C THE PUBLIC FINANCES

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 since the start of the current economic cycle in 1997-98 shows an annual average surplus up to 2008-09 of 0.1 per cent of GDP, showing the Government is meeting the golden rule on the basis of cautious assumptions. The average annual current surplus from 2008-09 to the end of the forecast period is about 0.7 per cent of GDP; and**
- **public sector net debt is projected to be low and stable over the forecast period stabilising at around 38½ per cent of GDP, below the 40 per cent ceiling set in the sustainable investment rule.**

INTRODUCTION

C.1 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.

C.2 The fiscal projections continue to be based on deliberately cautious key assumptions audited by the National Audit Office (NAO).

MEETING THE FISCAL RULES

C.3 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 cyclically-adjusted fiscal balances, are also shown.

Table C1: Summary of public sector finances

	Per cent of GDP							
	Outturns		Estimate	Projections				
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Fairness and prudence								
Surplus on current budget	-1.9	-1.6	-0.9	-0.6	0.1	0.5	0.7	0.8
Average surplus since 1997-1998	0.5	0.2	0.1	0.0	0.0	0.1	0.1	0.2
Cyclically-adjusted surplus on current budget	-1.4	-1.3	-0.3	0.4	0.7	0.7	0.7	0.8
Long-term sustainability								
Public sector net debt[1]	33.2	35.0	36.4	37.5	38.1	38.3	38.4	38.4
Core debt[1]	32.8	34.3	35.2	35.4	35.5	35.7	35.9	36.0
Net worth[2]	28.5	29.0	26.0	24.8	23.3	22.9	22.9	22.8
Primary balance	-1.6	-1.7	-1.3	-1.1	-0.5	-0.1	0.1	0.1
Economic impact								
Net investment	1.3	1.8	2.1	2.2	2.3	2.3	2.3	2.3
Public sector net borrowing (PSNB)	3.2	3.4	3.0	2.8	2.2	1.7	1.6	1.5
Cyclically-adjusted PSNB	2.7	3.0	2.4	1.9	1.6	1.6	1.6	1.5
Financing								
Central government net cash requirement	3.5	3.3	3.2	3.2	2.6	2.1	2.1	1.8
Public sector net cash requirement	3.5	3.3	3.0	2.9	2.4	1.8	1.8	1.5
European commitments								
Treaty deficit[3]	3.1	3.3	3.2	3.0	2.4	1.9	1.7	1.6
Cyclically-adjusted Treaty deficit[3]	2.6	2.9	2.5	2.0	1.8	1.7	1.7	1.7
Treaty debt ratio[4]	39.5	40.8	42.6	43.9	44.5	44.5	44.5	44.5
Memo: Output gap	-0.6	-0.4	-1.2	-1.4	-0.7	-0.1	0.0	0.0

[1] Debt at end March; GDP centred on end March.
[2] Estimate at end December; GDP centred on end December.
[3] General government net borrowing on a Maastricht basis.
[4] General government gross debt measures on a Maastricht basis.

The golden rule

C.4 The projections show that the Government is meeting the golden rule, on the basis of cautious assumptions, with an average annual surplus on the current budget over this economic cycle of around 0.1 per cent of GDP. On this basis, and based on cautious assumptions, the Government is meeting the golden rule and there is a margin against the golden rule of £16 billion in this cycle, including the Annually Managed Expenditure (AME) margin. The cyclically-adjusted surplus, which allows underlying or structural trends in the public finances to be seen more clearly by removing the estimated effects of the economic cycle, shows a small deficit in 2005-06, but a surplus of 0.4 per cent of GDP in 2006-07 and higher surpluses from 2007-08 onwards.

C.5 The economy is projected to return to trend in 2008-09. With the economy assumed to be on trend from then on, the projections show, based on cautious assumptions, that the average surplus over the period 2008-09 to 2010-11 is 0.7 per cent of GDP. At this early stage, and based on cautious assumptions, the Government will therefore continue to meet the golden rule after the end of this cycle.

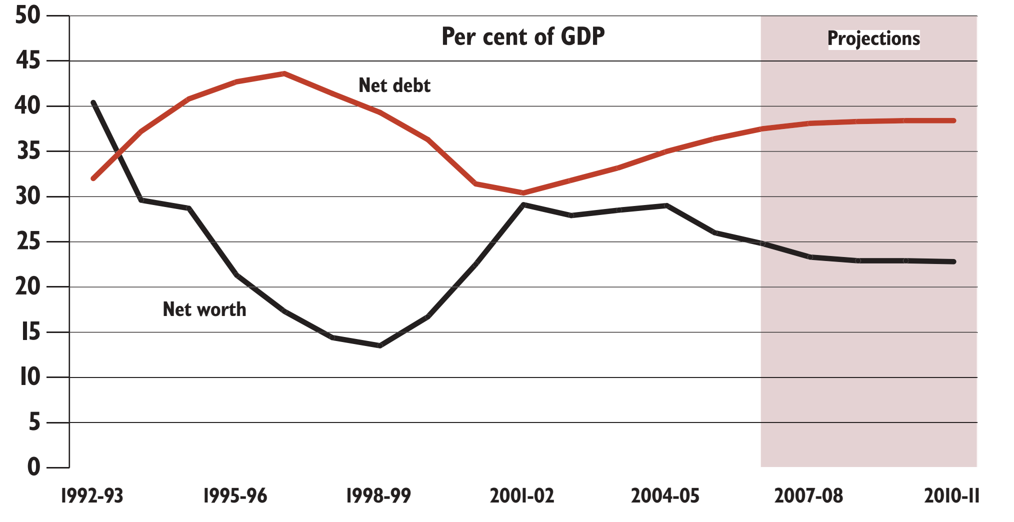
The sustainable investment rule

C.6 The sustainable investment rule is also met over the 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 licenses to repay debt, reduced debt to around 30 per cent of GDP by the end of 2001-02. It is now projected to grow slowly, as the Government borrows modestly to fund increased investment in public services, reaching around 38½ per cent of GDP by the end of the economic cycle, and stabilising at that level for the remainder of the forecasting period. The projections for core debt, which exclude the estimated impact of the economic cycle, rise 36 per cent of GDP. This is consistent with the fiscal rules, and with the key objective of intergenerational fairness that underpins the fiscal framework.

Net worth **C.7** Net worth is the approximate stock counterpart of the current budget. Modest falls in net worth are expected for the remainder of the projection period from the high level of 29 per cent of GDP in 2004-05. At present, net worth is not used as a key indicator of the public finances, mainly as a result of the difficulties involved in accurately measuring many government assets and liabilities.

C.8 Chart C1 shows public sector net debt and net worth as a per cent of GDP from 1992-93 to 2010-11.

Chart C1: Public sector net debt and net worth



Net investment **C.9** As a result of decisions taken in the 2004 Spending Review public sector net investment is projected to rise from 1.1 per cent of GDP in 2002-03 to $2^1/_4$ per cent from 2006-07 onwards. This increase is 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, below 40 per cent of GDP.

Net borrowing **C.10** Public sector net borrowing is expected to fall in every year of the forecast period from 3.4 per cent of GDP in 2004-05 to 3.0 per cent in 2005-06, and then to a level of $1^1/_2$ per cent of GDP by 2010-11.

Financing **C.11** The central government net cash requirement was 3.3 per cent of GDP in 2004-05. It is projected to be around 3.2 per cent in 2005-06, and falls to 1.8 per cent of GDP by 2010-11, mirroring the profile of net borrowing.

European commitments **C.12** Table C1 shows the Treaty measures of debt and deficit used for the purposes of the Excessive Deficit Procedure - Article 104 of the Treaty. The public finance projections set out in Budget 2006, which show the Government is meeting its fiscal rules over the cycle, maintaining low debt and sustainable public finances, combined with sustainable increases in public investment, are fully consistent with a prudent interpretation of the Pact. The projections meet the EU Treaty reference value for general government gross debt (60 per cent of GDP) by a considerable margin. In addition, the cyclically-adjusted level of general government net borrowing is 2.5 per cent of GDP in 2005-06 and is at 2 per cent of GDP or below from 2006-07 onwards.

CHANGES TO THE FISCAL BALANCES

C.13 Table C2 compares the latest estimates for the main fiscal balances with those in Budget 2005 and in the 2005 Pre-Budget Report.

Table C2: Fiscal balances compared with Budget 2005 and the 2005 Pre-Budget Report

	Outturn[1]	Estimate[2]	Projections				
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Surplus on current budget (£ billion)							
Budget 2005	-16.1	-5.7	1	4	9	12	
Effect of revisions and forecasting changes	*-3.8*	*-4.2*	*-6 1/2*	*-6 1/2*	*-5*	*-3 1/2*	
Effect of discretionary changes	*0.0*	*-0.8*	*2*	*2 1/2*	*2 1/2*	*2*	
PBR 2005	-19.9	-10.6	-4	0	7	11	13
Effect of revisions and forecasting changes	*0.9*	*-0.8*	*-2 1/2*	*1/2*	*0*	*-1*	*-1 1/2*
Effect of discretionary changes	*0.0*	*0.0*	*- 1/2*	*1/2*	*1*	*1/2*	*1/2*
Budget 2006	**-19.0**	**-11.4**	**-7**	**1**	**7**	**10**	**12**
Net borrowing (£ billion)							
Budget 2005	34.4	31.9	29	27	24	22	
Changes to current budget	*3.8*	*4.9*	*5*	*4*	*2 1/2*	*1 1/2*	
Changes to net investment	*0.6*	*0.1*	*0*	*0*	*0*	*0*	
PBR 2005	38.8	37.0	34	31	26	23	22
Changes to current budget	*-0.9*	*0.8*	*3*	*-1*	*- 1/2*	*1/2*	*1*
Changes to net investment	*1.7*	*-0.6*	*- 1/2*	*- 1/2*	*0*	*0*	*0*
Budget 2006	**39.7**	**37.1**	**36**	**30**	**25**	**24**	**23**
Cyclically-adjusted surplus on current budget (per cent of GDP)							
Budget 2005	-0.8	-0.3	0.1	0.3	0.6	0.8	
PBR 2005	-1.3	-0.1	0.7	0.7	0.7	0.7	0.8
Budget 2006	**-1.3**	**-0.3**	**0.4**	**0.7**	**0.7**	**0.7**	**0.8**
Cyclically-adjusted net borrowing (per cent of GDP)							
Budget 2005	2.4	2.4	2.2	2.0	1.6	1.5	
PBR 2005	2.9	2.2	1.6	1.6	1.6	1.5	1.4
Budget 2006	**3.0**	**2.4**	**1.9**	**1.6**	**1.6**	**1.6**	**1.5**
Net debt (per cent of GDP)							
Budget 2005	34.4	35.5	36.2	36.8	37.1	37.1	
PBR 2005	34.7	36.5	37.4	37.9	38.2	38.2	38.2
Budget 2006	**35.0**	**36.4**	**37.5**	**38.1**	**38.3**	**38.4**	**38.4**

[1] *The 2004-05 figures were estimates in Budget 2005.*
[2] *The 2005-06 figures were projections in Budget 2005.*

Changes between Budget 2005 and the 2005 Pre-Budget Report

C.14 In the 2005 Pre-Budget Report, the current budget was revised down by £$3^3/_4$ billion in 2004-05 and by around £5 billion a year in 2005-06 and 2006-07. The revisions were smaller in subsequent years and the current balance returned to surplus in 2007-08.

C.15 These revisions were mainly due to a combination of higher expenditure and lower receipts in 2004-05 and to lower projections of receipts, especially non-North sea corporation tax and VAT for 2005-06 onwards. However, these shortfalls were lower than would have been expected given changes in the level of money GDP and its components, partly because of higher receipts from North Sea taxes and partly because of the strong performance of the financial sector, which was not affected by slower economic growth in the same way as the rest of the economy.

C.16 Discretionary changes, including a further addition to the special reserve to meet the cost of military operations in Iraq and the UK's other international obligations, led to a further reduction in the current budget in 2005-06. For 2006-07 onwards, discretionary changes led to improvements in the current budget as changes to the North Sea oil taxation regime and further measures to combat tax fraud and avoidance more than offset extra spending on winter fuel payments for pensioners.

Changes between the 2005 Pre-Budget Report and Budget 2006

C.17 The Budget 2006 projections are broadly in line with those in the Pre-Budget Report, locking in the Government's prudent stance. The estimated outturn for the public sector current balance for 2005-06 is a deficit of £11.4 billion, compared with a deficit of £10.6 billion in the Pre-Budget Report, and the deficit is also higher in 2006-07. In later years there are only small changes in the current balance which returns to surplus in 2007-08.

C.18 The reclassification of the BBC as part of central government has no impact on overall public sector balances, but has led to higher projections of both receipts and expenditure than in the Pre-Budget Report. Other than this, overall receipts in 2005-06 are slightly above the Pre-Budget report projections, but current expenditure is now slightly higher, leading to the slightly larger deficit on the current balance. The expenditure increase in 2005-06 is broadly offset by reductions in subsequent years and the higher deficit on the current balance in 2006-07 arises from lower receipts projections, largely because of changes to economic determinants affecting North Sea tax revenues. There are only small forecasting changes to overall receipts in subsequent years.

C.19 Although public sector net investment in 2005-06 is projected to show growth of 24 per cent on 2004-05, the estimated outturn is now expected to be about £$^1/_2$ billion lower in 2005-06 than expected in the Pre-Budget Report. This largely offsets the change to the current balance and public sector net borrowing in 2005-06 is £37.1 billion, only very slightly higher than in the Pre-Budget Report. Net investment is also expected to be slightly lower than projected in the Pre-Budget Report in 2006-07 and 2007-08, and the path of public sector net borrowing is broadly in line with the Pre-Budget Report.

C.20 Discretionary changes include a commitment to increase the child element of the Child Tax Credit in line with average earnings to the end of this parliament, the introduction of Real Estate Investment Trusts, measures to modernise the tax system and to tackle tax fraud and avoidance, as well as other budget policy decisions. They also include resetting the AME margin.

FORECAST DIFFERENCES AND RISKS

C.21 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 2003 and Budget 2004, and the subsequent outturns were provided in the *End of year fiscal report*, published alongside the 2005 Pre-Budget Report.

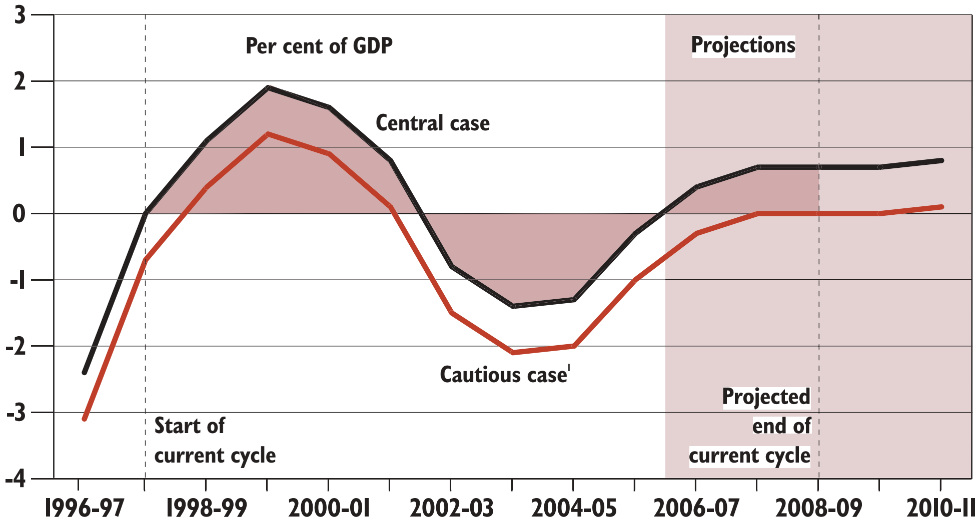
C.22 Overall, the economic forecast is unchanged from the 2005 Pre-Budget Report. Following growth of 1$^3/_4$ per cent in 2005, UK GDP is expected to grow by between 2 and 2$^1/_2$ per cent this year, still slightly below trend rates, reflecting a number of temporary factors. Private consumption growth is expected to be restrained by continued household appetite for saving, subdued growth in labour incomes, and the residual effects of higher energy prices. In the corporate sector, higher oil prices and high levels of gearing are likely to restrain the growth of business investment this year.

C.23 The set of risks surrounding the Budget 2006 economic outlook is similar to those surrounding the 2005 Pre-Budget Report forecast. The balance of risks has shifted a little, with domestic risks having receded while global uncertainties have increased somewhat. Globalisation means that the UK economy shares increasingly in the risks affecting the world economy and means that domestic risks are harder to differenciate.

C.24 The forecast for private consumption continues to be surrounded by both upside and downside risks. Further unexpected weakness of average earnings growth would tend to undermine household expenditure, although the boost to employment from weakening labour costs would tend at least partly to offset this affect.

C.25 A second important source of potential errors results from misjudging the position of the economy in relation to trend output. To minimise this risk, the robustness of the projections is tested against an alternative scenario in which the level of trend output is assumed to be one percentage point lower than in the central case. Chart C2 illustrates the Budget projection for this cautious case.

Chart C2: Cyclically-adjusted surplus on current budget



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

C.26 The Government has used the cautious case and cautious, audited assumptions to build a safety margin against unexpected events. This was combined with the decision to consolidate the public finances when the economy was above trend, which resulted in low debt. This has allowed the Government to safeguard the increase in investment in priority public services, allow the automatic stabilisers to work in full during the period of global economic uncertainty in the early part of the decade and meet in full the UK's international commitments, while continuing to meet the fiscal rules.

ASSUMPTIONS

C.27 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 $2^1/_2$ per cent up to 2006-07, $^1/_4$ percentage point lower than the Government's neutral view. The Government's neutral view of trend output is reduced to $2^1/_2$ per cent between

2007-08 and 2010-11, and so, to maintain a cautious approach, an assumption of $2^1/_4$ per cent is used in the public finances projections, still a $^1/_4$ percentage point lower than the Government's neutral view;

- there are no tax or spending policy 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 proposed in this Budget for consultation or other proposals where final decisions have yet to be taken, such as further extensions to maternity and paternity leave and the replacement of the current system of incapacity benefits;
- firm Departmental Expenditure Limits (DEL) as set out in the 2004 Spending Review up to 2007-08, but adjusted for the impact of policy decisions and reclassifications;
- total AME programmes to 2007-08 have been reviewed. The total has been adjusted for reclassification changes and for the cost of spending measures in this Budget. In accordance with normal practice the Government has decided to reset the AME margin to £1 billion in 2006-07 and to £2 billion in 2007-08;
- as is normal, the Treasury is setting out its assumption for public sector current expenditure for the period beyond the current Spending Review. Public sector current expenditure is forecast to grow by 2.0 per cent in real terms in 2008-09 and by 1.9 per cent in 2009-10 and 2010-11. This means that, on average, public sector current expenditure is forecast to grow by $2^1/_4$ per cent a year in real terms over the forecast period 2006-07 to 2010-11; and
- net investment is assumed to remain at $2^1/_4$ per cent of GDP in 2008-09 and subsequent years.

Table C3: Economic assumptions for the public finance projections

	Percentage changes on previous year						
	Outturn	Estimate	Projections				
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Output (GDP)	2 3/4	1 3/4	2 1/4	3	2 3/4	2 1/4	2 1/4
Prices							
CPI	1 1/2	2	2	2	2	2	2
GDP deflator	2 1/4	2	2 1/2	2 3/4	2 3/4	2 3/4	2 3/4
RPI[1] (September)	3	2 3/4	2 3/4	3	3	2 3/4	2 3/4
Rossi[2] (September)	1 1/4	2	2 1/4	2 1/4	2 1/4	2 1/4	2 1/4
Money GDP[3] (£ billion)	1,178	1,224	1,281	1,353	1,428	1,499	1,573

[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.*

C.28 The forecasts for different inflation indices are based on the conventional assumptions about the interrelationships between them. But, as in Chapter B notes, these relationships can change over time and are kept under review.

C.29 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.

Box C1: Key assumptions audited by the NAO[a]

• Dating of the cycle[e]	The end date of the previous economic cycle was in the first half of 1997.
• Privatisation proceeds[f]	Credit is taken only for proceeds from sales that have been announced.
• Trend GDP growth[f]	$2\frac{1}{2}$ per cent a year to 2006 and $2\frac{1}{4}$ per cent in subsequent years.
• UK claimant unemployment[d]	Rising slowly to 0.97 million in 2007-08, from recent levels of 0.91 million.
• Interest rates[f]	3-month market rates change in line with market expectations (as of 10 March).
• Equity prices[b]	FTSE All-share index rises from 3004 (close 10 March) in line with money GDP.
• VAT[b,c,e]	The VAT gap will rise by 0.5 percentage points per year from a level that is at least as high as the estimated outturn for the current year.
• Consistency of price indices[b]	Projections of price indices used to project the public finances are consistent with CPI.
• Composition of GDP[c]	Shares of labour income and profits in national income are broadly constant in the medium term.
• Funding[c]	Funding assumptions used to project debt interest are consistent with the forecast level of government borrowing and with financing policy.
• Oil prices[e]	\$57.4 a barrel in 2006, the average of independent forecasts, and then constant in real terms.
• Tobacco[f]	The underlying market share of smuggled cigarettes will be set at least at the latest published outturn. For Budget 2006, a share of 16 per cent is used for 2006-07 onwards.

[a] For details of all NAO audits before the 2003 Pre-Budget Report, see Budget 2003, 9 April 2003 (HC500).
[b] Audit of Assumptions for the 2003 Pre-Budget Report, 10 December 2003 (HC35).
[c] Audit of Assumptions for the Budget 2004, 17 March 2004 (HC434).
[d] Audit of Assumptions for the Budget 2005, 16 March 2005 (HC452).
[e] Audit of Assumptions for the 2005 Pre-Budget Report, 5 December 2005 (HC707).
[f] Audit of Assumptions for the Budget 2006. 22 March 2006 (HC937).

The audited assumptions

C.30 For this Budget, the Comptroller and Auditor General has audited the assumption for underlying trend growth used for the purpose of projecting the public finances, which is set a $\frac{1}{4}$ percentage point below the Government's neutral view. The review concluded that over the past four years the assumption has been reasonable and cautious, though other assumptions could have been adopted that would have introduced a greater degree of caution. Looking forward, the review concluded that the assumption currently remains reasonable and cautious but recommended that, because of the uncertainties involved in estimating trend growth rates, the Treasury kept its estimate under review.

C.31 The assumption for forecasting revenue from duty on tobacco, that the illicit market share is set at least at the latest published outturn level, would normally be due for review under the three-year rolling review. However, firm data for the illicit market share is currently only available for the first year of the rolling review period so that it is not possible to reach a conclusion for the three-year period as a whole. The Comptroller and Auditor General has therefore reviewed the evidence for 2003-04, concluding that the assumption had added caution to the fiscal projections in that year, and reviewed the issues that have arisen in producing an estimate for 2004-05. The Comptroller and Auditor General recommended areas of further analysis that HM Revenue and Customs (HMRC) will undertake over the next year and will be invited to conduct a full review at Budget 2007.

C.32 The Comptroller and Auditor General reviewed the yield from the Budget 2003 direct taxation compliance package and found that the projections of yield were reasonable and the method adopted to make adjustments to the projections in the light of outturn evidence was a helpful one to ensure caution.

C.33 The Comptroller and Auditor General also audited the conventions on short-term interest rates and privatisation proceeds. He concluded that the interest rate assumption methodology that three-month forward interest rates will be based on market expectations, was a reasonable one and incorporates an element of caution through the risk premium embodied in the forward rates. Over the past three years interest rate projections had been higher than outturn more often than not, and so been cautious to this extent, on the basis that higher interest rates have a negative impact on the public finances. The review concluded that the convention on privatisation proceeds had led to no systematic forecasting errors over the review period and that for the future it remains reasonable and is based on being cautious. In view of potentially large future privatisation receipts, close attention should be paid to the profile of receipts included in the fiscal projections.

C.34 Consistent with the *Code for fiscal stability*, the forecast does not take into account impact of the finance leases on public sector net debt, as the impact cannot be accurately estimated. The Office for National Statistics (ONS) is undertaking a programme of work to quantify the impact of these finance leases and is planning to issue the first estimates in mid-2006.

Box C2: Trend growth and caution in the public finances

Since 1997 the NAO has audited key assumptions underlying the public finance projections to ensure that they are consistent with the principles of transparency and responsibility. The key source of caution in the fiscal projections is the trend growth assumption, which has been audited by the NAO alongside Budget 2006.

The cautious trend growth assumption holds the annual growth of real non-oil GVA to a ¼ percentage point below the Government's neutral view of growth. As a result, the rate of economic growth used to forecast the public finances is at the bottom end of the projection range for GDP growth, as shown in the table below. Once the output gap has been closed in 2008-09, output - for the purposes of the public finance projections - grows at the trend rate of 2¼ per cent.

Table GDP growth (per cent)

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Neutral[1]	1¾	2¼ to 2¾	3 to 3½	2¾ to 3¼	2¼ to 2¾	2¼ to 2¾
For public finances	1¾	2¼	3	2¾	2¼	2¼

[1] The neutral GDP growth forecast is the same as that in Table 2.2 and B3. In this Table it is presented for financial years, but in Table 2.2 and B3 it is presented for calendar years. See footnote to table B9 for explanation of forecast ranges.

With lower growth in each year of the five-year projection period, the level of money GDP becomes progressively more cautious. The NAO-audited assumption on the composition of GDP – that labour income and profits receive broadly constant shares of GDP - ensures that the impact of the cautious trend growth rate feeds through equally to wages and salaries, the key determinant of income tax, and corporate profits, the key determinant of corporation tax. The NAO-audited equity price assumption, that the stock market rises in line with nominal GDP, ensures that equity prices, too, are constrained by the cautious trend growth assumption.

In the projections in Budget 2006, money GDP is around £19 billion lower in the public finance projection than the neutral view by 2010-11, with a direct feed-through in terms of lower wages and salaries and lower non-North Sea profits. In terms of the Budget receipts forecast, the effect of using the cautious trend growth assumption rather than the neutral view is to reduce the level of tax receipts in 2010-11 by between £6 billion and £8 billion.

FISCAL AGGREGATES

C.35 Tables C4 and C5 provide more detail on the projections for the current and capital budgets.

Table C4: Current and capital budgets

	Outturn	Estimate			Projections		
£billion	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Current budget							
Current receipts	451.3	486.1	516	553	585	615	645
Current expenditure	455.4	481.9	507	534	559	585	612
Depreciation	15.0	15.6	17	18	19	20	21
Surplus on current budget	**-19.0**	**-11.4**	**-7**	**1**	**7**	**10**	**12**
Capital budget							
Gross investment	41.9	47.9	52	55	57	60	63
Less asset sales	-6.3	-6.6	-7	-7	-7	-7	-7
Less depreciation	-15.0	-15.6	-17	-18	-19	-20	-21
Net investment	20.7	25.7	29	31	32	34	36
Net borrowing	**39.7**	**37.1**	**36**	**30**	**25**	**24**	**23**
Public sector net debt - end year	**419.8**	**455.8**	**493**	**530**	**560**	**590**	**619**
Memos:							
Treaty deficit[1]	38.5	38.6	38	32	27	26	26
Treaty debt[2]	480.4	520.9	563	602	635	668	700

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

Table C5: Current and capital budgets

	Outturn	Estimate			Projections		
Per cent of GDP	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Current budget							
Current receipts	38.3	39.7	40.3	40.9	41.0	41.0	41.0
Current expenditure	38.7	39.4	39.6	39.5	39.2	39.0	38.9
Depreciation	1.3	1.3	1.3	1.3	1.3	1.3	1.3
Surplus on current budget	**-1.6**	**-0.9**	**-0.6**	**0.1**	**0.5**	**0.7**	**0.8**
Capital budget							
Gross investment	3.6	3.9	4.1	4.1	4.0	4.0	4.0
Less asset sales	-0.5	-0.5	-0.5	-0.5	-0.5	-0.4	-0.4
Less depreciation	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3
Net investment	1.8	2.1	2.2	2.3	2.3	2.3	2.3
Net borrowing	**3.4**	**3.0**	**2.8**	**2.2**	**1.7**	**1.6**	**1.5**
Public sector net debt - end year	**35.0**	**36.4**	**37.5**	**38.1**	**38.3**	**38.4**	**38.4**
Memos:							
Treaty deficit[1]	3.3	3.2	3.0	2.4	1.9	1.7	1.6
Treaty debt ratio[2]	40.8	42.6	43.9	44.5	44.5	44.5	44.5

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

C.36 Following a deficit of 3 per cent of GDP in 1996-97, current budget surpluses of more than 2 per cent were recorded in 1999-00 and 2000-01. These surpluses allowed the Government to use fiscal policy to support monetary policy during the economic slowdown in 2001 and 2002, and as a result the current budget moved into deficit. The current budget is expected to remain in deficit until 2006-07 and then move back into surplus in 2007-08, with increasingly larger surpluses in later years, reaching 0.7 per cent of GDP in 2010-11.

C.37 The current budget surplus is equal to public sector current receipts minus public sector current expenditure and depreciation. The reasons for changes in receipts and current expenditure are explained in later sections.

C.38 Table C4 also shows that net investment is projected to increase from £21 billion in 2004-05 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 38.4 per cent of GDP or less throughout the projection period, within the 40 per cent limit set by the sustainable investment rule.

RECEIPTS

C.39 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 2005 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 2005 Pre-Budget Report

C.40 Table C6 provides a detailed breakdown of the main factors that have led to the changes in the overall projections since the 2005 Pre-Budget Report.

Table C6: Changes in current receipts since the 2005 Pre-Budget Report

	£ billion					
	Estimate	Projections				
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Effect on receipts of non-discretionary changes in:						
Assumptions audited by the NAO	0	1	2	1 1/2	1 1/2	1 1/2
Other economic determinants	0	-2	- 1/2	0	0	0
Other forecasting changes	3	1/2	1	1 1/2	1/2	1/2
Total before discretionary changes[1]	**3**	**0**	**2 1/2**	**3**	**2 1/2**	**2**
Discretionary changes[2]	0	0	1	1	1	1/2
Total change[1]	**3**	**0**	**3 1/2**	**4 1/2**	**3 1/2**	**2 1/2**

[1] *Total may not sum due to rounding.*
[2] *Includes measures announced since the 2005 Pre-Budget Report.*

Economic determinants audited by the NAO

C.41 Changes in economic determinants audited by the NAO increase current receipts by £1 billion in 2006-07 and by around £1½ to £2 billion thereafter. The main effect is from a higher projection for equity prices. The climb in the UK stock market since the Pre-Budget Report has raised the starting point for the equity price assumption, by around 8 per cent. Higher equity prices boost capital and stamp taxes and receipts of corporation tax paid by life assurance companies. There is also a smaller effect from higher dollar oil prices, which are $1.40 a barrel higher in 2006 than in the Pre-Budget Report. This increases North Sea revenues.

Other economic determinants **C.42** Other economic determinants reduce current receipts by £1$^{3}/_{4}$ billion in 2006-07 relative to the 2005 Pre-Budget Report but have little overall effect on receipts thereafter. Recent labour market developments mean that growth in the wage and salary bill is likely to be more modest than previously anticipated during 2006-07. There is also likely to be a marked effect on North Sea revenues in 2006-07 from lower than expected oil production and higher than anticipated capital expenditure. From 2007-08, these factors have little impact on North Sea revenues, while there are positive impacts on receipts from non-North Sea corporation tax determinants and from equity volumes on stamp duty and capital gains tax.

Fiscal forecasting changes **C.43** There are a number of other forecasting changes. The ONS reclassification of the BBC to the central government sector from the public corporations sector means TV licences are now included as receipts and boosts the level of current receipts throughout the forecast. The change is however fiscally neutral. Other factors include the impact of recent outturn data, not explained by economic factors, the impact of the smoking ban in enclosed workplaces and the lower projections for VAT refunds and council tax which are broadly fiscally neutral.

Tax-by-tax analysis

C.44 Table C7 shows the changes to the projections of individual taxes since Budget 2005 and the 2005 Pre-Budget Report for 2005-06 and 2006-07. Table C8 contains updated projections for the main components of public sector receipts for 2004-05, 2005-06 and 2006-07.

Table C7: Changes in current receipts by tax since Budget 2005 and the 2005 Pre-Budget Report

	£ billion			
	Budget 2005		PBR 2005	
	2005-06	2006-07	2005-06	2006-07
Income tax (gross of tax credits)	-2.1	-3.6	0.1	-0.7
Income tax credits	-0.7	-1.0	-0.1	-0.3
National insurance contributions	2.8	2.4	1.2	0.8
Non-North Sea corporation tax[1]	-3.1	-4.0	0.2	0.1
North Sea revenues	2.6	3.3	0.6	-1.5
Capital taxes[2]	-0.3	0.3	0.0	0.3
Stamp duty	1.2	1.7	0.7	0.8
Value added tax	-2.7	-3.6	-0.7	-0.8
Excise duties[3]	-1.8	-2.5	-0.8	-0.8
Other taxes and royalties[4]	0.9	-0.5	-0.5	-1.7
Net taxes and national insurance contributions	**-3.1**	**-7.5**	**0.7**	**-3.8**
Other receipts and accounting adjustments	2.5	3.6	2.4	3.6
Current receipts	**-0.6**	**-4.0**	**3.1**	**-0.2**

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

Table C8: Current receipts

	£ billion		
	Outturn 2004-05	Estimate 2005-06	Projection 2006-07
HM Revenue and Customs			
Income tax (gross of tax credits)	127.2	136.0	144.0
Income tax credits	-4.3	-4.7	-4.6
National insurance contributions	78.1	85.4	89.6
Value added tax	73.0	73.7	76.5
Corporation tax[1]	34.1	42.7	49.0
Corporation tax credits[2]	-0.5	-0.5	-0.6
Petroleum revenue tax	1.3	2.0	1.9
Fuel duties	23.3	23.5	24.0
Capital gains tax	2.3	2.9	3.8
Inheritance tax	2.9	3.2	3.6
Stamp duties	9.0	10.9	12.2
Tobacco duties	8.1	8.0	8.0
Spirits duties	2.4	2.3	2.3
Wine duties	2.2	2.3	2.4
Beer and cider duties	3.3	3.3	3.4
Betting and gaming duties	1.4	1.4	1.4
Air passenger duty	0.9	0.9	1.0
Insurance premium tax	2.4	2.3	2.4
Landfill tax	0.7	0.7	0.8
Climate change levy	0.8	0.7	0.7
Aggregates levy	0.3	0.3	0.3
Customs duties and levies	2.2	2.2	2.2
Total HMRC	**371.1**	**399.8**	**424.4**
Vehicle excise duties	4.7	5.0	5.1
Business rates	18.7	20.3	21.4
Council tax[3]	20.1	21.0	22.0
Other taxes and royalties[4]	11.7	12.8	13.6
Net taxes and national insurance contributions[5]	**426.5**	**458.7**	**486.5**
Accruals adjustments on taxes	1.4	2.3	2.3
Less own resources contribution to European Union (EU) budget	-4.1	-4.3	-4.2
Less PC corporation tax payments	-0.1	-0.1	-0.1
Tax credits adjustment[6]	0.5	0.6	0.6
Interest and dividends	5.5	5.3	5.7
Other receipts[7]	21.6	23.5	25.6
Current receipts	**451.3**	**486.1**	**516.4**
Memo:			
North Sea revenues[8]	5.2	9.7	10.2

[1] National accounts measure: gross of enhanced and payable tax credits.
[2] Includes enhanced company tax credits.
[3] Council tax increases are determined annually by local authorities, not by the Government. As in previous years, council tax figures are projections based on stylised assumptions and are not Government forecasts.
[4] Includes VAT refunds and money paid into the National Lottery Distribution Fund.
[5] Includes VAT and 'traditional own resources' contributions to EU budget.
[6] Tax credits which are scored as negative tax in the calculation of NTNIC but expenditure in the national accounts.
[7] Includes gross operating surplus and rent; net of oil royalties and business rate payments by Local Authorities.
[8] Consists of North Sea corporation tax, petroleum revenue tax and royalties.

Income tax and national insurance contributions

C.45 Income tax and National Insurance Contributions (NICs) in 2005-06 are expected to be around £1.2 billion above the 2005 Pre-Budget Report projection. The rise is primarily in NICs, in part reflecting lower personal pension rebates. There has also been a reallocation of receipts from income tax to NICs since the 2005 Pre-Budget Report. Self-assessment receipts are likely to be close to the level assumed in the 2005 Pre-Budget Report forecast, although more of the receipts scored in January rather than February compared with last year.

C.46 Pay-As-You-Earn (PAYE) and NICs receipts from wages and salaries are lower than anticipated in the 2005 Pre-Budget Report, reflecting recent average earnings and employment data. However, the impact from whole economy labour market developments on PAYE and NICs receipts has been partly offset by continued high receipts from the financial sector, which has a larger proportion of taxpayers who pay some of their income at the higher rate than elsewhere in the economy. Recent outturns suggest bonus growth in the financial sector is having a substantial impact on receipts growth.

C.47 In line with recent trends in labour market data, the growth in the wage and salary bill in 2006-07 is expected to be below the 2005 Pre-Budget Report projection, and leads to lower income tax in 2006-07. As in 2005-06, and consistent with the forecast for non-North Sea corporation tax, buoyant activity in the financial sector during 2006 is expected to boost income tax and NICs and provide a partial offset to the weaker growth in overall wages and salaries.

Non-North Sea corporation tax

C.48 Non-North Sea corporation tax receipts are estimated to grow by 16 per cent in 2005-06, slightly higher than expected in the 2005 Pre-Budget Report, with the January instalment payments particularly strong. Robust growth in receipts from financial sector companies has offset much weaker growth from industrial and commercial companies, where profits have been affected by higher input costs resulting from the rise in oil prices.

C.49 Growth in non-North Sea corporation tax is expected to remain buoyant in 2006-07, before gradually easing to a more moderate growth rate, broadly in line with the economy as a whole. A combination of sharply higher equity prices on a year earlier, strong commercial profit figures for many financial firms and a pickup in merger and acquisition activity all suggest that corporation tax receipts from the financial sector should remain robust in 2006-07. Thereafter, financial company profits are expected to grow in line with their long-run trend. Receipts from industrial and commercial companies should also be boosted through 2006 and 2007 as the economy picks up momentum. Relative to the 2005 Pre-Budget Report, higher equity prices are expected to increase receipts growth from life assurance companies and the more modest revival expected in business investment in the Budget forecast is likely to mean less capital allowances to be offset against tax.

North Sea revenues

C.50 North Sea revenues have grown significantly in 2005-06. This has resulted from a combination of higher oil and gas prices, the impact of the Budget 2005 measure to change payment dates for corporation tax instalments for North Sea companies and from the measure announced in the 2005 Pre-Budget Report to allow companies to defer 100 per cent first year capital allowances from 2005 to 2006. As anticipated in the 2005 Pre-Budget Report, the growth in North Sea revenues during 2005-06 was back-end loaded into the final months of the financial year. North Sea companies paid their first two quarterly instalments on their 2005 accounts in July and October. The Budget 2005 measure meant that both remaining instalments were due before the end of 2005-06 (rather than partly in April 2006 as in the previous system). In addition, the rise in the oil price over last summer meant that their first two instalment payments would not have fully taken on the implications for profits of the higher oil price, further boosting their instalment payments in January 2006. There were also additional payments relating to the 2005 Pre-Budget Report measure on deferring capital allowances. This added around £0.6 billion to receipts in 2005-06. The 2005 Pre-Budget Report had assumed that all the relevant receipts from this change would score in 2006-07. As a result of the earlier scoring, there will be a compensating reduction in receipts in 2006-07.

C.51 The projections for North Sea revenues use the NAO-audited assumption on oil prices. In line with the average of independent forecasts, oil prices are expected to average \$57.4 a barrel in 2006, compared with an assumption of \$56 a barrel in the 2005 Pre-Budget Report. They are then assumed to be constant in real terms. However, in 2006-07 the impact on North Sea revenues of the slightly higher oil price is more than offset by changes in assumptions on production and capital expenditure levels. Oil and gas production is expected to show a modest temporary drop in 2006 based on a survey of North Sea producers, compared with the small rise assumed in the 2005 Pre-Budget Report. Furthermore North Sea companies have raised their capital expenditure levels. With 100 per cent relief on all expenditure, this will have an immediate impact on receipts. From 2007-08 onwards, production returns to levels only slightly below those in the 2005 Pre-Budget Report projections and North Sea revenues are broadly unchanged from the 2005 Pre-Budget Report levels.

Capital gains tax and inheritance tax

C.52 Receipts from capital gains tax are forecast to record growth of around 25 per cent in 2005-06. This reflects the rise in the equity market in 2004-05 and continuing effects from the disposal of business assets following the maturing of the business asset taper in 2002-03. Higher equity prices will push up receipts of capital gains tax and inheritance tax by around £$^1/_2$ billion in total compared with the 2005 Pre-Budget Report, although tax payment lags mean most of this effect will only be observed from 2007-08 onwards.

Stamp duties

C.53 Stamp duties are expected to be £0.7 billion above the 2005 Pre-Budget Report projection in 2005-06, reflecting strong growth in both duties on shares and on land and property. Stamp tax on land and property has benefited from the continued upturn in housing market activity in the final part of 2005, reflected in the pick up in property transactions. In addition, receipts have also been boosted by robust growth in the commercial property market. Higher than expected equity prices and transactions have boosted stamp duty on shares with the starting point for the equity price assumption around 8 per cent higher than in the 2005 Pre-Budget Report. The higher equity price projection results in higher stamp duty on shares throughout the projection period.

VAT receipts

C.54 Growth in VAT receipts over the past year has been subdued and relative to the 2005 Pre-Budget Report projection, receipts are expected to be £0.7 billion lower in 2005-06. Growth has been affected by a combination of weak consumer spending growth, which accounts for around two-thirds of the total VAT tax base, the composition of consumer spending and further losses from fraudulent attacks on the system, in particular Missing Trader Intra-Community (MTIC) fraud. Real private consumption growth was subdued in 2005, while the slowdown was most pronounced in spending on consumer durables. This led to a decline in the proportion of spending subject to the standard rate of VAT. Year-on-year growth in VAT receipts has improved from the first half of 2005-06, but not by as much as expected in the 2005 Pre-Budget Report projection. Consumer spending growth has picked up moderately but remains below its long-run average.

C.55 The VAT forecast is partly determined by the NAO-audited assumption on VAT, whereby the VAT gap (the difference between the theoretical liability to VAT and VAT receipts as a percentage of the theoretical liability) is assumed to increase by 0.5 percentage points per year from at least the estimated outturn for the current year, before adjustments for the impact of the VAT compliance strategy. However, the forecast for 2006-07 assumes that the pre-strategy VAT gap rises by more than 0.5 percentage points. This largely reflects recent growth in MTIC fraud. As set out in Chapter 5, a series of measures have been introduced to protect VAT revenues and complement those introduced as part of the VAT Compliance Strategy. At the 2005 Pre-Budget Report the Government re-affirmed its commitment to tackling MTIC fraud. HMRC have since taken a number of steps to strengthen their operational response to the fraud and the Government is introducing a series of legislative changes to support this. This will increase VAT receipts, particularly from 2007-08 onwards. Growth in VAT receipts should also be boosted by the expected gradual strengthening in the economy.

Excise duties **C.56** Receipts of fuel duties have continued to be affected by the impact of oil market volatility and related high pump prices, and the effect of that on demand for fuel. This lowers revenues because fuel duties are charged on a per litre basis. With oil prices remaining around $60 a barrel, above the level assumed in the 2005 Pre-Budget Report, fuel duty revenues are expected to be £0.3 billion lower in 2005-06 than in the 2005 Pre-Budget Report projection. The decision to delay the revalorisation of fuel duties until September 2006 will further reduce revenues in 2006-07. The 2005 Pre-Budget Report had assumed, in line with convention, that fuel duties would rise in line with inflation on the day of the Budget.

C.57 The weakness in overall consumer spending in 2005 is likely to have been a factor in the sluggish growth in alcohol duty and the small drop in tobacco receipts expected in 2005-06. The 2005 Pre-Budget Report had assumed some acceleration in the year-on-year growth in both alcohol and tobacco receipts in the final part of the financial year. The tobacco forecast includes an estimate of the impact of the smoking ban on consumption in enclosed workplaces. This reduces receipts by around £0.5 billion a year from 2007-08.

Council tax **C.58** Council tax increases are determined annually by local authorities, not by the Government. The council tax figures for 2007-08 onwards are based on stylised assumptions and are not government forecasts. The methodology used to derive these assumptions is the same as in Budget 2005. The projected increase in 2006-07 is based on the latest available estimates released by the Chartered Institute for Public Finance and Accountancy (CIPFA) and the increases for later years on the arithmetic average of national council tax increases since their introduction. The increase in 2006-07 is lower than that assumed in the 2005 Pre-Budget Report with council tax expected to be £0.7 billion lower. Since changes to council tax are broadly balanced by changes to locally-financed expenditure, they have little material impact on the current balance or net borrowing.

Other taxes and receipts **C.59** The main changes to the projection for other taxes and receipts are due to the decision taken by the ONS and announced on 20 January 2006 that TV licences should no longer be regarded as a service charge, and the consequent reclassification of the BBC and S4C to the central government sector from the public corporations sector. Although this change is fiscally neutral for the public sector, it adds to both receipts and expenditure totals. The forecast for 2007-08 is based on an increase of RPI on the 2006-07 forecast and does not represent the Government's view on the level of the TV licence fee to apply from April 2007.

C.60 HM Treasury has decided to continue to follow Organisation for Economic Co-operation and Development (OECD) Revenue Statistics guidelines, which treat such licence receipts as a service charge, in respect of TV licence receipts following OECD guidelines allows the tax-GDP ratio to be more easily compared internationally. These receipts are not included in net taxes and social security contributions, but are included in other receipts.

C.61 Other receipts are also higher than in the 2005 Pre-Budget Report because of higher accruals adjustment, particularly from NICs, and higher interest and dividend receipts. The Budget forecast does not include the impact from the Pension Protection Fund (PPF) either on receipts or expenditure. The PPF is funded by an annual levy, but given that payments from the PPF to pension schemes are expected to be similar over time to the levy charged, the introduction of the PPF is expected to be fiscally neutral.

Tax-GDP ratio

C.62 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, based on net taxes and national insurance contributions. Chart C3 shows the tax-GDP ratio from 1980-81 to 2010-11.

C.63 The tax-GDP ratio is expected to rise from 36.2 per cent in 2004-05 to 37.5 per cent in 2005-06. Growth in receipts in 2005-06 has been stronger than would have been expected given the cyclical developments in the economy, primarily because of stronger growth in the financial sector and higher receipts of North Sea taxes. With net taxes and national insurance contributions £0.7 billion higher in 2005-06 than in the 2005 Pre-Budget Report, the tax-GDP ratio is 0.1 per cent higher than expected.

C.64 From 2006-07 onwards, the rise in the tax-GDP ratio is driven by rises in the income tax and corporation tax to GDP ratios. The rise in income tax largely arises from the normal fiscal forecasting convention on tax allowances and fiscal drag. The buoyant growth in non-North Sea corporation tax is expected to persist into 2006-07, but is expected to stabilise at 3.4 per cent of GDP from 2007-08 onwards. The small rise in the tax-GDP ratio relative to the 2005 Pre-Budget Report projections reflects mainly a lower nominal GDP level.

Table C9: Current receipts as a proportion of GDP

	Per cent of GDP						
	Outturn	Estimate	Projections				
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Income tax (gross of tax credits)	10.8	11.1	11.2	11.4	11.5	11.7	11.8
National insurance contributions	6.6	7.0	7.0	7.0	7.0	7.1	7.1
Non-North Sea corporation tax[1]	2.6	2.9	3.2	3.4	3.4	3.4	3.4
Tax credits[2]	-0.4	-0.4	-0.4	-0.4	-0.3	-0.3	-0.3
North Sea revenues[3]	0.4	0.8	0.8	1.0	1.0	0.9	0.8
Value added tax	6.2	6.0	6.0	6.0	5.9	5.9	5.8
Excise duties[4]	3.3	3.2	3.1	3.1	3.0	3.0	2.9
Other taxes and royalties[5]	6.6	6.9	7.1	7.1	7.1	7.1	7.2
Net taxes and national insurance contributions[6]	**36.2**	**37.5**	**38.0**	**38.5**	**38.7**	**38.7**	**38.7**
Accruals adjustments on taxes	0.1	0.2	0.2	0.2	0.2	0.2	0.1
Less EU transfers	-0.4	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3
Other receipts[7]	2.3	2.4	2.5	2.5	2.5	2.5	2.5
Current receipts	**38.3**	**39.7**	**40.3**	**40.9**	**41.0**	**41.0**	**41.0**

[1] *National accounts measure, gross of enhanced and payable tax credits.*
[2] *Tax credits scored as negative tax in net taxes and national insurance 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 EU budget. Cash basis.*
[7] *Mainly gross operating surplus and rent, excluding oil royalties.*

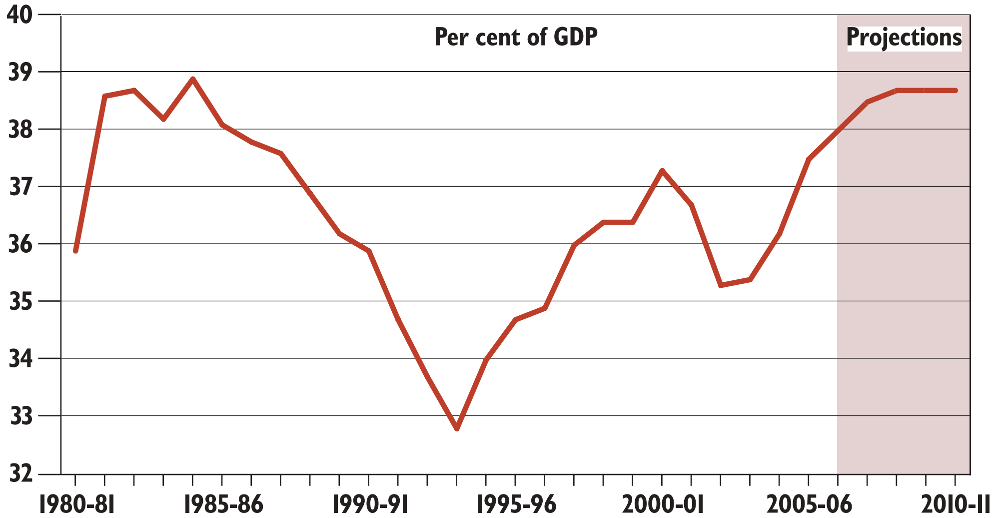
Table C10: Net taxes and national insurance contributions[1]

	Per cent of GDP						
	Outturn[2]	Estimate[3]	Projections				
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Budget 2005	36.3	37.3	37.9	38.3	38.5	38.5	
PBR 2005	36.3	37.4	38.2	38.5	38.5	38.6	38.6
Budget 2006	36.2	37.5	38.0	38.5	38.7	38.7	38.7

[1] *Cash basis. Uses OECD definition of tax credits scored as negative tax.*
[2] *The 2004-05 figures were estimates in Budget 2005.*
[3] *The 2005-06 figures were projections in Budget 2005.*

C.65 Chart C3 shows the tax-GDP ratio from 1980-81 to 2010-11.

Chart C3: Tax-GDP ratio[1]



[1] *Net taxes and national insurance contributions as defined in Table C10.*

PUBLIC EXPENDITURE

C.66 This section looks in detail at the projections for public expenditure. The spending projections cover the whole of the public sector, using the national accounts aggregate Total Managed Expenditure (TME).

C.67 For fiscal aggregates purposes, TME is split into national accounts components covering public sector current expenditure, public sector net investment and depreciation. For budgeting and other purposes, TME is split into DEL – firm three-year limits for departments' programme expenditure, and AME – expenditure that is not easily subject to firm multi-year limits. Departments have separate resource budgets, for current expenditure and capital budgets.

Changes in TME since 2005 Pre-Budget Report

C.68 The reclassification of the BBC to central government, (see Other taxes and receipts in the tax-by-tax analysis section) adds about £$2\frac{1}{2}$ billion a year to current expenditure and to current receipts. After allowing for this reclassification, TME in 2005-06 is expected to be around £$\frac{1}{2}$ billion higher than in the 2005 Pre-Budget Report, but is around £$\frac{1}{2}$ billion lower in both 2006-07 and 2007-08.

C.69 Discretionary changes to TME are set out in Chapter A and include the education package in 2006-07 and 2007-08 and continued indexation of the child element of the Child Tax Credit in line with earnings in 2008-09 and 2009-10.

C.70 Public sector current expenditure increases by around £$1\frac{1}{2}$ billion in 2005-06, and after allowing for discretionary changes this is offset by reductions in 2006-07 and 2007-08 combined. Public sector net investment is lower by around £$\frac{1}{2}$ billion each year from 2005-06 to 2007-08. The changes to spending components are discussed in more detail below.

C.71 The reclassification by ONS of the BBC to central government impacts on both receipts and expenditure. Certain commercial trading subsidiaries of the BBC remain in the public corporations sector as they continue to meet the definition of a market body. Before the reclassification the BBC's production and other current operating expenses were offset by income from the licence fee to form part of the public corporation gross operating surplus, which benefits the receipts side of the public sector finances. After reclassification, the current spending of the BBC is included in public sector current expenditure. The licence fee still benefits the receipts side of the public finances and hence the surplus on the current budget is not affected. The treatment of BBC capital spending in TME is unaffected although most of it now scores as a central government contribution to capital expenditure rather than that of a public corporation.

Table C11: Total Managed Expenditure 2004-05 to 2007-08

	£ billion			
	Outturn	Estimate	Projections	
	2004-05	2005-06	2006-07	2007-08
Departmental Expenditure Limits				
Resource Budget	257.2	277.6	294.5	309.7
Capital Budget	33.6	37.4	42.5	45.6
Less depreciation	-8.3	-11.9	-11.8	-11.5
Total Departmental Expenditure Limits	**282.5**	**303.0**	**325.2**	**343.8**
Annually Managed Expenditure				
Social security benefits[1]	121.5	127.4	131.5	138.3
Tax credits[1]	15.0	15.4	15.6	15.1
Net public service pensions[2]	1.1	0.3	0.4	0.3
National Lottery	1.8	1.9	1.7	1.5
BBC domestic services	2.9	3.1	3.3	3.4
Other departmental expenditure	2.9	4.3	3.6	3.2
Net expenditure transfers to EU institutions[3]	4.8	4.4	5.4	6.5
Locally-financed expenditure[4]	24.3	26.6	27.7	29.3
Central government gross debt interest	24.0	25.7	26.3	28.0
Public corporations' own-financed capital expenditure	2.2	2.8	2.9	2.9
AME margin	0.0	0.0	1.0	2.0
Accounting adjustments[5]	8.0	8.2	7.7	8.5
Annually Managed Expenditure	**208.5**	**220.2**	**227.1**	**238.9**
Total Managed Expenditure	**491.0**	**523.2**	**552.3**	**582.8**
of which:				
Public sector current expenditure	455.4	481.9	506.7	534.2
Public sector net investment	20.7	25.7	28.8	30.9
Public sector depreciation	15.0	15.6	16.8	17.7

[1] For 2004-05 to 2006-07, 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 on a national accounts basis.

[3] AME spending component only. Total net payments to EU institutions also include receipts scored in DEL, VAT based contributions which score as negative receipts and some payments which have no effect on the UK public sector in the national accounts. Latest estimates for total net payments, which exclude the UK's contribution to the cost of EU aid to non-Member States (which is attributed to the aid programme), and the UK's net contribution to the EU Budget, which includes this aid, are (in £ billion):

	2004-05	2005-06	2006-07	2007-08
Net payments to EU institutions	*3.2*	*3.9*	*1.3*	*4.8*
Net contribution to EU Budget	*2.6*	*3.3*	*0.6*	*4.2*

[4] This expenditure is mainly financed by council tax revenues. See footnote to table C8 for an explanation of how the council tax projections are derived.

[5] Excludes depreciation.

C.72 Chart C4 shows TME as a per cent of GDP from 1971-71 to 2007-08.

Chart C4: Total Managed Expenditure

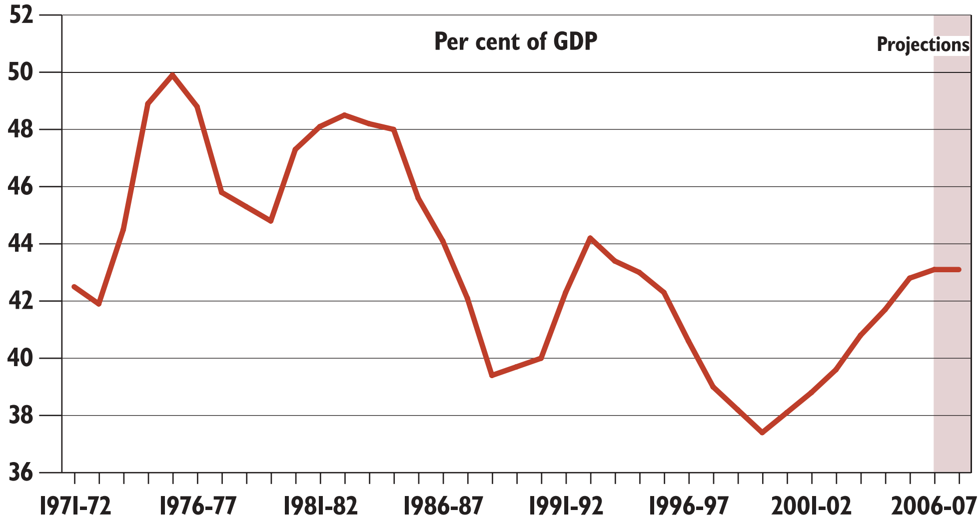


Table C12: Changes to Total Managed Expenditure since the 2005 Pre-Budget Report

	£ billion			
	Outturn	Estimate	Projections	
	2004-05	2005-06	2006-07	2007-08
Departmental Expenditure Limits				
Resource Budget	-9.0	-9.4	-10.5	-11.0
Capital Budget	8.2	8.3	10.5	10.3
Less depreciation	0.0	-0.2	0.3	0.3
Total Departmental Expenditure Limits	**-0.8**	**-1.3**	**0.4**	**-0.3**
Annually Managed Expenditure				
Social security benefits	0.2	0.2	-0.2	0.0
Tax credits	-0.3	0.0	0.9	0.5
Net public service pensions	0.0	-0.4	-0.1	-0.3
National Lottery	0.0	0.2	0.1	0.1
BBC domestic services	2.9	3.1	3.3	3.4
Other departmental expenditure	0.0	-0.5	-0.1	-0.1
Net expenditure transfers to EU institutions	-0.1	0.3	-0.5	0.0
Locally-financed expenditure	-1.5	-0.4	-0.4	-0.3
Central government gross debt interest	0.0	0.1	-0.1	-0.1
Public corporations' own-financed capital expenditure	-0.3	0.0	0.2	0.2
AME margin	0.0	0.0	-0.1	0.2
Accounting adjustments	3.4	2.1	-1.3	-1.0
Annually Managed Expenditure	**4.5**	**4.6**	**1.8**	**2.4**
Total Managed Expenditure	**3.7**	**3.2**	**2.2**	**2.1**
of which:				
Public sector current expenditure	1.9	4.0	2.5	2.2
Public sector net investment	1.7	-0.6	-0.6	-0.3
Public sector depreciation	0.1	-0.1	0.2	0.2

DEL and AME analysis

C.73 Table C11 sets out projected spending on DEL and the main components of AME to the end of the 2004 Spending Review period in 2007-08. Table C12 shows changes since the 2005 Pre-Budget Report.

DEL **C.74** Changes to the budgeting presentation of public expenditure are largely a result of budgeting regime changes announced in the 2005 Pre-Budget Report. These changes have no impact on national accounts definitions, and so have no impact on the definitions of current expenditure for the purposes of the fiscal rules. Other changes include discretionary measures announced in Budget 2006, as set out in Chapter A, and allocations from the reserves. The main changes are:

- the movement of spending on capital grants into capital budgets, so that the budgeting presentation aligns better with the fiscal framework. This reduces the resource budget and increases the capital budget in all years, and by £10 billion by 2007-08. This has no impact on total public sector current expenditure, the relevant measure of public spending for assessing performance against the golden rule;
- the movement of structural funds and other general income from the European Union (EU) into DEL, allowing departments to offset this income against their budgets. Resource and capital DEL budgets are restated to take account of this income, reducing them in all years and by around £4 billion on resource and £0.5 billion on capital by 2007-08;
- the movement of spending under the Common Agricultural Policy (CAP) from the Department for the Environment, Food and Rural Affairs (DEFRA) AME budget into DEL, along with the associated income from the EU. This has no net effect on DEFRA's DEL totals, with the exception of small differences due to the timing of payments and provisions for disallowance. The CAP line in the budgeting presentation of TME is removed as redundant;
- the movement of payments to National Health Service (NHS) Trusts to cover their depreciation costs from outside budgets into the Department of Health's resource DEL, bringing the treatment of Trust depreciation further into line with the budgeting treatment of depreciation for central government and obviating the need for its inclusion in the accounting adjustments; as well as other reprofiling of the Department of Health's resource budget over the 2004 Spending Review period, partly to reflect the forecast return to surplus in the NHS;
- the movement of Direct School Grant from local government DEL to the Department for Education and Skills (DfES) in 2006-07 and 2007-08, increasing DfES resource DEL by £28 billion in those years; and
- setting aside provision from within existing public spending plans to help meet the costs of Iraq, Afghanistan and our other international commitments, with funding allocated to the Special Reserve line.

C.75 The detailed allocations of DELs are shown in Table C13. In line with previous practice, resource and capital DEL for 2005-06 includes an allowance for shortfall reflecting likely underspends against departmental provision. Excepting the impact of reclassifications and other budgeting changes, estimated outturn for resource DEL is broadly as forecast in the 2005 Pre-Budget Report, while slippage in capital programmes in the Department of Health and DfES mean estimated outturn for capital DEL is lower than forecast.

AME **C.76** The main economic assumptions underpinning the AME projections are set out in Box C1 and Table C3. In particular it is assumed that the UK claimant count unemployment rises slowly to 0.97 million in 2007-08, from recent levels of 0.91 million. The AME total is also affected by the BBC change and by reclassifications described above.

C.77 Compared to the 2005 Pre-Budget Report projections, social security expenditure is forecast to be slightly higher in 2005-06, slightly lower in 2006-07 and unchanged in 2007-08. The effects of changes in economic determinants are broadly offset by changes in take up rates and average amounts claimed.

C.78 Forecasts for expenditure on the Child and Working Tax Credits are higher than in the 2005 Pre-Budget Report. This reflects the effects of changes in the economic determinants underlying the forecast, which have increased projected expenditure, and the latest administrative data, including on the overall numbers families that are in and out of work, which has also increased forecast spending.

C.79 Net public service pensions figures are shown on the transactions basis used in national accounts and consist of cash expenditure on pensions less cash income. On this basis, net pensions expenditure is slightly lower than was expected in the 2005 Pre-Budget Report, largely because of higher income to and lower expenditure by the Principal Civil Service Pension Scheme.

C.80 National lottery expenditure numbers increase slightly relative to the 2005 Pre-Budget report reflecting the latest assumption of draw downs by the distributing bodies, including draw down of extra proceeds from Olympic Lottery games.

C.81 Following the reclassification of the BBC to central government, the current and capital spending of the BBC home broadcasting service (the BBC excluding the World Service and its commercial subsidiaries) are shown aggregated into a separate AME line called BBC domestic services. The forecast for 2007-08 is based on an increase of RPI on the 2006-07 forecast and does not represent the Government's view on the level of the TV licence fee to apply from April 2007.

C.82 Other departmental expenditure in 2005-06 is lower than in the 2005 Pre-Budget Report forecast, largely because of lower capital spending.

C.83 The reclassifications and accounting changes described at the beginning of this section affect the scoring of several of the components making up the UK's net contributions to the EU. Some of the spending and receipts components are now in DEL rather than AME and the net expenditure transactions line in AME includes just the components remaining in AME, the GNI based contribution less the UK abatement. The components now in DEL have a broadly neutral effect on TME. Relative to the 2005 Pre-Budget Report, net expenditure transactions are slightly higher in 2005-06 but lower in 2006-07.

C.84 Figures on overall net payments to the EU institutions and the UK's net contribution to the EU budget are included in a footnote to Table C11. On 17 December 2005, Heads of State and Government of all Member States of the European Union agreed the multi-annual financial framework for the European Communities budget for 2007-13. This agreement has only a limited impact on overall net payments in the period covered by Table C11.

C.85 Changes to Local Authority Self-Financed Expenditure (LASFE) reflect the revision to the forecasting assumption made for increases to council tax, and changes to the forecasts of other local authority income. Council tax increases are determined annually by local authorities, not by the Government and the council tax figures for 2007-08 onwards are based on stylised assumptions and are not Government forecasts. The council tax increase in 2006-07 is lower than that assumed in the 2005 Pre-Budget Report leading to lower LASFE. Since changes to LASFE are broadly balanced by changes to council tax and other income, they have little material impact on the current balance or net borrowing.

C.86 Central government debt interest payments for 2005-06 are broadly in line with the 2005 Pre-Budget Report projections.

C.87 The changes to public corporations' own-financed capital expenditure mainly reflect reclassifications. The ONS decision to reclassify London and Continental Railways as part of the public sector adds to capital expenditure and leads to increased spending in 2005-06, 2006-07 and 2007-08, relative to the 2005 Pre-Budget Report. The BBC's capital expenditure is now included in the BBC domestic services line.

Table C13: Departmental Expenditure Limits - resource and capital budgets

	£ billion			
	Outturn	Estimate	Plans	
	2004-05	2005-06	2006-07	2007-08
Resource Budget				
Education and Skills	23.0	24.6	53.4	56.7
Health	69.2	76.9	82.0	89.1
of which : NHS	66.9	74.7	80.0	87.1
Transport	5.3	5.7	6.9	6.7
Office of the Deputy Prime Minister	3.5	3.3	3.5	3.7
Local Government	43.3	46.1	22.5	23.3
Home Office	12.0	12.7	13.1	13.6
Departments for Constitutional Affairs	3.3	3.7	3.9	4.0
Law Officers' Departments	0.6	0.6	0.7	0.7
Defence	31.3	33.3	32.6	32.8
Foreign and Commonwealth Office	1.7	2.0	1.8	1.7
International Development	3.8	4.4	5.0	5.3
Trade and Industry	4.3	5.5	5.6	5.8
Environment, Food and Rural Affairs	2.8	3.0	3.0	3.1
Culture, Media and Sport	1.3	1.4	1.5	1.6
Work and Pensions	7.8	7.9	7.8	7.7
Scotland[1]	19.3	20.8	22.2	23.4
Wales[1]	10.3	11.5	11.7	12.4
Northern Ireland Executive[1]	6.3	6.8	7.1	7.6
Northern Ireland Office	1.2	1.0	1.2	1.1
Chancellor's Departments	4.9	5.0	5.1	5.1
Cabinet Office	2.0	2.1	2.0	2.2
Invest to Save Budget	0.0	0.0	0.0	0.0
Reserve	0.0	0.0	0.9	2.1
Unallocated special reserve[2]	0.0	0.0	0.8	0.0
Allowance for shortfall	0.0	-1.0	0.0	0.0
Total Resource Budget DEL	**257.2**	**277.6**	**294.5**	**309.7**
Capital Budget				
Education and Skills	4.9	5.8	6.2	7.0
Health	2.7	3.0	5.3	6.3
of which : NHS	2.6	2.9	5.2	6.2
Transport	6.0	6.6	7.4	6.7
Office of the Deputy Prime Minister	5.1	5.6	5.7	6.2
Local Government	0.3	0.4	0.2	0.2
Home Office	1.1	1.1	1.2	1.3
Departments for Constitutional Affairs	0.2	0.2	0.1	0.1
Law Officers' Departments	0.0	0.0	0.0	0.0
Defence	6.8	6.8	6.9	7.5
Foreign and Commonwealth Office	0.1	0.2	0.2	0.1
International Development	0.0	0.0	0.0	0.0
Trade and Industry	0.8	1.3	1.2	1.1
Environment, Food and Rural Affairs	0.5	0.7	0.8	0.8
Culture, Media and Sport	0.1	0.3	0.3	0.2
Work and Pensions	0.3	0.4	0.2	0.1
Scotland[1]	2.2	2.4	2.9	3.1
Wales[1]	1.1	1.3	1.4	1.6
Northern Ireland Executive[1]	0.8	1.0	0.9	1.0
Northern Ireland Office	0.1	0.1	0.1	0.1
Chancellor's Departments	0.4	0.4	0.3	0.3
Cabinet Office	0.2	0.3	0.3	0.3
Invest to Save Budget	0.0	0.0	0.0	0.0
Reserve	0.0	0.0	0.8	1.5
Allowance for shortfall	0.0	-0.3	0.0	0.0
Total Capital Budget DEL	**33.6**	**37.4**	**42.5**	**45.6**
Depreciation	**-8.3**	**-11.9**	**-11.8**	**-11.5**
Total Departmental Expenditure Limits	**282.5**	**303.0**	**325.2**	**343.8**
Total education spending	**63.7**	**68.4**	**73.3**	**78.0**

[1] For Scotland, Wales and Northern Ireland, the split between resource and capital budgets is indicative and reflects the consequentials of the application of the Barnett formula to planned changes in UK departments' spending.

[2] This represents provision for the costs of military operations in Iraq and Afghanistan, as well as the UK's other international obligations.

C.88 The main accounting adjustments, which reconcile the DEL and AME measures of spending with the national accounts measure, are shown in Table C14. Changes to the accounting adjustments since the last forecast are mainly due to:

- the classification changes outlined above, particularly those affecting EU contributions;
- lower VAT refunds which reduce both receipts and expenditure; and
- changes to the adjustments for non-cash items in resource budgets as a result of changes in the composition of departmental spending.

Table C14: Accounting adjustments

	£ billion			
	Outturn	Estimate	Projections	
	2004-05	2005-06	2006-07	2007-08
Central government programmes	0.9	0.8	0.8	0.8
VAT refunds	9.6	10.5	11.4	12.2
Central government non-trading capital consumption	5.7	5.9	6.6	7.0
Non-cash items in resource budgets and not in TME	-8.9	-10.6	-12.1	-14.3
Expenditure financed by revenue receipts	0.1	0.2	0.1	0.1
Local authorities	3.6	4.0	4.8	5.4
General government consolidation	-4.5	-4.5	-4.5	-4.5
Public corporations	0.6	0.5	0.6	0.6
Financial transactions	0.4	0.5	0.7	0.8
Other accounting adjustments	0.6	0.7	-0.7	0.5
Total accounting adjustments	**8.0**	**8.2**	**7.7**	**8.5**

C.89 Table C15 shows public sector capital expenditure from 2004-05 to 2007-08.

Table C15: Public sector capital expenditure

	£ billion			
	Outturn	Estimate	Projections	
	2004-05	2005-06	2006-07	2007-08
Capital Budget DEL	33.6	37.4	42.5	45.6
Locally-financed expenditure	0.8	1.8	2.0	2.1
National Lottery	1.1	1.0	1.0	0.9
Public corporations' own-financed capital expenditure	2.2	2.8	2.9	2.9
Other capital spending in AME	-2.1	-1.8	-2.9	-3.2
AME margin	0.0	0.0	0.1	0.2
Accounting adjustments	0.1	0.1	0.1	0.1
Public sector gross investment[1]	**35.6**	**41.3**	**45.6**	**48.6**
Less depreciation	15.0	15.6	16.8	17.7
Public sector net investment	**20.7**	**25.7**	**28.8**	**30.9**
Proceeds from the sale of fixed assets[2]	6.3	6.6	6.6	6.6

[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.*

C.90 Table C16 shows estimated receipts from loans and sales of assets from 2004-05 to 2007-08. The figures for sales of financial assets include proceeds in the final quarter of 2005-06 of £0.3 billion from the sale of part of the Government's shareholding in QinetiQ (formerly the Defence Evaluation and Research Agency). The table only covers general government and so does not include the sale by BNFL of its Westinghouse subsidiary, which the company expects to finalise in the next six months. The proceeds from the sale are included in the public corporations column of Table C20 (public sector net cash requirement). It is anticipated that there will be a public sector neutral transfer of the proceeds to central government.

Table C16: Loans and sales of assets

	£ billion			
	Outturn	Estimate	Projections	
	2004-05	2005-06	2006-07	2007-08
Sales of fixed assets				
Central government	1.1	1.4	1.4	1.4
Local authorities	5.2	5.2	5.2	5.2
Total sales of fixed assets	**6.3**	**6.6**	**6.6**	**6.6**
Total loans and sales of financial assets	**-2.1**	**-2.5**	**-3.2**	**-3.6**
Total loans and sales of assets	**4.1**	**4.1**	**3.4**	**3.0**

PRIVATE FINANCE INITIATIVE

C.91 Under the Private Finance Initiative (PFI) the public sector contracts to purchase services on a long-term basis so as to take advantage of private sector management skills incentivised by having private finance at risk. The private sector has always been involved in the building and maintenance of public infrastructure, but PFI ensures that contractors are bound into long-term maintenance contracts and shoulder responsibility for the quality of the work they do. With PFI, the public sector defines what is required to meet public needs and ensures delivery of the outputs through the contract. Consequently, the private sector can be harnessed to deliver investment in better quality public services whilst frontline services are retained within the public sector. The Government's position on PFI is set out in the document *PFI: Strengthening Long Term Partnerships* published alongside the Budget.

C.92 The Government only uses PFI where it is appropriate and where it expects it to deliver value for money. This is based on an assessment of the lifetime costs of both providing and maintaining the underlying asset, and of the running costs of delivering the required level of service. In assessing where PFI is appropriate, the Government's approach is based on its commitment to efficiency, equity and accountability, and on the Prime Minister's principles of public service reform. PFI is only used where it can meet these requirements, and where the value for money it offers is not at the expense of the terms and conditions of staff. The Government is committed to securing the best value for its investment programme by ensuring that there is no inherent bias in favour of one procurement option over another.

C.93 Table C17 shows a breakdown by department of the estimated capital investment in public services resulting from signed PFI contracts. Table C18 shows the estimated total capital value of contracts that are at preferred bidder stage and are expected to reach financial close within the next three years. Under PFI, the public sector contracts for services, including the availability and management of facilities, and 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 C17 and C18 report the capital value of projects in order to show investment on a basis comparable with conventional capital procurement.

C.94 Table C19 shows a forecast of the estimated payments for services flowing from signed PFI projects. Actual expenditure will depend on the details of the payment mechanism for each contract. Payments may be lower than those estimated as a result of deductions that can be applied if the supplier fails to meet required performance standards. Variances may also occur as a result of agreed changes to the service requirements that are made during the course of the contract, or because of contractual arrangements that trigger compensation on termination. The fact that capital investment only represents one element of the overall contract means that the figures presented in this table should not be taken to be directly comparable with a public sector debt liability.

Table C17: Departmental estimate of capital spending by the private sector (signed deals)[1,2,3]

	£ million		
		Projections	
	2005-06	2006-07	2007-08
Education and Skills[4]	491	372	158
Health	943	784	621
Transport[5]	1497	1390	1085
Office of the Deputy Prime Minister	84	63	34
Home Office	61	10	0
Constitutional Affairs	25	10	0
Defence	501	375	357
Foreign and Commonwealth Office	5	5	5
Trade and Industry	6	2	0
Environment, Food and Rural Affairs	67	58	37
Culture, Media and Sport	45	26	0
Work and Pensions	51	46	55
Scotland	277	213	62
Wales	22	0	0
Northern Ireland Executive	39	27	33
Chancellor's Departments	13	5	2
Total	**4127**	**3386**	**2449**

[1] Investment in assets scored on the public sector balance sheet also score as public sector net investment.
[2] PFI activity in local authority projects is included under the sponsoring central government department.
[3] Figures do not include PFI projects undertaken by public corporations.
[4] Excludes private finance activity in educational institutions classified to the private sector.
[5] Includes estimates of the capital expenditure for the London Underground Limited Public Private Partnership PFI contracts in the years that investments are expected to take place.

Table C18: Estimated aggregated capital value of projects at preferred bidder stage[1,2]

	£ million	
	Projections	
	2005-06	2006-07
Education and Skills	313	303
Health	64	4819
Transport	52	95
Office of the Deputy Prime Minister	207	315
Home Office	0	30
Defence	0	4269
Environment, Food and Rural Affairs	55	334
Culture, Media and Sport	22	0
Scotland	0	405
Wales	61	0
Northern Ireland Executive	31	148
Total	**805**	**10718**

[1] *Figures based on Departmental returns.*

[2] *These figures are the total capital value of projects; the actual annual capital spending figures will be lower, as capital spending on large projects is typically spread over several years.*

Table C19: Estimated payments under PFI contracts - March 2005 (signed deals)[1]

	£ billion		
	Projections		
2005-06	5.9	2018-19	4.9
2006-07	6.5	2019-20	4.9
2007-08	6.7	2020-21	5.0
2008-09	6.9	2021-22	4.6
2009-10	7.3	2022-23	4.6
2010-11	7.4	2023-24	4.5
2011-12	7.6	2024-25	4.5
2012-13	7.6	2025-26	4.4
2013-14	7.7	2026-27	4.1
2014-15	7.6	2027-28	3.8
2015-16	7.7	2028-29	3.4
2016-17	7.8	2029-30	3.1
2017-18	7.1	2030-31	2.7

[1] *The figures between 2005-06 and 2017-18 include estimated payments for the LUL PPP contract. These contracts contain periodic reviews each 7.5 years and therefore the service payments are not fixed after 2009-10.*

FINANCING REQUIREMENT

C.95 Table C20 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 not affect its financing requirement.

Table C20: Public sector net cash requirement

	2005-06				2006-07			
	General government				General government			
£ billion	Central government	Local authorities	Public corporations	Public sector	Central government	Local authorities	Public corporations	Public sector
Net borrowing	**36.9**	**1.8**	**-1.4**	**37.1**	**35.9**	**1.9**	**-2.0**	**35.8**
Financial transactions								
Net lending to private sector and abroad	2.5	0.1	-1.0	1.6	3.1	0.1	-0.6	2.6
Cash expenditure on company securities	-0.3	0.2	0.0	-0.1	0.1	0.0	-2.9	-2.8
Accounts receivable/payable	-0.7	0.0	0.5	-0.2	2.7	0.0	-0.6	2.1
Adjustment for interest on gilts	-2.9	0.0	0.0	-2.9	-0.6	0.0	0.0	-0.6
Miscellaneous financial transactions	0.0	1.4	0.0	1.4	-2.4	0.0	2.4	0.0
Own account net cash requirement	35.4	3.5	-1.9	37.0	38.8	2.0	-3.7	37.1
Net lending within the public sector	5.2	-5.1	-0.1	0.0	2.4	-2.0	-0.4	0.0
Net cash requirement[1]	**40.6**	**-1.6**	**-2.0**	**37.0**	**41.2**	**0.0**	**-4.1**	**37.1**

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

C.96 Table C21 updates the financing arithmetic for both 2005-06 and 2006-07 in line with the updated fiscal forecasts. The central government net cash requirement (CGNCR) for 2005-06 is now forecast to be £40.6 billion, a decrease of £2.7 billion from the 2005 Pre-Budget Report forecast of £43.3 billion.

C.97 The forecast for the CGNCR for 2006-07 is £41.2 billion. Gross gilt redemptions are £29.9 billion and National Savings & Investments' net contribution to financing is estimated to be £3.0 billion. This means that the net financing requirement for 2006-07 is forecast to be £65.0 billion. The Debt Management Office (DMO) will aim to meet the net financing requirement by:

- gross gilts issuance of £63.0 billion;
- an increase in the Treasury bill stock of £2.0 billion by end March 2007; and
- a planned reduction in short-term financing of £3.1 billion (which reduces the financing requirement in 2006-07).

C.98 The gilt market experienced low and sometimes volatile yields at the longest maturities during 2005-06. These unusual conditions may continue next year. Therefore, to help both the DMO and the gilt market more generally to deal with a potentially challenging environment in 2006-07, the DMO's remit contains temporary changes intended to allow greater responsiveness in gilt issuance by the DMO during 2006-07 whilst retaining the Government's firm commitment to transparency and predictability in debt management policy. The key changes to the remit next year are that:

- the £63.0 billion of gross gilt issuance will be made up of: (i) a £53.0 billion 'core' issuance programme pre-allocated by maturity and type of gilt at Budget; and (ii) a £10.0 billion 'unallocated' gilt issuance programme to be allocated between maturity and type of gilt each quarter during 2006-07;
- the first £2.5 billion of the 'unallocated' £10.0 billion of gilt issuance will be allocated at Budget to long-dated conventional gilts in the first quarter of 2006-07; and
- the remaining £7.5 billion will be allocated between maturity and type of gilt by DMO during the last three quarters of 2006-07 (broadly £2.5 billion per quarter).

C.99 Full details of the DMO's financing remit including further information on the structure of gilts issuance and the gilt auction calendar for 2006-07 can be found in the *Debt and Reserves Management Report 2006-07* which is published alongside the Budget and is available on HM Treasury's website.

Table C21: Financing requirement forecast

£ billion	April 2005 Revised Remit[1]	2005-06 December 2005 Pre-Budget Report	March 2006 Budget	2006-07 March 2006 Budget
Central government net cash requirement	**40.2**	**43.3**	**40.6**	**41.2**
Gilt redemptions	14.6	14.6	14.6	29.9
Financing for the Official Reserves	0.0	0.0	0.0	0.0
Buy-backs	0.0	0.0	0.1	0.0
Planned short-term financing adjustment[2]	-2.7	-2.5	-2.5	-3.1
Gross Financing Requirement	**52.1**	**55.4**	**52.8**	**68.0**
less				
Assumed net contribution from National Savings and Investments	3.5	4.2	4.8	3.0
Net Financing Requirement	**48.6**	**51.2**	**48.0**	**65.0**
Financed by:				
1. Debt issuance by the Debt Management Office				
(a) Treasury bills	**-2.5**	**-1.1**	**-1.2**	**2.0**
(b) Gilts	**51.1**	**52.3**	**52.3**	**63.0**
2. Other planned changes in short-term debt[3]				
Change in Ways & Means	0.0	0.0	0.0	0.0
3. Unanticipated changes in short-term cash position[4]	0.0	0.0	3.1	0.0
Total financing	**48.6**	**51.2**	**51.1**	**65.0**
Short-term debt levels at end of financial year				
Treasury bill stock in market hands	18.0	19.2	19.1	21.1
Ways & Means	13.4	13.4	13.4	13.4
DMO net cash position	0.2	0.2	3.3	0.2

[1] *Budget 2005 financing arithmetic was revised on 20 April 2005 to reflect outturn data for 2004-05.*
[2] *To accommodate changes to the current year's financing requirement resulting from: (i) publication of the previous year's outturn CGNCR and / or (ii) carry over of unanticipated changes to the cash position from the previous year.*
[3] *Total planned changes to short-term debt are the sum of: (i) the planned short-term financing adjustment; (ii) Treasury bill sales; and (iii) changes to the level of the Ways & Means advance.*
[4] *A negative (positive) number indicates an addition to (reduction in) the financing requirement for the following financial year.*

C.100 Table C22 below sets out the split of gilt issuance between maturity and type of gilt. Table C22 will be updated and published each quarter to show how the unallocated tranche of financing is being allocated quarter-by-quarter throughout the year and shows the allocation of the initial tranche of the unallocated gilt issuance programme referred to above.

Table C22: Gilt issuance split 2006-2007

£ billion			Quarter 1 Additional gilt issuance allocation	Quarter 1 Updated financing programme
Planned gilt sales		**63.0**		
Pre-allocated gilt issuance		**53.0**		
Of which minimum:				
Conventional	Short	10.0		10.0
	Medium	10.0		10.0
	Long	17.0	2.5	19.5
Index-linked		16.0		16.0
Total pre-allocated gilt issuance		**53.0**	**2.5**	**55.5**
Gilt issuance to be allocated		**10.0**		**7.5**

ANALYSIS BY SUBSECTOR AND ECONOMIC CATEGORY

C.101 Table C23 shows a breakdown of general government transactions by economic category for 2004-05 to 2007-08. Table C24 shows a more detailed breakdown for public sector transactions by sub-sector and economic category for 2004-05, 2005-06 and 2006-07.

C.102 The allocation of public sector transactions between sub-sectors has changed since the 2005 Pre-Budget Report, largely because of better data on the split of TME. This has the effect of substantially increasing central government net borrowing, and hence the cash requirement, and reducing local authority counterparts.

Table C23: General Government transactions by economic category

				£ billion
	Outturn	Estimate	Projections	
	2004-05	2005-06	2006-07	2007-08
Current receipts				
Taxes on income and wealth	161.2	180.5	195.6	214.5
Taxes on production and imports	154.5	160.8	168.0	176.5
Other current taxes	27.2	27.9	29.3	28.4
Taxes on capital	2.9	3.2	3.6	3.9
Compulsory social contributions	80.2	86.6	90.6	95.9
Gross operating surplus	10.9	11.5	12.7	13.5
Rent and other current transfers	2.1	1.9	2.0	2.0
Interest and dividends from private sector and abroad	4.2	4.6	4.9	5.3
Interest and dividends from public sector	4.4	4.0	4.1	4.3
Total current receipts	**447.7**	**481.1**	**510.8**	**544.2**
Current expenditure				
Current expenditure on goods and services	254.0	271.6	286.5	302.8
Subsidies	6.5	6.2	6.6	6.6
Net social benefits	137.6	143.5	147.4	153.0
Net current grants abroad	-0.6	-4.7	-3.8	-4.7
Other current grants	33.0	38.7	41.9	45.7
Interest and dividends paid	24.4	26.3	26.7	28.4
AME margin	0.0	0.0	0.9	1.8
Total current expenditure	**454.9**	**481.4**	**506.3**	**533.7**
Depreciation	10.9	11.5	12.7	13.5
Surplus on current budget	**-18.1**	**-11.9**	**-8.3**	**-3.0**
Capital expenditure				
Gross domestic fixed capital formation	22.1	24.9	28.4	31.2
Less depreciation	-10.9	-11.5	-12.7	-13.5
Increase in inventories	0.0	0.2	0.1	0.1
Capital grants (net) within public sector	-0.2	0.5	0.6	0.5
Capital grants to private sector	10.7	13.7	14.3	14.3
Capital grants from private sector	-1.2	-1.1	-1.2	-1.1
AME margin	0.0	0.0	0.1	0.2
Net investment	**20.5**	**26.7**	**29.6**	**31.7**
Net borrowing[1]	**38.6**	**38.6**	**37.8**	**34.7**
of which:				
Central government net borrowing	38.2	36.8	35.9	32.7
Local authority net borrowing	0.4	1.8	1.9	2.0
Gross debt (Maastricht basis)				
Central government	427.6	467.5	509.3	548.2
Local government	52.9	53.4	53.4	53.4

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

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

	£ billion			
	2004-05			
	General government			
	Central government	Local authorities	Public corporations	Public sector
Current receipts				
Taxes on income and wealth	161.2	0.0	-0.1	161.1
Taxes on production and imports	154.3	0.2	0.0	154.5
Other current taxes	7.7	19.4	0.0	27.2
Taxes on capital	2.9	0.0	0.0	2.9
Compulsory social contributions	80.2	0.0	0.0	80.2
Gross operating surplus	5.7	5.2	6.9	17.8
Rent and other current transfers	2.1	0.0	0.0	2.1
Interest and dividends from private sector and abroad	3.2	1.0	1.3	5.5
Interest and dividends from public sector	3.7	0.8	-4.4	0.0
Total current receipts	**421.0**	**26.7**	**3.6**	**451.3**
Current expenditure				
Current expenditure on goods and services	153.8	100.2	0.0	254.0
Subsidies	4.8	1.7	0.0	6.5
Net social benefits	123.2	14.4	0.0	137.6
Net current grants abroad	-0.6	0.0	0.0	-0.6
Current grants (net) within public sector	94.2	-94.2	0.0	0.0
Other current grants	32.9	0.0	0.0	33.0
Interest and dividends paid	24.0	0.4	0.5	24.9
AME margin	0.0	0.0	0.0	0.0
Total current expenditure	**432.3**	**22.6**	**0.5**	**455.4**
Depreciation	5.7	5.2	4.1	15.0
Surplus on current budget	**-16.9**	**-1.2**	**-0.9**	**-19.0**
Capital expenditure				
Gross domestic fixed capital formation	8.9	13.2	3.8	25.9
Less depreciation	-5.7	-5.2	-4.1	-15.0
Increase in inventories	0.0	0.0	-0.1	0.0
Capital grants (net) within public sector	8.7	-8.9	0.2	0.0
Capital grants to private sector	9.6	1.1	0.3	11.0
Capital grants from private sector	-0.3	-0.9	0.0	-1.2
AME margin	0.0	0.0	0.0	0.0
Net investment	**21.3**	**-0.7**	**0.1**	**20.7**
Net borrowing	**38.2**	**0.4**	**1.1**	**39.7**

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

	£ billion			
	2005-06			
	General government			
	Central government	Local authorities	Public corporations	Public sector
Current receipts				
Taxes on income and wealth	180.5	0.0	-0.1	180.4
Taxes on production and imports	160.6	0.2	0.0	160.8
Other current taxes	7.9	20.1	0.0	27.9
Taxes on capital	3.2	0.0	0.0	3.2
Compulsory social contributions	86.6	0.0	0.0	86.6
Gross operating surplus	5.9	5.6	8.4	19.9
Rent and other current transfers	1.9	0.0	0.0	1.9
Interest and dividends from private sector and abroad	3.3	1.2	0.7	5.3
Interest and dividends from public sector	3.3	0.7	-4.0	0.0
Total current receipts	**453.2**	**27.9**	**5.0**	**486.1**
Current expenditure				
Current expenditure on goods and services	164.8	106.8	0.0	271.6
Subsidies	4.4	1.8	0.0	6.2
Net social benefits	128.1	15.4	0.0	143.4
Net current grants abroad	-4.7	0.0	0.0	-4.7
Current grants (net) within public sector	100.1	-100.1	0.0	0.0
Other current grants	38.7	0.0	0.0	38.7
Interest and dividends paid	25.8	0.4	0.4	26.7
AME margin	0.0	0.0	0.0	0.0
Total current expenditure	**457.2**	**24.3**	**0.4**	**481.9**
Depreciation	5.9	5.6	4.1	15.6
Surplus on current budget	**-9.9**	**-2.1**	**0.5**	**-11.5**
Capital expenditure				
Gross domestic fixed capital formation	12.3	12.6	3.3	28.2
Less depreciation	-5.9	-5.6	-4.1	-15.6
Increase in inventories	0.2	0.0	0.0	0.2
Capital grants (net) within public sector	9.3	-8.8	-0.5	0.0
Capital grants to private sector	11.4	2.3	0.3	14.0
Capital grants from private sector	-0.3	-0.8	0.0	-1.1
AME margin	0.0	0.0	0.0	0.0
Net investment	**26.9**	**-0.3**	**-1.0**	**25.7**
Net borrowing	**36.9**	**1.8**	**-1.4**	**37.1**

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

	£ billion			
	2006-07			
	General government			
	Central government	Local authorities	Public corporations	Public sector
Current receipts				
Taxes on income and wealth	195.6	0.0	-0.1	195.5
Taxes on production and imports	167.7	0.2	0.0	168.0
Other current taxes	8.2	21.1	0.0	29.3
Taxes on capital	3.6	0.0	0.0	3.6
Compulsory social contributions	90.6	0.0	0.0	90.6
Gross operating surplus	6.6	6.2	9.1	21.8
Rent and other current transfers	2.0	0.0	0.0	2.0
Interest and dividends from private sector and abroad	3.5	1.4	0.8	5.7
Interest and dividends from public sector	3.2	1.0	-4.1	0.0
Total current receipts	**480.9**	**29.8**	**5.7**	**516.4**
Current expenditure				
Current expenditure on goods and services	175.2	111.3	0.0	286.5
Subsidies	4.7	1.9	0.0	6.6
Net social benefits	131.5	16.0	0.0	147.4
Net current grants abroad	-3.8	0.0	0.0	-3.8
Current grants (net) within public sector	104.0	-104.0	0.0	0.0
Other current grants	41.9	0.0	0.0	41.9
Interest and dividends paid	26.3	0.4	0.4	27.2
AME margin	0.9	0.0	0.0	0.9
Total current expenditure	**480.6**	**25.6**	**0.4**	**506.7**
Depreciation	6.6	6.2	4.1	16.8
Surplus on current budget	**-6.3**	**-2.0**	**1.1**	**-7.0**
Capital expenditure				
Gross domestic fixed capital formation	14.7	13.7	3.5	31.9
Less depreciation	-6.6	-6.2	-4.1	-16.8
Increase in inventories	0.1	0.0	0.0	0.1
Capital grants (net) within public sector	9.9	-9.3	-0.6	0.0
Capital grants to private sector	11.8	2.5	0.3	14.6
Capital grants from private sector	-0.3	-0.9	0.0	-1.2
AME margin	0.1	0.0	0.0	0.1
Net investment	**29.8**	**-0.2**	**-0.8**	**28.8**
Net borrowing	**35.9**	**1.9**	**-2.0**	**35.8**

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

	Per cent of GDP								
	Public sector current budget	Cyclically adjusted surplus on current budget	Public sector net borrowing	Cyclically adjusted public sector net borrowing	Public sector net cash requirement	Net taxes and national insurance contributions	Public sector current receipts	Public sector net debt[1]	Public sector net worth[2]
1970-71	6.7		-0.6		1.2		43.3		
1971-72	4.2		1.1		1.4		41.4		
1972-73	2.0	2.5	2.8	2.3	3.6		39.0		
1973-74	0.3	-0.8	4.9	6.0	5.9		39.6		
1974-75	-1.1	-2.6	6.6	8.1	9.0		42.3	52.1	
1975-76	-1.6	-1.8	7.0	7.2	9.3		42.9	53.8	
1976-77	-1.2	-0.7	5.5	5.0	6.4		43.3	52.3	
1977-78	-1.4	-1.2	4.3	4.1	3.7		41.5	49.0	
1978-79	-2.6	-2.4	5.0	4.8	5.2	33.5	40.2	47.1	
1979-80	-1.9	-1.8	4.1	4.0	4.7	33.9	40.7	43.9	
1980-81	-3.0	-1.6	4.9	3.4	5.2	35.9	42.4	46.0	
1981-82	-1.4	2.5	2.3	-1.5	3.3	38.6	45.8	46.2	
1982-83	-1.5	2.8	3.0	-1.3	3.2	38.7	45.5	44.8	
1983-84	-2.0	1.7	3.8	0.1	3.2	38.2	44.4	45.1	
1984-85	-2.2	0.9	3.7	0.7	3.1	38.9	44.3	45.3	
1985-86	-1.2	0.6	2.4	0.6	1.6	38.1	43.2	43.5	
1986-87	-1.4	-1.2	2.1	1.9	0.9	37.8	42.0	41.0	
1987-88	-0.3	-1.6	1.0	2.3	-0.7	37.6	41.1	36.8	74.3
1988-89	1.7	-1.0	-1.3	1.3	-3.0	36.9	40.7	30.5	79.3
1989-90	1.4	-1.4	-0.2	2.6	-1.3	36.2	39.9	27.7	71.2
1990-91	0.4	-1.2	1.0	2.6	-0.1	35.9	38.9	26.2	60.6
1991-92	-2.0	-1.5	3.8	3.3	2.3	34.7	38.5	27.4	53.3
1992-93	-5.6	-3.6	7.6	5.6	5.9	33.7	36.6	32.0	40.4
1993-94	-6.2	-4.1	7.8	5.6	7.1	32.8	35.6	37.2	29.6
1994-95	-4.8	-3.5	6.3	4.9	5.3	34.0	36.7	40.8	28.7
1995-96	-3.4	-2.7	4.8	4.0	4.3	34.7	37.6	42.7	21.3
1996-97	-2.8	-2.3	3.5	3.1	2.9	34.8	37.0	43.6	17.3
1997-98	-0.2	0.0	0.8	0.7	0.2	36.0	38.1	41.4	14.4
1998-99	1.2	1.1	-0.4	-0.3	-0.7	36.4	38.6	39.3	13.5
1999-00	2.2	1.9	-1.7	-1.4	-0.9	36.4	38.9	36.3	16.7
2000-01	2.2	1.6	-1.6	-1.0	-3.8	37.2	39.6	31.4	22.5
2001-02	1.0	0.8	0.0	0.3	0.4	36.7	38.7	30.4	29.1
2002-03	-1.2	-0.8	2.4	2.0	2.4	35.3	37.3	31.8	27.9
2003-04	-1.9	-1.4	3.2	2.7	3.5	35.4	37.6	33.2	28.5
2004-05	-1.6	-1.3	3.4	3.0	3.3	36.2	38.3	35.0	29.1

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

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

Table C26: Historical series of government expenditure.

	£ billion (2004-05 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	172.7	32.4	53.1	225.8	32.6	6.1	10.0	42.7
1971-72	181.6	28.7	50.0	231.6	33.3	5.3	9.2	42.5
1972-73	189.0	27.5	49.8	238.8	33.1	4.8	8.7	41.9
1973-74	207.8	30.9	55.9	263.7	35.1	5.2	9.4	44.5
1974-75	229.9	32.7	59.5	289.4	38.8	5.5	10.0	48.9
1975-76	234.9	32.1	59.0	293.9	39.9	5.5	10.0	49.9
1976-77	242.1	26.3	54.2	296.3	39.9	4.3	8.9	48.8
1977-78	238.7	17.9	45.8	284.5	38.4	2.9	7.4	45.8
1978-79	245.8	15.5	44.1	289.9	38.4	2.4	6.9	45.3
1979-80	252.0	14.4	43.4	295.4	38.2	2.2	6.6	44.8
1980-81	259.4	11.6	40.9	300.3	40.8	1.8	6.4	47.3
1981-82	271.0	5.9	35.0	306.1	42.6	0.9	5.5	48.1
1982-83	276.8	9.7	38.0	314.8	42.7	1.5	5.9	48.5
1983-84	285.4	12.0	40.1	325.5	42.3	1.8	5.9	48.2
1984-85	293.6	10.6	37.3	330.9	42.6	1.5	5.4	48.0
1985-86	293.5	8.9	32.7	326.2	41.0	1.2	4.6	45.6
1986-87	298.0	5.3	29.5	327.5	40.1	0.7	4.0	44.1
1987-88	301.5	5.2	27.5	329.0	38.6	0.7	3.5	42.1
1988-89	294.3	2.9	25.9	320.2	36.2	0.4	3.2	39.4
1989-90	296.3	9.9	33.1	329.4	35.7	1.2	4.0	39.7
1990-91	298.1	11.9	32.1	330.3	36.1	1.4	3.9	40.0
1991-92	315.7	15.1	32.2	348.0	38.4	1.8	3.9	42.3
1992-93	331.5	16.5	32.6	364.1	40.2	2.0	3.9	44.2
1993-94	341.3	13.3	29.2	370.5	40.0	1.6	3.4	43.4
1994-95	352.0	12.9	29.4	381.5	39.7	1.5	3.3	43.0
1995-96	357.6	12.5	29.1	386.7	39.1	1.4	3.2	42.3
1996-97	358.1	6.9	21.6	379.7	38.3	0.7	2.3	40.6
1997-98	356.4	6.2	20.5	376.9	36.9	0.6	2.1	39.0
1998-99	358.8	7.5	21.2	379.9	36.1	0.8	2.1	38.2
1999-00	366.3	5.4	19.2	385.5	35.5	0.5	1.9	37.4
2000-01	385.7	6.3	20.3	406.0	36.2	0.6	1.9	38.1
2001-02	396.0	11.1	25.3	421.4	36.5	1.0	2.3	38.8
2002-03	414.2	12.7	27.5	441.6	37.3	1.1	2.5	39.8
2003-04	437.9	14.8	29.4	467.3	38.4	1.3	2.6	41.0
2004-05	455.4	20.7	35.6	491.0	38.7	1.8	3.0	41.7

[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 principal 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 EU 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, self-assessment income tax and some other HMRC taxes which, because of practical difficulties, are scored on a cash basis) on an accruals basis, and impute the value of some transactions where no money changes hands (for example, non-trading capital consumption).

Full details of the sources for each table are included in Budget 2006 technical annex: data sources, available on the Treasury's internet site and on request from the Treasury's Public Enquiry Unit (020 72704558).

The outturn figures are based on series published in the monthly Public Sector Finance release (last published on 20 March 2006).

The principal measures drawn from the national accounts are described below.

FISCAL AGGREGATES

The current budget (formerly known as the current balance) measures the balance of current account revenue over current expenditure (including depreciation). 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. The current budget is used to measure progress against the golden rule. The actual measure is the average surplus on the current budget expressed as a ratio to GDP over the economic cycle.

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 fiscal 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.

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 liabilities. 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.

PUBLIC SECTOR RECEIPTS

Net taxes and national insurance contributions (NTNIC) is a measure of net cash payments made to the 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;
- payments of customs duties and agricultural and sugar levies that are collected by the government, but then paid to the EU, are subtracted as they do not score as government receipts in the national accounts. These receipts make up the traditional own resources element of net payments to the EU;
- 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 NTNIC, 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 ONS have adopted this treatment for the Working Tax Credit and Child Tax Credit, which were 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 NTNIC are added back into current receipts in Table C8;
- a similar adjustment is made for TV licences, which the ONS treat as tax receipts in the national accounts. They score as non-tax receipts in NTNIC, in line with OECD Revenue Statistics guidelines;
- interest and other non-tax receipts, which are excluded from NTNIC, are added. This excludes oil royalties, as they are already included in NTNIC, even though the national accounts treat them as non-tax receipts; and
- business rates paid by local authorities are included in the calculation of NTNIC but not PSCR. These are therefore deducted from NTNIC before arriving at PSCR.

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 C15. 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 DEL and AME:

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 spending that is included in departmental AME 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, or disability, caring responsibilities and bereavement, as well as housing costs for all groups with effect from Budget 2004. Some expenditure on housing-related benefits is, however, covered by the locally financed expenditure category.

Tax credits for individuals scored as expenditure includes spending on the Working Families' Tax Credit (WFTC) and Disabled Person's Tax Credit (DPTC) and that element of the Working Tax Credit and the Child Tax Credit that is classified as public expenditure under national accounts definitions.

Net public service pensions expenditure is reported on a national accounts basis and represents the difference between the cash paid out during the year and any contributions received for the main unfunded public service pension schemes.

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

BBC domestic services includes the current and capital spending of the BBC home broadcasting service (that is the BBC excluding the World Service and its commercial subsidiaries).

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

Net expenditure transfers to EU institutions include the AME spending component of the UK's contribution to the EU, comprising the Gross National Income (GNI) based contribution less the UK abatement. The other components of UK net payments to EU institutions are either included in DEL, or in public sector current receipts (VAT based contribution). Some contributions, such as CAP expenditure and receipts, have no impact on public sector fiscal aggregates as they score as direct transactions between the EU and farmers in national accounts.

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 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 reconcile the DEL and AME framework of departmental budgets to the national accounts measure of TME, and are shown in Table C14:

Tax credits adds in spending on individuals' tax credits which is scored as negative tax in net taxes and national insurance contributions but as public expenditure in national accounts. As explained in the public sector current receipts section this mainly includes elements of company tax credits and WFTC and DPTC, which were replaced by new tax credits in 2003-04.

Other central government programmes covers various items which relate to central government programme expenditure and where budgeting and national accounts treatment differ, for example the depreciation costs of NHS Trusts and tax credits for companies.

VAT refunds adds back 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.

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

Non-cash items in resource budgets and not in TME includes cost of capital charge, write-offs, notional audit fee, take-up, movements in the value, and release of provisions, the subsidy and bad debt element of student loans, and movement in stocks.

Expenditure financed by revenue receipts adds in certain receipts which are deducted from departmental budgets but which are not treated as negative expenditure in TME.

Local authorities adds in local authority depreciation and subsidies paid to local authority trading bodies, and deducts capital grants from local authorities to public corporations, local authority receipts of investment grants from private sector developers and certain license fees collected by local authorities.

General government consolidation adjusts for the fact that payments of certain taxes, grants and interest that are within the public sector do not score in TME, as TME is a consolidated public sector concept.

Public corporations adds receipts from public corporations of interest, dividends and equity withdrawals that are netted-off in budgets, interest paid by public corporations to the private sector and abroad (as property income paid by the public sector to the rest of the economy is in TME, but not in departmental budgets) and deducts the profit or loss of the Forestry Enterprise.

Financial transactions deducts net lending, acquisition of securities and profit or loss on sale of financial assets.

Other accounting adjustments deducts depreciation and impairments in AME and the cost of over 75 TV licences in AME social security as these represent payments within central government, from DWP to BBC. An adjustment is also made to reconcile to actual and expected national accounts outturn.