to £5.35 from October 2006.**

## BUILDING A FAIRER SOCIETY

**I.22** The Government's long-term economic goal is to combine flexibility with fairness. Policies that ensure fairness act to minimise the short-term costs that can be associated with the changes that are needed in flexible outward-looking economies. Fairness provides security and support for those that need it and ensures that everyone has the opportunity to fulfil their potential in the global economy, now and in the future. The Government is also at the forefront of global efforts to achieve the Millennium Development Goals for global poverty, and to reduce debt in the poorest countries.

**Action so far I.23** Chapter 5 describes the range of reforms the Government has undertaken to achieve its goals in these areas, including:

- **support for families and children** to lift children out of poverty and so ensure they have the opportunity to fulfil their potential;

- **support for pensioners** to tackle poverty and ensure security in retirement for all pensioners, with extra help for those who need it most and rewards for those who have saved modest amounts;
- **steps to encourage saving**, including through the introduction of the Child Trust Fund, stakeholder pensions and Individual Savings Accounts; and
- **measures and reforms to improve the tax system**, and to ensure that everyone pays their fair share toward extra investment in public services.

**Next steps I.24** Building on these reforms, the Government is committed to taking the long-term decisions to promote opportunity and fairness. The Budget announces:

- that **from April 2008 every pensioner and disabled person in England will have free off-peak national bus travel**;
- building on progress in reducing the number of children in poverty, **a commitment to increase the child element of the Child Tax Credit at least in line with average earnings until the end of the Parliament**;
- measures to enable employers to support working parents with their childcare, by **raising the tax and national insurance contributions exemption for employer supported childcare to £55 per week** and by making available **capital grants to help employers establish workplace nurseries**;
- that the **payments into Child Trust Fund accounts at age seven will be £250 for all children, with £500 for children from lower-income families**;
- a review of policy for children and young people, supported **in this Budget by £10 million over two years to promote youth engagement in their communities, sports and local media**;
- **an increase in the stamp duty land tax threshold to £125,000**, exempting an additional 40,000 homebuyers each year;
- **that the inheritance tax threshold will rise to £312,000 in 2008-09 and £325,000 in 2009-10**, to continue to provide a fair and targeted system; and
- **establishing this Government's largest ever consultation with the third sector**, to be overseen by a cross-departmental ministerial group;
- further reforms to **modernise the tax system**, including investing in high capacity online filing services and a number of measures to clamp down on **tax fraud and avoidance**.

## DELIVERING HIGH QUALITY PUBLIC SERVICES

**I.25** The Government's aim is to deliver world class public services, with extra investment tied to reform and results. Investment in key public services provides the foundation on which the UK will be able to meet the long-term global economic challenges. A healthy, skilled and educated workforce, modern and reliable transport networks, and an adequate supply of affordable housing will promote productivity and flexibility, and also help to ensure opportunity and security for all, both now and in future generations. The Government's strategy is to deliver improvements in public services through sustained investment and reform to ensure that taxpayers receive value for money.

**Action so far I.26** Chapter 6 sets out the steps the Government has taken to deliver lasting improvements in the delivery of public services, including:

- **a new framework for managing public spending** that strengthens incentives for departments to plan for the long term;
- **significant extra resources for public services**, consistent with the strict fiscal rules.
- **challenging efficiency targets** for all departments, delivering over £20 billion of efficiency gains a year by 2007-08 to be recycled to front-line public services.

**I.27** A decade on from the first Comprehensive Spending Review (CSR), the Government will be conducting a second CSR reporting in 2007. In preparation, this Budget announces:

- **plans for a national debate about how public services should respond to the long-term challenges facing the UK;**
- **a series of reviews that will inform the CSR** in the areas where cross-departmental collaboration and innovative solutions are required to meet these challenges;
- **further details of the next phase of the Government's value for money programme**, including progress on asset disposals and a review of opportunities for transforming service delivery across government, looking at how the channels through which services are delivered can be made more efficient and responsive to the needs of users; and
- **early spending settlements for the Department for Work and Pensions, HM Revenue and Customs, Cabinet Office and HM Treasury Group which see their Departmental Expenditure Limits fall by five per cent per year in real terms over the CSR period, releasing over £1.8 billion in total for re-investment in front-line public services.**

**Next steps I.28** The Government's long-term goal is to deliver world class public services through investment and reform, while ensuring efficiency and value for money. The Budget announcements include further measures directing resources towards the Government's priorities, including:

- £585m of additional resources over 2006-07 and 2007-08 to provide further support for personalised learning in schools in England. Further, capital investment in schools will rise from £6.4 billion in 2007-08 to £8.0 billion by 2010-11, matching today's level of private sector per pupil capital investment;
- £100m to accelerate the recruitment of Police Community Support Officers (PCSOs) together with firm spending plans for the Home Office over the CSR period which lock in the large real increases in resources since 1999, providing the long-term funding certainty needed to lead the fight against crime and terrorism and realise the benefits of police force restructuring and reform;
- a commitment of £200m of Exchequer funds to ensure elite athletes have the best chance of success in a British Olympics in 2012; and
- £800m of provision for the Special Reserve in 2006-07, set aside from within existing public spending plans, to help meet the costs of Iraq, Afghanistan and other international commitments.

## PROTECTING THE ENVIRONMENT

**I.29** The Government's goal is to deliver sustainable growth and a better environment, by addressing the challenges of climate change, poor air quality and environmental degradation in urban and rural areas. Sustainable development is vital to ensure a better quality of life for everyone, today and for generations to come. Economic growth is key to rising national prosperity. However, growth in the developed world, accompanied with the rapidly growing and highly populated economies of China and India, will place increasing demands on the world's resources and environment over the coming decade. Meeting this long-term challenge requires action at a local and national level, but crucially also through international cooperation.

**Action so far I.30** Chapter 7 describes the steps the Government has taken to deliver its environmental objectives, including:

- **tackling climate change** and reducing emissions of greenhouse gases in line with domestic as well as international targets – in particular through the Climate Change Levy and reduced VAT rates for energy saving materials;
- **improving air quality** to ensure that air pollutants are maintained below levels that could pose a risk to human health – including through support for cleaner fuels and vehicles;
- **improving waste management**, so that resources are used more efficiently and waste is re-used or recycled to deliver economic value – for example through increases in the landfill tax; and
- **protecting the UK's countryside and natural resources**, to ensure that they are sustainable economically, socially and physically – in particular by introducing the aggregates levy.

**Next steps I.31** The Government is committed to delivering sustainable growth, and a better environment and to tackling the global challenges of climate change. It is using a range of economic instruments to address the challenges posed by sustainable development, whilst taking into account other social and economic factors. The Pre-Budget report describes the next steps in the Government's strategy, focused on tackling the global challenge of climate change, including:

- encouraging energy efficiency in the business sector through **an increase in the climate change levy, in line with inflation, from 1 April 2007**;
- further measures to improve household energy efficiency, **including an extra 250,000 subsidised insulation measures in British homes over the next two years, funding for local authority-led publicity and incentive schemes, trialling the use of 'smart' gas and electricity meters, and a new voluntary initiative with major retailers to reduce the energy use of consumer electronics**;
- the development of a new **National Institute of Energy Technologies, in partnership with the private sector** to better leverage the substantial public sector funding of energy research;
- further support for the development of alternative energy sources, including **an additional £50 million to develop microgeneration technologies and the launch of a consultation document on the barriers to large-scale commercial deployment in the UK of carbon capture and storage**;

- **further detail on the Renewable Transport Fuel Obligation to increase the use of biofuels** – with the obligation set at 2.5 per cent in 2008-09 and 3.75 per cent in 2009-10, **and the biofuels duty incentive maintained at 20 pence per litre in 2008-09;**
- **reforms to vehicle excise duty (VED) to sharpen environmental incentives** including reducing the rate to zero for cars with the very lowest carbon emissions and introducing a new top band for the most polluting new cars. 50 per cent of cars will see their VED frozen or reduced;
- **the deferral to 1 September 2006 of the inflation-only increase in main road fuel duties, reflecting continuing volatility in the oil market; and a similar increase of 1.25 pence per litre, also from 1 September 2006, in duty for rebated fuels,** maintaining the differential with main fuel duty rates to support the Oils Strategy; and
- **a freeze in air passenger duty** due to the impact of volatile oil prices on the aviation industry, and funding for an international scientific conference in the UK that will look at the impact of aviation on climate change.

**I.32** The Budget also reports on the Government's strategy for tackling other environmental challenges, including:

- **an increase in the value of the landfill tax credit scheme to £60 million in 2006-07** with a challenge to the private and voluntary sector partners in the scheme to provide additional opportunities for young people to volunteer on environmental projects; and
- **a freeze in the rate of the aggregates levy.**

## BUDGET MEASURES AND THEIR IMPACT ON HOUSEHOLDS

**I.33** The measures introduced in this and previous Budgets support the Government's objectives of promoting enterprise, skills and science, creating employment opportunity, tackling child and pensioner poverty, and protecting the environment. Consistent with the requirements of the *Code for fiscal stability*, the updated public finance projections in Budget 2006 take into account the fiscal effects of all firm decisions announced in the Budget. The fiscal impact of Budget policy decisions is set out in Table 1.2. Full details are provided in Chapter A of the FSR.

**I.34** As a result of personal tax and benefit measures coming into effect in 2006–07, by October 2006, in real terms:<sup>1</sup>

- families with children will be, on average, £50 a year better off, while those in the poorest fifth of the population will be, on average, £100 a year better off;
- a single earner couple with 2 children, with earnings up to the median for full time workers – £24,000 per year – will be at least £70 a year better off; and
- a lone parent with 2 children, working 16 hours a week at the National Minimum Wage,<sup>2</sup> will be at least £315 per week better off.

<sup>1</sup> Compared to the 2005-06 system of taxes and benefits, indexed to 2006-07 prices.

<sup>2</sup> The National Minimum Wage will be £5.35 for adults from October 2006.

**I.35** As a result of personal tax and benefit measures introduced since 1997, by October 2006, in real terms:<sup>3</sup>

- households will be, on average, £950 a year better off;
- families with children will be, on average, £1,500 a year better off;
- families with children in the poorest fifth of the population will be, on average, £3,400 a year better off.

**I.36** As a result of personal tax and benefit measures introduced since 1997, in 2006-07:<sup>3</sup>

- pensioner households will be, on average £1,400 a year better off in real terms; and
- the poorest third of pensioner households will have gained £2,050 a year in real terms.

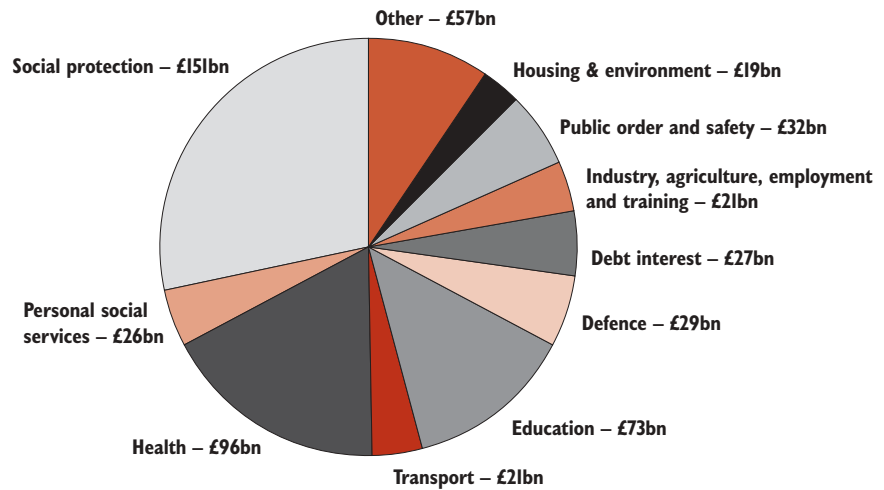
## GOVERNMENT SPENDING AND REVENUE

**I.37** Chart 1.1 presents public spending by main function. Total managed expenditure (TME) is expected to be around £552 billion in 2006-07. TME is divided into Departmental Expenditure Limits (DEL), shown in Table C13 of the FSBR, and Annually Managed Expenditure (AME), shown in Table C11 of the FSBR.

<sup>3</sup> Compared to the 1997-98 system of taxes and benefits, indexed to 2006-07 prices.

### Chart I.1: Government spending by function

Total managed expenditure: £552 billion

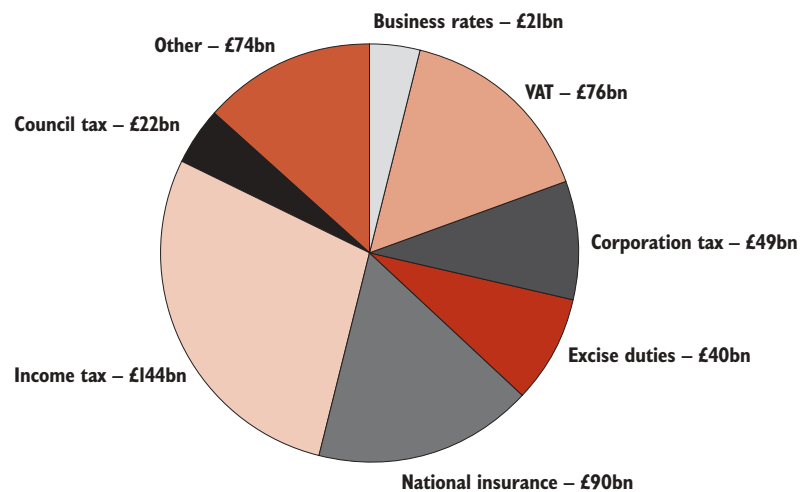


Source: HM Treasury, 2006-07 near-cash projections. Spending re-classified to functions compared to previous presentations and is now using methods specified in international standards. Other expenditure includes spending on general public services; recreation, culture, media and sport; international cooperation and development; public service pensions; plus spending yet to be allocated and some accounting adjustments. Social protection includes tax credit payments in excess of an individual's tax liability, which are now counted in AME, in line with OECD guidelines. Figures may not sum to total due to rounding.

**I.38** Chart 1.2 shows the different sources of government revenue. Public sector current receipts are expected to be around £516 billion in 2006-07. Table C8 of the FSR provides a more detailed breakdown of receipts consistent with this chart.

### Chart I.2: Government receipts

Total receipts: £516 billion



Source: HM Treasury, 2006-07 projections. Other receipts include capital taxes, stamp duties, vehicle excise duties and some other tax and non-tax receipts – for example, interest and dividends. Figures may not sum to total due to rounding.

Table 1.2: Budget 2006 policy decisions

	(+ve is an Exchequer yield)			£ million
	2006-07 indexed	2007-08 indexed	2008-09 indexed	2006-07 non-indexed
<b>MEETING THE PRODUCTIVITY CHALLENGE</b>				
1 Changes to venture capital schemes	*	-15	-15	*
2 Extending the scope of R&D tax credits	0	-15	-40	0
3 Real Estate Investment Trusts	+35	+155	+130	+35
<b>INCREASING EMPLOYMENT OPPORTUNITY FOR ALL</b>				
4 Work Focused Interviews for lone parents	0	-20	0	0
5 Doubling skills coaching pilots for women	-5	-5	0	-5
6 Expanding the National Employer Training Programme	-10	-10	0	-10
7 Matched funding for Sector Skill Councils	-5	-5	0	-5
<b>BUILDING A FAIRER SOCIETY</b>				
<b>Supporting families and communities</b>				
8 Income tax: indexation of starting and basic rate limits	0	0	0	-570
9 Child Tax Credit: uprating child element in line with earnings until 2009-10	0	0	-200	0
10 Employer-supported childcare	-10	-20	-25	-10
11 Inheritance tax: increase of threshold	0	0	-10	0
12 Stamp duty land tax: increase of threshold	-40	-30	-30	-40
<b>Protecting tax revenues</b>				
13 Financial products avoidance	+125	+135	+100	+125
14 VAT: Countering Missing Trader Fraud	+100	+500	+425	+100
15 Countering CGT avoidance	0	+40	+35	0
16 Avoidance using employment related securities	+70	+65	+45	+70
17 VAT: supplies of goods under finance agreements	*	+10	+15	*
18 Rebated oils: changes to excepted vehicles schedule	0	+10	+10	0
<b>Duties and other tax changes</b>				
19 Alcohol duties: freeze spirits, cider and sparkling wine, revalorise beer and wine duties	-35	-30	-30	+170
20 Tobacco duties: revalorise rates	0	0	0	+25
21 VAT: reduced rate for contraceptive products	-5	-10	-10	-5
22 Further changes to oil valuation for tax purposes	+40	+80	+80	+40
23 Changes to group relief in corporation tax	-50	-50	-50	-50
24 Film tax reliefs: expanding the scope	*	-10	-10	*
25 Stamp duty land tax: ending relief for initial transfers into unit trusts	+50	+50	+40	+50
26 Removal of income tax exemption for loaned computers	+50	+100	+150	+50
27 Aligning the inheritance tax treatment for trusts	0	+15	+15	0
<b>PROTECTING THE ENVIRONMENT</b>				
<b>Environment</b>				
28 Climate change levy: revalorise from 1 April 2007	-20	-20	-20	0
29 Climate change levy: exemption of gas used in Northern Ireland	*	*	-5	*
30 Aggregates levy: freeze	-10	-10	-10	0
31 Enhanced Capital Allowances for water efficient technologies	*	-5	-5	*
32 Increasing the landfill tax credit scheme	-10	-10	-10	-10
<b>Transport</b>				
33 VAT: revalorise fuel scale charges	0	0	0	+10
34 Company car tax thresholds	-10	-20	+25	-10
35 Fuel duties: revalorise rates from 1 September 2006	-275	0	0	+380

**Table I.2: Budget 2006 policy decisions**

	(+ve is an Exchequer yield)			£ million
	2006-07 indexed	2007-08 indexed	2008-09 indexed	2006-07 non-indexed
36 Fuel duties: maintain differential for rebated oils from 1 September 2006	+40	+75	+80	+50
37 Fuel duties: maintain differential for biodiesel and bioethanol until 2008	*	0	+10	0
38 Fuel duties: maintain differential for road fuel gases	*	0	+5	*
39 Vehicle Excise Duties: enhancing environmental incentives	+5	+5	+5	+115
40 Other VED changes	0	+20	+35	+10
41 Air passenger duty: freeze	-10	-30	-30	0
<b>OTHER POLICY DECISIONS</b>				
42 Supporting further education reform	0	-55	0	0
43 Direct payments to schools	-270	-440	0	-270
44 Additional Police Community Support Officers	-100	0	0	-100
45 2012 Olympics: supporting elite athletes	-30	-35	0	-30
<b>TOTAL POLICY DECISIONS</b>	<b>-380</b>	<b>+415</b>	<b>+705</b>	<b>+115</b>
<i>* negligible</i>				
<b>MEMO ITEMS</b>				
Resetting of the AME margin	-90	+200		

