

CHAPTER 2 – RESOURCE BUDGET – CENTRAL GOVERNMENT’S OWN EXPENDITURE

Overview

137. The resource budget scores most of the department’s current expenditure. Expenditure is recorded on an accruals basis. So the Resource Budget includes expenditure on pay, current procurement, current grants and subsidies, depreciation, cost of capital charges and the take-up, revaluation and release of provisions (as well as the cash payments associated with the release of the provision – which are recorded by economic type, i.e. pay, current procurement etc as above).
138. Since the resource budget includes the resource consequences of acquiring and owning assets departments should consider the inter-relationship of the resource and capital budgets when planning and monitoring expenditure. That inclusion should also help departments manage their entire asset stock as well as considering annual changes to the stock through new investments or disposals.
139. This chapter covers in detail the treatment of some specific items of departmental expenditure in the Resource Budget. NDPB expenditure scores in budgets in the same way as departments’ – see also chapter on NDPBs. See next chapter for the treatment of income in resource budgets. See separate chapters for the resource budget implications of loans to the private sector, PFI deals, support for local authorities and support for public corporations. See also separate chapters for the rules governing the division of the resource budget into administration budgets/ programme expenditure and near-cash /non-cash.
140. In general, items of central government’s own expenditure taken through the operating cost statement (OCS) score in the Resource Budget. Care should be taken however as not all items in the OCS score in the Resource Budget. For example, capital grants to the private sector go through the OCS and do not score in the Resource Budget. Instead they score in the Capital Budget. See Annex A for a table of the main differences between accounts and budgets.

Grants and Subsidies

141. DRAs do not distinguish between current grants and subsidies and capital grants. However, the national accounts do, with current grants and subsidies affecting the current balance and capital grants not. Therefore departments have to distinguish between current and capital grants according to national accounts principles. Current grants and subsidies score in the Resource Budget; capital grants score in the Capital Budget.
142. Current grants are paid to individuals and to not for profit bodies serving households. Subsidies are current payments paid to profit making bodies designed to influence levels of production, prices or wages.

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143. Capital grants are unrequited transfer payments which the recipient has to use to:
 - # buy capital assets (land, buildings, machinery &c); or
 - # buy stocks; or
 - # repay debt (but not to pay early repayment debt interest premia).
144. Where grants are paid that may be used at the recipient’s discretion either on capital or on current expenditure they should be treated as current grants or subsidies.
145. Normally, debts are written off because the department is unable to enforce the debt against the debtor. Capital grants are imputed in the national accounts in those cases where debts are written off “by mutual consent”, that is, where for policy reasons the creditor department chooses not to enforce the debt. See section on bad debts below.
146. Payments of compensation to owners of capital goods destroyed or damaged by acts of war or natural disasters count as capital grants.
147. Major payments in compensation for extensive damage or serious injuries not covered by insurance policies may also count as capital grants – departments should consult the Treasury.
148. Pensions bulk transfer payments are treated as capital transactions in the national accounts and pass through the resource budget (albeit offset by the release of the provision) – see pensions chapter.

Provisions in Respect of Capital Grants

149. Where departments take provisions in respect of an obligation to pay a capital grant, the take-up, revaluation and release of the provision should score in the Capital Budget, as well as the grant itself.
150. Cost of capital credits on such provisions should normally score in the Capital Budget - see the chapter on Capital Budgets for more information.

Resource Budget Consequences of Asset Ownership

Tangible and Intangible Fixed Assets

151. The impact of tangible (e.g. land, buildings, IT systems) and intangible (e.g. patents, trademarks) fixed assets on the Resource Budget is through depreciation, capital charges and impairments, which score in the Resource DEL, as set out in this guidance. Gains or losses on the disposal of tangible and intangible fixed assets also score in the Resource DEL. Further guidance on the treatment of new capital spending on tangible and intangible fixed assets and investments and on the disposal of assets can be found in the Chapter on Capital Budgets.

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Investments

152. Investments are treated in the same manner as other fixed assets. As they are not depreciated, they normally only impact on the resource budget through the setting of an appropriate cost of capital charge, which scores in the Resource DEL.
153. They should be recorded on the department’s balance sheet at market value with any fluctuations in value being dealt with through the revaluation reserve. However, where an investment suffers an impairment (i.e. a permanent write-off of value) this amount should be included in the resource budget. For further detail on the treatment of different types of investments in public sector bodies outside the departmental boundary, or other financial instruments, please refer to the FREM.

Depreciation

154. Depreciation is a measure of the wearing out, consumption or other reduction in useful life of a fixed asset, whether arising from use, passage of time or obsolescence through technical or market changes. Depreciation is charged on fixed assets annually and scores in the resource budget
155. Accounting policies for depreciating assets are chosen by the Department, as set out in the FREM. Both the Treasury and the external auditor (in most cases the National Audit Office) must agree changes in the rate of depreciation on given class of assets.
156. Depreciation should always be a positive number. If a department nonetheless believes that negative depreciation is appropriate, they are asked to write to their designated contact in the Central Accountancy Team, HM Treasury, explaining the circumstances before tallying their data.
157. To calculate the depreciation charge for budgeting purposes, departments should include all depreciation on all assets, however they were originally funded. In some cases it is appropriate to score an offsetting release from a donated asset or government grant reserve (see below)

Donated / Government Grant Reserve

158. In the case of assets funded from the Lottery or from a Donation from the Private Sector, the depreciation charge will be offset in the accounts and budgets by a release from government grant reserve or the donated asset reserve as appropriate. This is consistent with the special treatment set out in Section 3.3 of the FREM. There is therefore no overall impact on the department’s Resource budget. Despite this offsetting item, depreciation for these items must be recorded in budgets like any other depreciation so that the correct overall level of depreciation is recorded in the National Accounts.
159. With regards to EC funded assets, under the FREM, this special treatment applies where a government department receives a grant from the EC towards funding of a fixed asset. The depreciation charge on these assets is offset in the

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operating cost statement and the Estimate by a release from the government grant reserve. Again, the National Accounts will include depreciation on such assets, so this number needs to be recorded in budgets (albeit then offset).

Impairments

160. Impairments are recorded where there is the permanent loss or write-off of recoverable value of an asset below the value recorded on the balance sheet in the accounts. Impairments score in the Resource Budget alongside the depreciation charge, but are separately identified.

Theft

161. Theft of assets is treated either as stock write down or impairment of fixed assets (i.e. permanent loss of its recoverable value), depending on what is stolen. Either way, the write down or impairment will be shown in the Resource budget.

Cost of Capital Charge

162. There is a cost to the government from holding assets. In economic terms this is the opportunity cost of not undertaking an alternative investment. At the margin this will be the social time preference rate (explained further in the "Green Book" – see Annex C). In financial terms, it could be the interest government incurs on borrowing to finance investment.
163. To ensure that the full cost of services is reflected in accounts and budgets, this opportunity cost is devolved to departments as a cost of capital charge. The charge reflects the opportunity costs of holding assets or committing exchequer funds, and scores in the department’s Resource Budget.
164. The purpose of including the charge is so that departments take management decisions which take account of the value tied up in the assets that they use. Departments have an incentive to dispose of unneeded or underutilised assets in order to free up spending power within their budgets by saving future cost of capital charges.
165. Cost of capital charges apply to the assets of the department and other bodies within the departmental budgeting boundary. Cost of capital credits arise from liabilities and reduce the overall cost of capital charge. So the cost of capital charge applies to net assets (assets minus liabilities). The charge is calculated as a percentage of the balance sheet values of assets and liabilities.
166. The normal rule is that the cost of capital charge is calculated using average values. However, the FReM also permits departments to use adjusted opening values where they apply the same basis for calculating depreciation/ amortisation. This option is designed to facilitate in-year control of capital charges for budgeting.

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167. Currently the cost of capital charge is normally levied at 3.5% real rate (changes in the rate are notified in a PES paper). But there are some exceptions:
- # The cost of capital charge on student loans is set at the same rate as the discount rate used for long term liabilities (see separate chapter on loans);
 - # for loans / equity made to the private sector, it is likely that a higher cost of capital will be appropriate. Departments are asked to agree a suitable cost of capital charge with their spending team in HMT; and
 - # For trading bodies, particularly public corporations, the cost of capital charge incurred by the department will be higher. Please refer to the chapter on Public Corporations.
168. Cost of capital charges on DEL programmes score in DEL, and those on AME programmes score in AME. The only exceptions are the cost of capital charges associated with the roads network and nuclear decommissioning, as well as certain programmes run by the Northern Ireland Executive. These remain in AME under full Resource Budgeting because of their volatility

Differences between Accounts and Budgets on Cost of Capital Charges

169. The cost of capital charge in resource budgets is the same as that in the accounts with these exceptions:
- # charges in respect of public corporations where the department has no investment or where a different capital base is used – see PC chapter;
 - # cost of capital credits on provisions in respect of capital grants normally score in capital budgets (note that where a liability corresponding to a capital grant is classified as a creditor the corresponding cost of capital credit should score in the resource budget in the normal way) – see chapter on Capital Budgets below;
 - # Cost of capital charges on assets outside budgets do not score in budgets. However, departments may include them in the DEL spending if it is not worth the hassle of separating them out. Departments need to operate this policy consistently and not dip in and out of DEL; and
 - # No asset funded by a grant from the Lottery or by a grant from a local authority attracts a cost of capital charge in budgets. Accounts will show a cost of capital charge for such assets.

Budgeting Treatment of Current Assets and Liabilities

Stocks

170. In general terms, stocks will impact on the resource budget only when they are consumed or written off, and through the cost of capital charge on stock holdings. In exceptional instances certain purchases treated as increases in stocks are included in the capital budget – see separate chapter on Capital Budgets.

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171. The total value of stock purchases will be included in a department’s net cash requirement (NCR), which is voted in Estimates. The value of stocks consumed during the year should be included in the resource budget, as should any amounts for stock items that are written off. Stocks should be valued at cost (or current replacement cost). If they will not be used they should be written down to their net realisable value, i.e. the actual or estimated net sale proceeds. This write-down scores in the Resource DEL.

Example:		
Opening balance:	30	
Purchases:	<u>20</u>	(NCR: 20)
Use of stocks	(23)	(Resource DEL: 23)
	==	
Closing balance:	27	

Cash

172. Cash balances do not convey spending power. They only impact on the budget where there is a cost of capital charge.

Debtors - General

173. Debtors are assets, and typically arise when the department has delivered goods and services, but is yet to receive payment, or has prepaid for goods or services. Changes in debtors generally represent a movement in working capital. Debtors in general terms therefore only impact on the budgeting framework through the cost of capital charge, provisions for bad debt, and write-offs.

Debtors – Long Term Debtors and Pre-Payments

174. However in certain cases movements in debtors are more akin to net lending, for example in complex contractual scenarios over an extended timeframe (that is, more than one year). In these cases the budgeting system scores movements in debtors in the capital budget of the department concerned. That scoring is intended to capture and control the impact of what is in effect lending on Public Sector Net Debt, the measure of the Sustainable Investment Rule.
175. Accordingly, departments should treat, as net lending, in their capital DEL the whole amount of transactions that meet both of the following criteria:
- # first, the transaction is either:
 - ~ a long-term debtor or pre-payment (that is a debtor that will last over 12 months at the point that the prepayment is made), or
 - ~ a short term debtor or prepayments where there is an expectation that it will be renewed so that it is in effect long term;

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- # second, the total value of the debtor / prepayment involved is above £20m (where there is a related group of pre-payments, the £20m limit applies to the group).
176. Only for pre-payments made during 2006-07, departments may apply to their normal Treasury spending team for exceptional treatment if they can demonstrate that a pre-payment falling within the category above is not in the nature of lending.
177. There is further guidance on the treatment of pre-payments and debtor assets in budgets in the chapter on capital budgets below.
178. Note that the OCS will show a cost of capital charge on the asset, and in addition if the prepayment is discounted a credit entry as that discount unwinds (the credit entry represents an interest payment from the holder of the prepaid cash). Both these transactions score in the resource budget.

Creditors

179. Creditors are liabilities, and typically arise where a department is yet to pay for goods or services it has consumed or it has received payment in advance of providing the goods or services to which the payment relates. Creditors also affect the resource budget through a cost of capital credit.

Provisions

180. Provisions are one of the most puzzling aspects of accounting for non-accountants. At the same time, the budgeting treatment of provisions is something that many accountants struggle to get to grips with. So provisions is one area in particular where budgeting officers and accountants will need to work closely together in order to arrive at the right result.

What a Provision is

181. A provision is a liability of uncertain timing or amount. A cost is recognised in the departmental resource account when a department has a present obligation (legal or constructive) as a result of a past event, when it is probable that a transfer of economic benefits will be required to settle this obligation, and when a reliable estimate can be made of the amount of the obligation (e.g. early retirement costs). For further guidance on when provisions should be recognised and how to value them please refer to the FREM.

The stages of a provision’s life-cycle

182. The resource budget recognises this cost at the same time that the accounts do. When recording provisions in the resource budget there are 3 key stages:
- # the initial **take-up**, and any **revaluation** (such as the unwinding of the discount, or writing back down of the liability), score in the resource budget;
 - # the **actual payment of cash** to extinguish the liability (or recognition of bad debt) also scores in the resource budget (like any other payment for services or charge for bad debt); and

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- # the **release of the provision** scores as an equal and opposite (negative) amount in the resource budget. These last two items net to zero in the resource budget to prevent both the initial take up (and any revaluations) and the subsequent draw down counting in the resource budget. See however the treatment for the purpose of controls on non-cash and near-cash in Resource DEL in a following chapter.

What the Budgeting System is trying to achieve

183. In departmental accounts the draw down of the provision and the release of the provision are simply a cash movement on the balance sheet (debit liabilities / credit cash).
184. However, the budgeting system recognises both these entries as well as the initial take up and any revaluations that appear in the OCS (or P&L account).
185. This dual recognition is because in the national accounts (the set of economic accounts used to define and measure the fiscal rules) the initial recognition of the liability does not score upfront, rather the actual transfer scores when the cash is paid. Scoring the separate elements to the transaction in this way ensures that the information required for the national accounts is available and allows us to control spending in support of the fiscal framework.
186. This need to support the fiscal framework is a key consideration when looking at the impact of provisions on near-cash and non cash in Resource Budgets (see later chapter).

DEL and AME

187. Provisions in respect of DEL spending normally score in DEL, provisions in respect of AME spending score in AME, and in provisions in respect of non-budget spending do not score in budgets.

Split Treatment Provisions

188. In respect of certain DEL programmes, the initial take up of the provision scores in AME, as does the release of the provision. This means that only the cash payment scores in DEL. These provisions are referred to as *Split Treatment Provisions**. This treatment is only applicable in certain circumstances agreed with HM Treasury, and is only used exceptionally where the provision would be volatile or otherwise unmanageable in DEL.

Provisions in respect of capital spending

189. Certain provisions in respect of capital spending score in Capital Budgets – see chapter on capital budgets.

* Split treatment provisions have the treatment that all provisions had under Stage I of Resource Budgeting.

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Scoring Examples

190. The examples below illustrate the scoring of provisions and related expenditure, in this case making a payment . Note that the transactions in provisions are non-cash and the associated expenditure is normally in near-cash – see chapter on near-cash in Resource Budget DEL below.

Example 1 – Standard Provision in Respect of DEL spending	
Year 1 – Take-up of provision	RB: DEL + £10
Year 2 – Revalue provision upwards	RB: DEL + £2
Year 3 – Release provision	RB: DEL - £12
Make a payment	RB: DEL + £12
	Net RB:DEL £0
Example 2 – Split Treatment Provision	
Year 1 – Take-up of provision	RB: AME + £10
Year 2 – Revalue provision upwards	RB: AME + £2
Year 3 – Release provision	RB: AME - £12
Make a payment	RB: DEL + £12
	Net RB:DEL + £12

Student Loans

191. These rules do not apply to provisions in respect of student loans, whose treatment is set out in the later chapter on loans.

Contingent Liabilities

192. Amounts for contingent liabilities are not included in the resource budget, but they are contained in notes to the accounts, and not recognised as actual liabilities on the balance sheet. Departments should consider in the course of drawing up their budget whether any contingent liabilities are likely to crystallise. If so then these amounts should be treated as creditors or as a provision as appropriate and an expense scored in the Resource budget accordingly.

Bad debts

193. Where a department writes off a debtor, or other financial asset, the OCS will record a charge in respect of that write off and the balance sheet value of the asset will be reduced to zero. The cost in the OCS is a charge to the resource budget.
194. For the national accounts we need to distinguish between bad debts extinguished “by mutual consent” and those extinguished unilaterally.

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Unilateral write off

195. The vast majority of debt write-offs will be because it has become uneconomic to seek to settle the debt, or the debtor has in some way disappeared – through insolvency etc. Where the asset is written off because the asset has become un-collectable this is termed a unilateral write off in the national accounts. No special treatment is recorded for these write-offs – the bad debt scores only in resource budgets in the normal way.

Debts written off by Mutual consent

196. In other cases, the department may choose to write off a debt that the debtor could repay. In these cases, the department has taken a policy decision to write off the debt to free up resources for the recipient; in effect the department has given a gift to the recipient. So these cases are viewed in the national accounts as the giving of a capital grant to the recipient, who on receipt of the grant uses the proceeds to repay the outstanding debt.

197. Although these debts are termed write-offs “by mutual consent” there does not need to be a formal agreement with the debtor. It is enough for the department not to pursue a debt that could economically be recovered.

Effect on the Fiscal Rules of Debts Written off by Mutual Consent

198. The effect on the fiscal rules of a debt write-off by mutual consent is the same as the effect of a unilateral debt write-off: the Government’s debt position is worse off relative to what it would have been had the debt been repaid. The charge to the department’s non-cash resource budget is therefore the same in both cases. However debts written off by mutual consent are recorded separately on COINS so that the imputed capital grant can be shown in the national accounts. That is because a capital grant scores in certain measures which do not include loan repayments, in particular: Total Managed Expenditure, Public Sector Net Borrowing and General Government Net Borrowing.

Budget Treatment of Debts Written off by Mutual Consent

199. The charge to the department’s **resource budget** is the same for both types of grant write-off: the resource budget records a non-cash cost.

Information to HM Treasury

200. Where departments are considering large write-offs of debts by mutual consent – say more than £200m – they are asked to inform the Treasury beforehand. That gives the Treasury warning of the effects on the fiscal numbers.

Insurance

201. Generally departments and public sector bodies do not insure because government as a whole is well placed to absorb the risk, rather than paying to lay off that risk to the private sector. However in certain circumstances departments will have insurance. Payments of insurance premia are current costs in resource DEL.

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202. Where an insured asset is lost, stolen or otherwise written off, a charge will be recognised in the OCS and resource budget to reflect that cost. The subsequent payment from the insurance company should be recognised as income in the OCS and resource DEL in the accounting period in which it was recognised.
203. Replacement of the asset will require the appropriate (most likely capital) budgetary cover.

Notional Insurance Payments

204. Under paragraph 4.5.2 of the FREM, notional insurance should not be shown in the Operating Cost Statement (OCS) or the Vote. Any department that is recording notional insurance should therefore remove it.
205. If any department believes that it should record notional insurance in the OCS or the Vote or the Budget they are asked to write to their normal Treasury spending team explaining the circumstances in order to obtain agreement before submitting data.

Tax Credits

206. Tax credits are transfers of resources made through the tax system. Some tax credits only reduce the amount of tax that an individual or enterprise needs to pay (“non-payable tax credits”). Others may lead in some cases to a cash payment to an individual or enterprise where the amount of the tax credit exceeds the tax liability (“payable tax credits”).
207. Tax credits are included in budgets on the OECD basis of scoring. That is, only the payable element of a tax credit scores in budgets. The payable element means the amount that is paid out in cash to the beneficiary as opposed to being set against their tax liability. Tax credits in budgets normally score in Departmental AME.
208. Where the ONS has determined that for the purposes of UK national accounts a tax credit should be treated as not being integral to the tax system, the non-payable element of the tax credit scores as public expenditure in the national accounts. It is normally excluded from budgets (ie it is in non-Departmental AME).
209. Tax credits are not included in the HM Revenue and Customs resource accounts. Both payable and non-payable tax credits are accounted for in the Trust Statement that reports on tax revenues on the OECD basis.

	Departmental Budget (usually AME)	Other AME	TME	DRAs	Trust Statement
Tax Credits treated as integral part of the Tax System for National Accounts					
Non-Payable Tax Credit	Y	Y	Y	Y	U
Payable Tax Credit – amount offsetting tax	Y	Y	Y	Y	U
Payable Tax Credit – payable amount	U	Y	U	Y	U

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	Departmental Budget (usually AME)	Other AME	TME	DRAs	Trust Statement
Tax Credits not treated as integral part of the Tax System for National Accounts					
Non-Payable Tax Credit	Y	U	U	Y	U
Payable Tax Credit – amount offsetting tax	Y	U	U	Y	U
Payable Tax Credit – payable amount	U	Y	U	Y	U

Notional Audit Fees

210. Notional audit fees score in the department's DEL as resource expenditure within administration costs. The expenditure needs to be separately identifiable on the COINS database in order that it can be removed in the AME accounting adjustments to line up with TME as measured by the National Accounts.

Prior Period Adjustments

211. Prior period adjustments (PPAs) are material adjustments applicable to prior periods arising from changes in accounting policies or from the correction of fundamental errors. PPAs are treated differently in the Operating Cost Statement (OCS), Estimates and Budgets. Suppose that in year 2 a fundamental error is discovered in the accounts for year 1:

- # **OCS:** the asset or liability value on the balance sheet would be restated, and the effect taken in reserves. Nothing passes through the OCS - in accordance with the *FREM*
- # **Budgets:** in the budgets, the year 1 figures will be restated on the database so that they are right. Changes in DEL budget outturns would affect accumulated end-year flexibility entitlements, and so need to be discussed with the Treasury. Changes in budget outturns could also mean that departments turn out to have been in breach of budget limits, in which case appropriate corrective action would need to be taken (see Chapter 1);
- # **Estimates:** for Estimates, appropriate provision needs to be made during year 2 in order to obtain the spending authority that should have been sought for year 1. It follows that a PPA needs to be voted.

212. It is clear therefore that a PPA as an item of expenditure in year 2 is solely an accounts and Estimates concept. In budgets the restated level of spending should be shown in the year to which it belongs – so a PPA is a reason for restating the prior years numbers on COINS. So although the PPA is shown on COINS it is outside of budgets – but the budget number for the previous year should be restated.

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Example

Assume that depreciation on a major type of asset had been incorrectly calculated and was, as a result, grossly understated to the extent that this was a fundamental error.

- # In budgets, the figure in year 1 would be restated.
- # The year 1 accounts would not be altered (as they would be closed), instead the asset value on the balance sheet in year 2 would be restated.
- # In Estimates, the PPA needs to appear as a specific item outside of budgets.

213. Where there has been a PPA in the Estimates for a previous year, the PPA itself will not appear in the provision/ outturn columns in later year Estimates. Instead, the underlying numbers in the previous year will have been restated, and it is the restated numbers that will appear in the provision/ outturn columns.

CHAPTER 3 - INCOME AND RESOURCE BUDGETS

214. Departments may not set income against budgets except where permitted.
215. This chapter:
- # Gives an overview of treatment
 - # Lists the income that may be set against the Resource Budget
 - # Lists income that may not be set against Resource budgets
 - # Describes some of the rules respecting certain sorts of income in more detail
 - # Sets out guidance on the timing of recording income
 - # Sets out guidance on the relationship of Estimates and budgeting treatment
 - # Sets out when departments may obtain the benefit of additional negative DEL income above the levels taken into account in the SR.
216. The same rules apply to NDPBs as to Departments. A separate chapter deals with income in the capital budget. The chapter on loans covers departments' income in respect of loans. The chapter on Public Corporations covers the budget treatment of departments' income from PCs.
217. It follows that income that passes through the DRA OCS may be in Resource Budgets, in Capital Budgets, or excluded from budgets. Income that scores in budgets scores in DEL or AME along with the associated expenditure.

Income Overview

218. In the national accounts some income reduces public expenditure and some finances it. For example, income from payments for goods and services reduces public spending (negative public expenditure), while tax receipts are shown on the revenue side of the government's account and finance spending. The distinction is carried through into budgets following these principles:
- # Income from taxes and other revenue should be pooled so that the spending it finances can be prioritised across the range of government activities; and
 - # Departments that obtain income should spend it where that provides good management incentives.
219. It is the Office for National Statistics acting as an independent agency that determines the treatment of income in the national accounts. Annex C gives links to some guidance notes describing the national accounts treatment of income. Then Treasury determines the budgeting treatment of income. If you are in doubt about the national accounts

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treatment or the budgeting treatment you should approach HM Treasury.

Income treated as negative public expenditure in the resource budget

220. All current income that is classified as negative current public expenditure in national accounts is netted off resource budgets, (although please see section on delegated limits). In addition, certain other income, revenue in the national accounts, is treated as a benefit to the resource budget. To be netted off Resource Budget DEL the income needs to arise in connexion with a DEL programme.
221. The following forms of departmental income are treated as a benefit to the resource budget:
- # Sales of goods and services *
 - # Royalties and associated payments to use Intellectual Property Rights *
 - # Sales of some licences where the ONS has determined that there is a significant degree of service to the individual applicant *
 - # Income from licences and levies, treated as revenue in the national accounts, where the Chief Secretary to the Treasury has agreed that they may be netted off budgets
 - # Income from fines and penalties where the Chief Secretary to the Treasury has agreed that they may be netted off budgets
 - # Income from insurance payments*
 - # Receipts in respect of compensation (where the ONS treat the income as impacting on the current budget)
 - # Interest and dividends where the department is paying the appropriate cost of capital charge on the associated financial asset, for example a loan made to the private sector
 - # Income from rent of buildings * and land
 - # Profit on disposal of asset sales (part of the calculation of capital expenditure in the national accounts)
 - # Those donations that are treated as current in the national accounts (donations can be capital as well)
 - # Income obtained from National Lottery distributing bodies that finances current expenditure
 - # Income from the EC that finances current expenditure
 - # Business * and Non-Business VAT refunds
222. Income that is negative current public expenditure in the national accounts is marked with a *

Income that may not be set against Resource Budgets

223. The following income may not be treated as negative in resource budgets:
- # Taxes, licences treated as revenue in the national accounts and levies, unless the Chief Secretary has agreed to negative DEL treatment
 - # Fines and penalties, unless the Chief Secretary has agreed to negative DEL treatment
 - # Economic rents, other than those classed as rent of land
 - # Income treated as capital including:
 - ~ Developer contributions that are capital in nature.
 - ~ Income from the EC that finances capital expenditure
 - ~ Equity withdrawals / super dividends

Further Guidance on Individual Types of Income

Sales of Goods and Services

224. Sales of goods and services count as negative public expenditure in the national accounts, and hence in budgets, provided they meet certain criteria. In brief:
- # There is a clear and direct link between the payment of the charge and the acquisition by the payer of specific goods and charges. In other words, the transaction should be rather like shopping. The issue of regulatory licences may count as the sale of a service if there is a direct benefit to the person paying for the licence such as providing them with an objective measure of fitness or suitability. And
 - # Unless the good or service is being sold in an open competitive market, the price should not exceed the cost of production (on a full cost basis, including depreciation and cost of capital, but excluding capital expenditure).
225. See Annex C for a link to the guidance note on when transactions are sales of goods and services in the national accounts.

Royalties and Economic Rents

Royalties

226. Royalties is a term from national accounts. Annex C contains a link to a guidance note on the national accounts treatment.
227. In brief, royalties are payments for the right to use produced assets made and sold in an open market, such as inventions given patent protection, computer software, copyright material, artistic and literary originals, and the income from allowing use of a government agency's logo by a commercial organisation.

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228. For something to be a produced asset, it should be of a sort that is or could be produced by the private sector. So an invention made in a government scientific laboratory could be an open market asset, since a private sector firm could have run such a laboratory and made the invention, even if in practice firms do not do research in this area. But if the government has for example a legal monopoly which has led to the creation of the asset, then it is less likely to be seen as an open market asset.
229. Royalties from the use of intangible assets made and sold in an open market are treated as income from the sale of good and services. The allowable cost is the market value of the royalty – in essence, what the market will pay. So the whole of the amount paid for the asset, good, or service may be treated as negative public expenditure.

Capital or Current?

230. It may be difficult to tell whether a one-off payment covering a number of years is for the sale of an asset or an upfront payment in respect of a number of years' royalty. Similarly, it may be hard to test whether a payment spread over a number of years is for the sale of an asset or a current royalty.
231. The tests used by commercial or GAAP accountants applying Financial Reporting Standard 5 - *Reporting the Substance of a Transaction*, will be a guide as to whether a capital asset has been sold or rented out. For larger cases, departments should consult the Treasury to ensure that they are treating the income in accordance with the national accounts.
232. In general:
- # a sale leading to a current receipt - royalty for the use of an asset - would be a sale offering the user a right to use the asset for a period of time, but underlying ownership of the asset or resource would stay with the vendor. Changes in the value of the asset would not normally affect the user as they would not be able to sell on their rights; but
 - # capital income - sale of an asset - would be when the buyer had obtained:
 - ~ all significant rights or other access to benefits relating to that asset; and
 - ~ all significant exposure to the risks inherent in those benefits.
233. Ownership rights would typically include unimpeded use of the asset, right to resell the asset and benefit or suffer from changes in the value of the asset. Typically, capital income is shown as a single entry in the accounts at the time of sale, but the cash may come in tranches (deferred consideration). Where the asset has been sold outright, the income is capital and the whole of the income is to be treated as negative public expenditure.

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Economic Rents and other Cases that are not Royalties

234. “Royalty” may be used in a number of cases other than the national accounts meaning of the term. These cases may not be netted off budgets as royalties:

- # royalties/ sales/ rents in respect of assets created in nature, eg North Sea Oil, the radio spectrum, or water. Such income is normally classified as economic rent, and is revenue in the national accounts (but see “rent of land” below); and
- # royalties / sales in respect of concessions or franchises given by the government to run a commercial or government operation

Taxes, Licences (treated as revenue in the national accounts) and Levies

235. Taxes, licences treated as taxes, and levies are compulsory unrequited payments to general government. “Unrequited” means that the payer obtains nothing personal in return. That includes not only obvious taxes like Income Tax, but also cases where a tax is hypothecated, perhaps to provide services generally for business in an area, or to recover costs from businesses that are in general the cause of some harm that needs to be remedied (eg pollution).

236. In exceptional cases, the Chief Secretary to the Treasury may agree that taxes be netted off budgets. The Chief Secretary will bear in mind the criteria below when considering applications:

Criteria to be applied to licences and levies:

1. The service delivered should be closely linked to the payer of the licence or levy, either because they are the beneficiaries of the service, or because they are the cause of the expenditure being incurred;
2. The licence or levy is appropriate, i.e. applied in the economically most advantageous way in the circumstances;
3. Introducing the levy or licence should not materially restrict the Government’s fiscal policy (as currently embodied in the Golden Rule, and the Sustainable Investment rule);
4. The activity financed by the levy or licence must further the Government’s economic goals;
5. Netting off the income would improve the efficiency with which resources are allocated eg because of a difficulty in otherwise matching resources to unpredictable changes in externally driven demand. There needs to be a clear advantage over DEL funding.
6. Where appropriate, charges should be set using the principles of the Fees and Charges Guide, and surpluses would have to be surrendered;
7. There should be adequate efficiency regimes in place to keep costs

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down, including stretching targets and regular efficiency reviews, often tied in with the biennial Spending Review;

8. Day-to-day decisions on the level of charges and an efficient level of costs should be taken separately from the body raising the levy, to prevent abuse of its monopoly power. Normally this would be by the departmental minister.
9. There will be periodic reviews involving the Treasury, of the operation of the licences and levies, including: whether they should exist at all; whether netting off remains the most appropriate means of funding; what scale of activity is appropriate; and the level of charges set. The periodicity of the review shall be set as part of the agreement to allow netting off

237. Departments who wish to propose that tax income be netted off DEL should contact the Treasury for advice as to how a submission should be compiled. See Annex B for contact details.

238. Netting off proposals should be linked to the Spending Review. The following guidance will therefore apply from the next SR: *Proposals for income to be newly netted off DEL should be made as part of the SR and to the SR time-table. Cases will only be considered outside the SR process if departments can demonstrate that they could not reasonably have been foreseen at the time of the SR.*

Fines and Penalties

239. Fines and penalties are compulsory unrequited payments to general government that are in the nature of a punishment.

240. In exceptional cases, the Chief Secretary to the Treasury may agree that fines and penalties be netted off budgets. The Chief Secretary will bear in mind the criteria below when considering applications:

Criteria to be applied to fines and penalties:

1. Will performance against policy objectives, e.g. crime fighting and prevention, be likely to be improved?
2. Are arrangements in place which will ensure that the activity will not lead to the abuse of fine and penalty collection as a method of revenue raising, and that operational priorities will remain undistorted?
3. Will revenues always be sufficient to meet future costs, with any excess revenues over costs being surrendered?
4. Can costs of administering the programme be readily identified and apportioned without undue bureaucracy, and with interdepartmental and inter-agency agreement, where necessary?
5. Can savings be achieved through the change (from a normal DEL funding regime to a netting off regime), and are adequate efficiency regimes in place to control costs, including regular efficiency

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reviews. The periodicity of the review shall be set as part of the agreement to allow netting off, and will involve the Treasury. It will consider whether the fines and penalties should exist at all; whether netting off remains the most appropriate means of funding; what scale of activity is appropriate; and the level of fine set.

241. Departments who wish to propose that fine income be netted off DEL should contact the Treasury for advice as to how a submission should be compiled. See Annex B for contact details.
242. Netting off proposals should be linked to the Spending Review. The following guidance will therefore apply from the next SR: *Proposals for income to be newly netted off DEL should be made as part of the SR and to the SR time-table. Cases will only be considered outside the SR process if departments can demonstrate that they could not reasonably have been foreseen at the time of the SR.*

Dividends and Equity Withdrawals

243. A dividend is a payment made to a shareholder in consideration of having put equity finance into a body. The equity finance may be in the form of Companies Act shares, Public Dividend Capital or the implied equity in a statutory public corporation. Public sector bodies may hold equity in other public sector bodies or in private sector organisations. Dividends are payments made out of current earnings.
244. If dividends are greater than the profits of the current and two previous years – super-dividends - they count as equity withdrawals in the national accounts (a financial transaction as opposed to a current receipt in the National Accounts). Equity withdrawals count as capital income for budgeting. A more detailed definition of when a payment is a dividend as opposed to a withdrawal of equity for budgeting purposes is given in the PC chapter.
245. In DRAs, reductions of equity in the form of sales of shares or PDC reductions would not normally go through the OCS. But special payments from bodies that are not accompanied by actual reductions in equity holdings would go through the OCS; they may be termed super-dividends. Such super-dividends would be equity withdrawals in the sense above.
246. “Dividends” received from bodies within central government, including joint ventures classified to the central government sector, are not dividends but transfers within government and as such are not generally treated as negative in budgets.

Rent of buildings / land

247. Income from the rent of buildings and land counts as negative expenditure in budgets.
248. In addition to the rent of land, this heading includes rents payable to the owners of inland waters and rivers for the right to exploit such waters for recreational and other purposes. Rent of land does not include rents on sub-soil assets, or of other natural assets (spectrum &c).

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249. Any proposal to treat as negative DEL rent other than the conventional rent of land or buildings needs explicit Treasury agreement
250. Note that rent of land is treated as a benefit to the resource budget, even though it is revenue in the National Accounts.

Profit / loss on sale of assets

251. DRAs divide the proceeds from the sale of an asset into an element that covers book value and a profit or loss on disposal.
252. The book value is a benefit to the capital budget.
253. The profit / loss on sale is in the resource budget. Profit is a benefit to the resource budget (negative spending) while loss is a cost (positive spending).

Treatment of Asset Sales in the National Accounts

254. In the national accounts, capital expenditure is recorded net of income from sales of capital assets. The national accounts do not separate the profit/loss on disposal from the book value element of sales income. Both of those components of the transaction are taken through the capital account of the national accounts.
255. That treatment explains why profit/loss on disposal is treated as part of non-cash in the division of the Resource Budget into near-cash and non-cash – even though profit/loss clearly is associated with cash. Profit/loss on disposal is not an influence on the Golden Rule, since achievement of the Golden Rule is measured by reference to transactions on the current account.

Donations

Donations that may be netted off

256. Donations may benefit either resource or capital budgets: capital donations are dealt with in chapter 7. Donations in kind are not normally included in budgets.
257. Donations have to be entirely voluntary. They have to be unrequited - that is the donor should receive no direct benefit in return. They also have to come genuinely from outside the body that receives them, ie not be financed or backed in some way by the recipient. Departments and public bodies may net off the donations that are made to finance expenditure for the common good and that are directed by the donor to a specific project, programme or body, for example:
- # a current gift left in the collection box of an individual museum to be spent at that museum's discretion;
 - # sponsorship funds raised for a specific venture to the benefit of the public.

Donations that may not be netted off

258. Departments should exclude such donations from budgets. Examples of donations that may not be netted off include:

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- # donations which related to income that would otherwise be classified as revenue anyway, for example, conscience money (people guiltily and voluntarily paying over money in respect of past unpaid tax); and
- # donations that relate directly to the public sector's balance sheet - eg legacies to reduce the national debt.

Income from National Lottery distributing bodies

259. The Government's hypothecated income from the National Lottery is a tax. The spending by the National Lottery distributing bodies counts as expenditure in AME.
260. Where a Government department or NDPB that is not a National Lottery distributing body obtains income from a distributing body to finance spending in the Resource Budget DEL it should take the income into budgets as negative Resource Budget DEL

Income from the European Community

261. Income from the EC may be netted off Resource Budget DEL if it is in support of DEL spending and if it supports current expenditure.
262. It is government policy that departments should fully take up the UK's structural funds allocation, and that EC money should be used where it supports programmes that are value for money.
263. Departments are reminded that the European Community is funded by Member States, including the UK. Our contribution to the EC budget means that each £1 of income has cost the Exchequer £0.14 in the gross contribution alone. Moreover, given the UK's budget rebate or abatement, receipt of these monies in practice costs the Exchequer about £0.71 in the £1. So EC income is not free to the UK.
264. That makes it particularly important that departments ensure that they claim discretionary EC income only in support of programmes that are good value for money.

VAT Refunds

265. Departments' budgets should be set net of any recoverable VAT. Departments may retain VAT refunds for business activities and also for certain non-business activities.

Wider Markets Initiative

266. Income may be generated from activities under the Wider Markets Initiative – see Annex C for the link to the main policy paper. To decide whether such income should be set against budgets, please refer to this chapter, in the same way that you would for all other income. That the income is generated from Wider Markets activities does not of itself determine the correct treatment.

Timing of Recording of Income

267. In general, for sales of goods and services, interest, and dividends, departments should record income for budgets at the same time as they record it for accounts.
268. Taxes and economic rents that are in budgets should be recorded for budgeting purposes at the time that the income falls due, that is, the period of assessment for the tax.
269. In some cases where for example taxes are closely hypothecated, DRAs may record taxes so as to match the timing of work done by the department, rather than the timing of the period of assessment. In cases where departments are trying to match income to expenditure in each year, and the difference in recording in DRAs is simply reflecting the inevitable minor mismatches of income and expenditure, departments may follow the DRA treatment.
270. However, where departments are as a matter of policy seeking to advance or delay the collection of taxes compared with the timing of spending, departments must record taxes for budget purposes in the period of assessment, even if that opens up a difference from DRAs.
271. Taxes and economic rents are not separately identified in DRAs. Departments should use the national accounts categorisation of income to identify which income counts as taxes or economic rents. That may include not only obvious taxes but also certain licence fees and similar income.

Budget and Estimates Treatment of Income

272. Note that while the budgeting treatment of income influences the treatment in Estimates, the reverse does not apply. So for example:
- # In Estimates, income may normally only be appropriated-in-aid against related expenditure in the same part of the Estimate. That restriction normally means that the income is given the same budgeting treatment as the expenditure to which it relates. So, income that is negative DEL in budgets may be appropriated-in-aid of related DEL expenditure in the Estimate. The same would apply to income and expenditure in AME, or even outside of budgets. But income that is outside budgets may not normally be appropriated in aid of DEL spending. So you need to know the budgeting treatment of income before you can work out the Estimates treatment;
 - # However, whether income has been appropriated-in-aid or treated as a Consolidated Fund Extra Receipt (CFER) does not necessarily tell you anything about the budgeting treatment. You may have negative DEL CFERs and non-budget appropriations-in-aid. So you need to address the budgeting treatment separately from the Estimates treatment.
273. “Appropriation in Aid” and “CFER” are Estimates terms. They are often mis-used to indicate budgeting treatment (A-in-A for negative DEL and

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CFER for non-budget). However, since the budgeting treatment does not follow from the Estimates treatment that usage risks confusion. We recommend using distinct terms for budgets, such as “negative DEL” or “non-budget” income when describing the treatment of such flows in respect to budgets.

When Departments may keep additional negative DEL income

274. In many cases current income does no more than cover the costs of production of the activity to which it relates. For example, fees and charges are typically set so as to recover no more than current costs (including depreciation and cost of capital charges).
275. To ensure that they obtain the right level of income from such sources, Departments will want to consider whether they have any services where less than full costs are currently recovered and which should move towards full cost recovery, or other services which may be appropriate candidates for the introduction of user charging.
276. In other cases, income can generate returns that far exceed current costs of production, for example licensing the exploitation of an invention in the open market. In these cases the Government has to balance two considerations:
 - # Departments should be encouraged to obtain such income by being allowed to retain and spend it; and
 - # Government funds should be prioritised across the whole range of spending to where they would do most good.
277. And we need to keep the rules simple.
278. Departmental budgets are set in the SR net of negative RDEL income. So the SR settlement has to be informed by the expected level of negative RDEL income. So, the SR process should be used to identify the expected level of Department’s income, any expected changes, and an assessment of the potential for new income. That will look especially at the prospects of moving under-performing services towards full cost recovery and/or identifying new sources of income from user charging. The SR settlement will include an explicit statement of the expected level of income in the years of the SR period.
279. The Treasury encourages Departments to engage in **Wider Market** activities. Not only does the income they generate support public spending, but also undertaking pioneering or inventive activity can enhance the skill set of civil servants, and can lead to more innovative provision of public services. The SR provides an opportunity for challenging departments’ expected level of such activities and encouraging departments to exploit spare capacity. At this stage in the evolution of the Wider Markets initiative, the Treasury believes that it creates a helpful incentive for Departments to be allowed to keep wider markets income that scores as negative DEL, and will set Departmental Expenditure Limits in this spirit.

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280. Departments will be allowed to keep the negative DEL income that they obtain in the SR period up to the amount that was taken into account in the SR. Income cannot be predicted wholly accurately, and the Treasury wishes to encourage departments to find new income streams where appropriate. Departments may therefore in any year also retain negative RDEL income up to 20% above the level envisaged for that year as part of the SR settlement without an adjustment to budgets.
281. In the case of the SR04 period, for those departments where the SR settlement did not clearly set out an expected level of income, departments may in any year retain total negative RDEL income up to 5% of spending in Resource DEL without an adjustment to budgets.
282. If departments expect to obtain more negative RDEL income than provided for above, they should talk to the Treasury about whether they may retain all or part of the income without an adjustment to budgets. When considering proposals, the Treasury will wish in particular to encourage Wider Markets activity where opportunities could not be foreseen at the time of the SR and other cases where the additional income represents the results of positive management action, as opposed to under-forecasting.

CHAPTER 4 – ADMINISTRATION BUDGETS

What are Administration Budgets?

283. In Spending Reviews, Administration Budgets are set for most central government departments (incorporating their agencies) unless specific exemptions have been agreed. At present, the Ministry of Defence, the Export Credits Guarantee Department, the Forestry Commission and trading funds are excluded from the regime. Although devolved administrations are not set Administration Budgets in Spending Reviews, these bodies operate their own arrangements for constraining the costs of running central government.
284. Expenditure that does not fall within Administration Budgets set in Spending Reviews is known as programme expenditure.

The Boundary between Administration Budgets and Programme Spending

285. Administration Budgets cover the costs of all central government administration other than the costs of direct frontline service provision or support activities that are directly associated with frontline service delivery. In practice Administration Budgets include activities such as provision of policy advice, business support services, back-office administration of benefits, advice on and administration of grant programmes, technical or scientific support, and the work of the Government's Regional Offices.
286. To illustrate the boundary between front line and other staff, the table below sets out some of the activities that have recently been reclassified out of administration budgets along with the rationale. The reclassifications were approved by the Chief Secretary to the Treasury.

Activity	Rationale
Consular services	The Consular service offers front line consular assistance to UK nationals in difficulty or distress abroad.
Immigration and nationality work	Asylum caseworkers and immigration officers at ports and airports provide frontline services.
Prison establishments	Keeping in custody those who have been committed by the courts represents a front line service. In addition, with the creation of the National Offender Management Service the scoring of prison establishment costs needed to be aligned with the costs of the probation service (which already scored outside administration costs).
Administration of NHS pensions	In effect, part of the direct costs of managing the NHS. Other such NHS management costs already score as programme

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ACAS	ACAS provides information, advice, training and works on the front line with employers and employees to solve problems and improve performance. In addition, ACAS is an NDPB, nearly all of which are in programme already.
Crown Prosecution Service	Public prosecution (including lawyers working in courts and counsel) represents a front line service. Prosecutors also work directly with police and other services, which are mainly funded from outside administration costs.
Court Service	The equivalent costs for magistrates' courts are outside admin budgets and consistency is needed for the creation of the Unified Courts administration.

287. To keep the number of reclassifications to manageable levels, the Treasury is only willing to consider cases that represent a substantial body of on-going work. Also, the merits of very substantial reclassifications need to be weighed against the potential effects on the Administration Budgets regime overall as well as presentational and timing issues.

Definition of Administration Budgets

288. Administration Budgets are simply a sub-set of Resource DEL and share most of the characteristics of DEL. They are set net of negative DEL that relates to administration expenditure. The chief components of expenditure within Administration Budgets are:

- # **employee costs**, including civil service pay, superannuation, training, travel and subsistence;
- # current expenditure on **accommodation**, including rent, rates and maintenance;
- # current expenditure on **office services** including stationery, postage, telecommunications and computer maintenance, etc.;
- # current expenditure on comparable **contracted-out services** (including some consultancy costs, see below);
- # **depreciation and cost of capital** charges incurred carrying out activities falling within administration costs (and where fixed assets are used for both administration and programme work, these costs should be apportioned);
- # **cost of capital charges on working capital** related to activities falling within administration costs (and where it is not possible to analyse the cost of capital between administration and programme expenditure, these costs should be charged to the more significant of the two); and
- # **Other non-cash items** such as auditors' remuneration and expenses, loss or gain on disposal of fixed assets held for

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administration purposes, and provisions for early departure costs.

Consultancy costs

289. Consultancy fees and contract charges should be charged against Administration Budgets where the consultancy relates to some component of administration expenditure listed above, or where the work carried out might otherwise be carried out by staff funded from Administration Budgets. This includes:
- # Any costs associated with out-sourcing of support services. For example: payroll services, omnibus building service charges under PFI or other accommodation contracts, departmental switchboards, etc.
 - # Provision of policy advice or support by consultants employed in substantially the same role as if the work were being carried out by a civil servant.
290. This rule is designed to avoid any perverse incentive to contract out functions, or use consultants in place of civil servants, simply because the resulting work would then be charged under programme costs. Decisions on how support or policy services should be supplied should be made purely on an assessment of what offers the best combination of value for money and effectiveness, rather than because programme cover may be more readily available than administration cost cover or vice-versa.

Allowable income

291. Departments may offset negative Resource Budget DEL income relating to administration costs against their Administration Budget. This includes income from NDPBs and other UK public sector bodies that are outside the administration costs regime.

Comparability with Departmental Resource Accounts

292. Departmental Resource Accounts must include a note reporting outturn against final Administration Budgets.
293. The element of net operating costs that falls with Administration Budgets is reported in the Operating Costs Statement as net administration costs. The only differences between outturn against Administration Budgets and net administration costs are the differences that apply generally between the Operating Costs Statement and Resource Budget set out in Table 1 of Annex A. Differences will not generally arise from scoring of NDPBs, local Authorities, public corporations or NHS trusts as these all fall outside Administration Budgets.

Approval for Changes to Administration Budgets

294. All changes to Administration Budgets – including changes to expenditure and income provision within Administration Budgets – require Treasury approval.

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295. HMT spending teams may give approval at official level for:
- # Some increases to the Administration Budget, including:
 - ~ funds allocated under the Invest to Save Budget;
 - ~ transfers between departments where the overall effect is neutral; and
 - ~ draw-down of Administration Budget End-Year Flexibility.
 - # changes to expenditure and income provision within Administration Budgets where the Administration Budget itself remains unchanged or is reduced.
296. Approval from the Chief Secretary to the Treasury is required for most other increases to the Administration Budget. In particular:
- # increases involving claims on the DEL Reserve (other than the draw down of Administration Budget EYF);
 - # transfers from programme funds.

In-year control

297. As with all spending, departments or agencies and their Accounting Officers have to take ultimate responsibility for ensuring an outturn within Administration Budgets. Outturn which exceeds an Administration Budget constitutes the breach of a budget and will be subject to the arrangements set out in Chapter 1.
298. Administration Budgets include both non-cash and near-cash spending in Resource Budget DEL. Switches between these components are allowed provided they do not conflict with the overall controls on near-cash and non-cash set out in a subsequent Chapter.

End year flexibility

299. Departments are eligible for 100 per cent End Year Flexibility (EYF) on their Administration Budgets. Administration Budget EYF is held separately from other Resource and Capital DEL EYF. Normally neither other Resource or Capital DEL EYF may be used to supplement administration costs budgets in future years. However, any Resource underspending (on Administration Budget or other Resource DEL) will be used, in the first instance, to recoup Resource DEL Reserve claims.
300. Where Departments agree with the Treasury a transfer of functions out of Administration Budgets into programme costs then an adjustment will need to be made to their EYF distribution. Administration Budget EYF should be reduced (and programme EYF increased accordingly) in proportion to the amount of expenditure being moved from administration costs.

Estimates & administration budgets

301. The Estimates treatment of income (ie, whether the income is appropriated-in-aid or CFERed) does not impact on whether or not the income is treated as negative administration budgets. Departments

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must note that, although the administration budget is not specifically voted as a limit by Parliament, it is included within the department's Supply Estimate and any breach of the limit will lead to an Excess Vote. Detailed guidance on administration costs and Estimates is available in *Government Accounting*.

CHAPTER 5 – NEAR-CASH IN RESOURCE DEL

302. This chapter applies to the element of Resource Budget DEL which impacts directly on the Golden Rule – near-cash. Near-cash in Resource DEL is a control total.
303. The chapter should also inform the management of Resource Budget AME programmes which include material amounts of both non-cash and near-cash spending. The budgeting system does not distinguish between these concepts in Capital Budgets.

What we are trying to Achieve

304. The framework for managing public spending has two objectives:
- # to support the fiscal rules; and
 - # to enable public spending to be planned and controlled in a way that improves the quality and cost-effectiveness of public services.
305. The fiscal rules are measured on a national accounts basis. Although national accounts are mostly consistent with the GAAP basis we use for Departmental Resource Accounts, there are some differences, including:
- # a different measure of depreciation is used;
 - # national accounts do not include cost of capital charges;
 - # rather than scoring the creation and revaluation of provisions, national accounts score the related cash flows.
306. Near-cash is that element of Resource Budgets that corresponds most closely to the measure of current expenditure that affects the current balance in the national accounts, used to assess performance against the Golden Rule. So we aim to control near-cash to support the fiscal rules.
307. The fiscal rules are concerned with how much needs to be raised now by way of taxation and borrowing. They are measured on an accruals basis. So they generally focus on spending that normally involves a cash payment at, or near to, the time the expenditure is made. For example, staff costs accrue as the time is worked and staff are paid soon after i.e. at the end of the month. So pay is an expenditure item in the measurement of the Golden Rule.
308. Near-Cash is defined as accruals measures of transactions that normally turn into cash flows soon. So the main components of near-cash in resource budgets are: pay, current procurement, grants and subsidies to the private sector and subsidies to public corporations. Near-cash also covers amounts paid out that are covered in budgeting and accounting terms by the release of provisions. A full table of definitions is at Appendix 1 to this chapter.
309. Non-cash items are included in budgets to ensure that departments' budgets reflect the full economic cost of their activities even though

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Chapter 5 – Near-Cash in Resource DEL

there is not a direct link to departments' cash flows in the relevant period. These will either never require a cash payment as such (e.g. cost of capital charges, which have an indirect correspondence with the Government's debt interest charges) or will only give rise to cash payments years into the future (e.g. provisions).

310. Depreciation is in the calculation of the Golden Rule, but on a different measurement basis from the figure in DRAs. So for the purposes of the control regime depreciation in budgets is outside near-cash.
311. Profit and loss on disposal of assets does show up as a cash flow: the total income from asset sales will be the sum of net book value plus profit/loss on disposal. However, in the national accounts the whole of the income is a benefit to the capital account, with no split into net book value and profit/loss. So profit and loss on disposal do not affect the Golden Rule, which relates to current transactions only. And hence profit/ loss is treated as non-cash in resource budgets, where we are focusing on control in support of the golden rule.
312. Appendix 2 to this chapter shows how the main non-cash costs score in accounts and budgets.
313. At the same time, we wish to encourage good management. Departments are expected to manage non-cash costs with the same rigour as all other elements of their budgets.
314. So, where ongoing savings in the level of non-cash are made as a result of improved decision-making, the savings in Resource DEL should be deployed where they will do most good, whether non-cash or near-cash, subject to the constraints set out below.

Near-Cash in Resource DEL and the Spending Review

315. Near-cash in Resource DEL is a control total. The expected level of all near-cash spending (on a slightly different definition from that in this guidance) was set out in departments' Spending Review 04 settlement letters, and settlement letters for the next SR will set out near-cash spending plans

Flexibility between Near-cash in Resource DEL and non-cash elements of Resource DEL

Non-Cash to Near-Cash in Resource DEL

316. Where ongoing savings in the level of non-cash are made as a result of improved decision-making the Treasury will not block a managerially worthwhile switch except in those cases where the switch really represents a risk to the fiscal framework.
317. Departments may therefore make switches resulting from improved management decisions of up to £20 million in total per financial year without specific Treasury approval. However, Departments and Treasury spending teams should track such changes so that they always know what the approved level of Near-Cash in Resource DEL spending is. In the normal way the Estimates approval process may

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provide a suitable opportunity, as spending teams will need to approve any resulting increase to the Net Cash Requirement.

318. All other switches must be agreed with the Treasury. Unless they threaten achievement of the Government's fiscal rules, the Treasury will not, in general, block switches which:

- # represent departments' legitimate responses to the very incentives Resource Accounting and Budgeting is intended to bring; or
- # are the manifestation of better financial management within departments.

319. Thus, for example, unless it is unaffordable fiscally, the Treasury is likely to be sympathetic to switching into near-cash where non-cash resource are freed up due to:

- # reductions in depreciation and/or cost of capital arising from changes that both represent value for money and are consistent with discussions departments have had with Treasury in Spending Reviews and subsequently about capital expenditure plans (e.g. an improvement in the management of assets which lengthens real asset lives, faster than expected progress on stock or fixed asset disposal plans, lower than expected capital expenditure while still meeting PSA targets for service delivery or changes arising from acceleration of a policy on PFI);
- # higher forecasts of downward revaluation of provisions compared to plans where these changes arise from beneficial management action (e.g. action which has reduced the level of bad debts or legal claims against the department); or
- # a change in accounting policy that had already been agreed with HMT or where there is a clear improvement in the quality in accounting.

320. The corollary is that the Treasury would not be sympathetic to switches where reductions in non-cash requirements arise from inadequate forecasting, poor data or changes in accounting treatments which are not driven by virtuous rationales.

321. The Treasury will also consider sympathetically non-cash to near cash switches where a liability is discharged by a **pensions bulk transfer** to a real fund.

Near-Cash in Resource DEL to Non-Cash

322. Departments are free to move provision from Near-cash in Resource DEL to non-cash within Resource DEL.

Policy Ring-Fences

323. Where spending is subject to specific policy ring-fences, these apply as well as the general restrictions on moving money between near-cash and non-cash.

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324. So savings on ring-fenced provision may not be used to increase spending elsewhere
325. However, unless a closer control has specifically been provided for, the policy ring-fence applies at the level of the Resource Budget/ Capital Budget. So if provision for near-cash within a ring fenced budget is switched to provision for non-cash within the ring-fenced budget, non-ring-fenced near-cash provision may rise by the same amount. Departments may be asked to demonstrate that the non-cash element within the ring-fenced budget is needed for that programme. The same point applies to administration expenditure within policy ring fences.

Outturn against plans

326. Outturn higher than the final level of near-cash provision (i.e. after making use of the flexibilities and any agreed in-year switches) would be subject to the same breach procedures as for Resource Budget DEL (see Chapter 1).
327. Overspending on non-cash Resource Budget DEL would not be regarded as a breach provided it did not lead to an overspend on Resource DEL as a whole.

End-Year Flexibility

328. End Year Flexibility attributable to Near-cash in Resource DEL is identified separately in the Public Expenditure Outturn White Paper. Departments are not permitted to apply non-cash EYF to near-cash spending in Resource DEL.

Cash and Near-Cash

329. Cash is not the same as Near-Cash. Near-Cash is an accruals measure of certain spending in the resource budget, as described in this chapter, while cash is cash.
330. Note that measures of cash (including “cash required by operations” in accounts and the Net Cash Requirement (NCR) in Estimates) will have a different coverage from Near-Cash in Resource Budget DEL. For example, capital expenditure impacts on the NCR and capital grants on cash required by operations; neither cash measure is divided into DEL and AME.
331. Therefore, departments should monitor and control Near-Cash in Resource Budget DEL directly, just as they do Resource Budget DEL overall and Administration Budgets.
332. However, departments may find it helpful to monitor cash and use unexpected increases in cash outflows as a trigger to check whether Near-Cash spending is rising above expectation. However, because of the differences referred to above, that cash outflows are in line with expectations does not prove that Near-Cash is under control.

Ministry of Defence

333. The Treasury has agreed with the Ministry of Defence tailored arrangements for the control of non-cash to near-cash switches, including a specific definition of near-cash. Accordingly, the specific guidance in this Chapter does not apply to MoD.

APPENDIX 1 TO CHAPTER 5: DEFINITIONS IN TERMS OF ACCOUNTING CODES

High Level Recording

334. Under COINS the boundaries between DEL, AME and non-budget spending are maintained by Programme Objects, while the Resource/Capital boundary is maintained by reference to the Budget Category Tags attached to SCOA codes; which themselves record the economic nature of the transaction being recorded . It follows that **RDEL** equals

Programme Object = DEL *and*

Budget category tags (tags associated with SCOA's) with the following values:

~ B-CON *plus* B-C-N

plus

~ B-NCH *minus* B-C-N

335. This formula simplifies to the sum of B-CON and B-NCH inside DEL.

336. To select Near Cash in RDEL or Non-cash in RDEL the full formula for each component should be used. In other words:

Near-Cash is defined as B-CON *plus* B-C-N

Non-Cash is defined as B-NCH *minus* B-C-N.

337. The formula works also to derive Near-cash in **AME**, if programme objects with AME characteristics are used.

338. Note: The **B-C-N** tag is used where provisions on the balance sheet are utilised, and ensures that both the cash utilisation and non-cash release of the provision score in budgets. So amounts recorded on B-C-N are added to Near-Cash budgets and subtracted from Non-Cash budgets.

Economic Category Recording

339. On COINS the economic substance of a transaction is described by the account code, as defined in the SCOA. Spending may also be divided into near-cash and non-cash according to groupings of economic categories. The tables below show the standard attribution to near-cash and non-cash of the main economic categories. This attribution is consistent with the attribution to budget category tags shown above.

340. When using the tables:

There are some economic categories not listed below. Where departments use such codes for spending within Resource DEL they should refer to the Treasury for guidance on whether the spending would be near-cash or non-cash;

In spite of inclusion in the list below, some of these economic categories, eg W15, are only exceptionally to be used in RDEL;

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- # Where a department has unallocated non-cash expenditure they are asked to talk to their Treasury spending team;
- # Where a department identifies special circumstances which suggest that the attribution of ECs to near-cash or non-cash in the tables is not appropriate, the department should contact HM Treasury.

Near Cash

A15	Pay and pension costs
B35	Current expenditure on goods and services
B45	Receipts treated as negative DEL and as revenue in national accounts
B60	Payments and receipts of rent of land (not buildings)
B80	Receipts of donations
C10	Subsidies to the private sector.
C20	Subsidies to central government and local authority market kind of activity units, and quasi corporations
C35	Subsidies to public corporations
C50	Subsidies that are generally available to the private sector
D10	Current grants to the private sector
D20	Current transfers abroad
D40	Public sector occupational pension schemes: pensions in payment/receipts of pensions contributions
D90	Departmental Unallocated Provision/ current expenditure to which an EC cannot be assigned *
E20	Renewals maintenance expenditure (use with HMT approval only)
K30	Dividends paid to or received from the private sector and the Bank of England
K40	Dividends paid by public corporations to central government
M10	Current grants to local authorities within AEF/AEG
M15	Current grants to local authorities outside AEF/AEG
M20	Uncapitalised grants to local authorities covering loan charges
M30	Current grants made by the European Communities to local authorities
M40	Non-Domestic Rates
S10	Payments of interest to and receipts of interest from the private sector
S15	Payments of interest to and receipts of interest from local authorities
S20	Central government's payments of interest to and receipts of interest from public corporations
S25	Payment of interest to, and receipts of interest from, abroad
S30	Interest payable on finance leases (to the private sector)
T30	Public corporations' profits or losses
W15	Grant in aid to Non-Departmental Public Bodies in the central government sector
W16	Payments by one central government body to another, and corresponding receipts
W40	Interest payments/receipts within central government

Non-cash

B38	Notional audit fees
B85	Bad debts relating to pay, procurement and capital
B86	Bad debts relating to loans, grants and transfers
B90	Depreciation (departments, agencies and NDPBs)
B92	Release from Donated Assets Reserve
B95	Impairments of fixed assets

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- B98 Cost of capital charge relating to loans and public dividend capital in respect of public sector bodies
- B99 Cost of capital charges other than B98
- D30 Preferential loans to persons: Grant implied in lending. (Use with HMT approval only).
- F20 Write-offs of stocks
- L10 Provisions relating to pay, procurement etc and associated income: take-up and revaluations only
- L11 Provisions relating to pay, procurement etc and associated income: release of provision only
- L15 Provisions for pensions for staff where body has own unfunded pension scheme: take-up and revaluations only
- L16 Provisions for pensions for staff where body has own unfunded pension scheme: release of provision
- L20 Provisions relating to grants and associated receipts: take-up and revaluations only
- L21 Provisions relating to grants and associated receipts: release of provision only
- L30 Provisions relating to bad debts on loans: take-up and revaluations only
- L31 Provisions relating to bad debts on loans: release of provision only
- L40 Provisions for pension costs excluding interest on liabilities (pensions schemes under FRS17): take up and revaluation only
- L45 Provisions for pension costs - interest on scheme liabilities only (pensions schemes under FRS17): take up and revaluation only
- L46 Provisions for pension costs (pensions schemes under FRS17): release only
- X06 Profit and loss on disposal of land
- X11 Profit and loss on disposal of existing buildings
- X12 Profit and loss on sale of company securities
- X16 Profit and loss on sale of other tangible capital

APPENDIX 2 TO CHAPTER 5: SCORING OF CERTAIN TRANSACTIONS IN ACCOUNTS AND BUDGETS

341. The following table illustrates how the each of the main non-cash items in Resource DEL typically scores in budgets, accounts and cash.

	BUDGETING			ACCOUNTING		CASH
	RDEL ⁽¹⁾		CDEL	OCS ⁽¹⁾	Balance sheet	
	Near-cash	Non-cash				
PROVISIONS						
Create a provision		20		20	(20)	
Revalue the provision downwards		(5)		(5)	5	
Cash paid out against the provision ⁽²⁾	4	(4)			4	(4)
DEPRECIATION						
Buy an asset			10		10	(10)
Depreciate over its life		7		7	(7)	
Sell it for £2 – that is for less than its residual value		1	(3)	1	(3)	2
COST OF CAPITAL						
Buy an asset			29		29	(29)
Charge cost of capital each year @ 3.5%		1		1		

⁽¹⁾ Charges to the Operating Costs Statement (OCS) for these non-cash items normally equal the (net) charge to RDEL.

⁽²⁾ A faster than expected rate of payments against a set of provisions on the balance sheet has no net effect on Resource Budget DEL but means that non-cash requirements will be lower and near-cash requirements higher than planned. Note that if the eventual total bill is higher than the total amount of the relevant provision on the balance sheet, then the excess scores in the Resource Budget DEL as well as in near-cash because there is no provision to release against the cash payment.

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Chapter 5 – Near-Cash in Resource DEL

342. **Provisions.** The examples below copy the table in chapter 2 with the addition of a column to show non-cash and near-cash.

Example 1 – Standard Provision in Respect of DEL spending		
Year 1 – Take-up of provision	RB: DEL + £10	Non-cash
Year 2 – Revalue provision upwards	RB: DEL + £2	Non-cash
Year 3 – Release provision	RB: DEL - £12	Non-cash -£12
Make a payment	RB: DEL + £12 Net RB:DEL £0	Near-cash +£12
Example 2 – Split Treatment Provision		
Year 1 – Take-up of provision	RB: AME + £10	Non-cash
Year 2 – Revalue provision upwards	RB: AME + £2	Non-cash
Year 3 – Release provision	RB: AME - £12	Non-cash
Make a payment	RB: DEL + £12 Net RB:DEL + 12	Near-cash +£12

CHAPTER 6 - CAPITAL BUDGET – CENTRAL GOVERNMENT’S OWN EXPENDITURE

343. This chapter sets out guidance on specific issues relating to central government’s own expenditure in the Capital Budget.
344. NDPBs’ capital expenditure scores in budgets in the same way as departments’. See next chapter for the treatment of income in capital budgets. See separate chapters for the capital budget implications of loans to the private sector, PFI deals, support for local authorities and support for public corporations.

Capital Budgets overview

345. New capital spending by departments and NDPBs scores in the capital budget at the same value and with the same timing as in accounts. Some areas can give rise to tricky decisions on whether they are capital or not, and departments should check carefully the treatment of
- # in-house capital formation, including Research and Development expenditure and in house production of IT; and
 - # Software purchases.
346. Capital budgets are net of any income that is treated as negative expenditure in capital budgets – see separate section. Capital spending includes expenditure on tangible and intangible fixed assets, howsoever financed.
347. In addition capital budgets include net acquisitions of financial assets (e.g. movements in loans to the private sector) that score as movements in fixed assets on the balance sheet. In exceptional cases movements in debtors or other current assets (stocks / prepayments) may be included in the capital budget.
348. When budgeting for capital expenditure, departments should consistently follow agreed accounting policies when deciding what costs of a project should be capitalised (in most cases this should be uncontroversial but there are a few categories of expenditure, such as some consultancy costs, that could be either capital or resource).
349. Capital budgets include capital grants.

Departmental Investment Strategies

350. Departments’ agreed capital spending plans following SR04 were detailed in their Departmental Investment Strategies (DIS), published following the Spending Review. DIS include asset management plans, disposal plans and plans for all sorts of assets.
351. The DIS is a way of ensuring that the capital budget effects of spending and the consequential for the resource budget (eg depreciation) are considered together.

Predicting Capital Values

352. In line with the FreM, fixed assets are carried at current values rather than being based on historical costs. This policy normally requires land and buildings and other fixed assets to be valued professionally every five years and to use indices in the interim years.
353. Departments need to make assumptions about future expected disposals and acquisitions of fixed assets and movements in the value of fixed assets held, to be able to budget for the resource consequences (depreciation and cost of capital charge) of holding these items.
354. Whilst the departments latest audited balance sheet will provide the starting point for forecasting fixed asset balances, the Departmental Investment Strategy should set out any major investment or disposal programmes which are planned.
355. Past trends and movements in indices should provide evidence to support the revaluation of assets. The Treasury issues forecast indices that may be used by departments for estimating future capital values. These indices were issued under cover of PES papers (most recently in PES(2005)03).
356. As the assumptions used in forecasting fixed asset values will no doubt change over time, departments should regularly review their continued appropriateness and bring any significant changes to the early attention of their spending team.

Stocks treated as capital in budgets

When Stocks are treated as Capital in Budgets

357. DRAs do not treat purchases of stocks as investment in fixed assets. Rather, stock movements are treated as changes in current assets. Normally, budgets follow accounts in their treatment of stocks, and stocks are excluded from budgets until they are used, disposed of or written off.
358. The net acquisition of stocks is an item of capital spending in national accounts and increases TME. Therefore it would be appropriate to score all net acquisitions of stocks in capital budgets. However in the interest of keeping down compliance costs we normally ask departments to follow the treatment in DRAs.
359. Different budgeting rules are however appropriate where the item being acquired for stock would be the acquisition of a fixed asset if it were not being acquired for stock.
360. For example, land acquired by English Partnerships for reclamation and development scores as capital expenditure in capital budgets.
361. Where departments are aware of stock acquisitions that might fall into the category above, they should consult the Treasury on whether treatment in capital budgets would be appropriate.

How to Score Stocks Treated as Capital in Budgets

362. Where stocks score in Capital Budgets they score like fixed asset transactions. The costs of purchase and improvement of land treated as stocks score in the capital budget. Disposal scores at net book value as a benefit in the capital budget. Any write offs or profit / loss on disposal score in the resource budget.

Debtors and Pre-payments treated as capital in budgets

363. Normally, movements in debtors and pre-payments are treated as working capital and do not impact directly on budgets – see Chapter 2.

When Long-term Debtors and Pre-payments are treated as Capital in Budgets

364. Debtors and prepayments are assets, and typically arise where a department has delivered goods and services, but is yet to receive payment, or where the department has prepaid for goods or services, Changes in debtors generally represent a movement in working capital, that in general terms only impacts on the budgeting framework through the cost of capital charge or if written off.

365. However in certain cases movements in debtors are more akin to net lending, for example in complex contractual scenarios over an extended timeframe (that is, more than one year). In these cases the budgeting system scores movements in debtors in the capital budget of the department concerned. That scoring is intended to capture and control the impact of what is in effect lending on Public Sector Net Debt, the measure of the Sustainable Investment Rule.

366. Accordingly, departments should treat, as net lending, in their capital DEL the whole amount of transactions that meet both of the following criteria:

- # first, the transaction is either:
 - ~ a long-term debtor or pre-payment (that is a debtor that will last over 12 months at the point that the prepayment is made), *or*
 - ~ a short term debtor or prepayment where there is an expectation that it will be renewed so that it is in effect long term;
- # second the total value of the debtor / prepayment involved is above £20m (where there is a related group of pre-payments, the £20m limit applies to the group).

367. During 2006-07 only, departments may apply to their normal Treasury spending team for exceptional treatment if they can demonstrate that a pre-payment falling within the category above is not in the nature of lending.

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How to Score Debtors and Pre-payments Treated as Capital in Budgets

368. The scoring in such cases would be:
- # Capital budgets would score as net lending the full amount of such pre-payments;
 - # Any increase in the value of the prepayment as the discount unwinds scores as increased net lending (i.e. a cost)
 - # As the pre-payment is utilised, the capital budget would take a benefit (i.e. negative net lending).
369. In other words, the treatment would be on a net basis like the treatment of loan principal.
370. Note that the transaction financed by the prepayment would also score in budgets in the normal way. For example a payment of rental costs scores in the resource budget in the year the services are consumed, whether prepaid or not. In the case of capital budget transactions, the utilisation of the pre-payment would provide an element of budget cover.
371. Note that the OCS will show a cost of capital charge on the asset, and in addition if the prepayment is discounted a credit entry as that discount unwinds (the credit entry represents an interest payment from the holder of the prepaid cash). Both these transactions score in the resource budget.

Capital Grants to the Private Sector and Abroad

372. DRAs do not distinguish between current grants and subsidies and capital grants. However, the national accounts do, with current grants and subsidies affecting the current balance and capital grants not. Therefore departments have to distinguish between current and capital grants according to national accounts principles. Current grants and subsidies score in the Resource Budget; capital grants score in the Capital Budget.
373. Capital grants are unrequited transfer payments which the recipient has to use to:
- # buy capital assets (land, buildings, machinery &c); or
 - # buy stocks; or
 - # repay debt (but not to pay early repayment debt interest premia).
374. Where grants are paid that may be used at the recipient’s discretion either on capital or on current expenditure they should be treated as current grants or subsidies.
375. Capital grants are imputed in the national accounts (but not in budgets – which show loan write-offs) where debts are written off “by mutual consent”, that is, where the debtor could repay the loan or debt but for policy reasons the creditor department chooses not to enforce the debt.

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See the section on Bad Debt in the Chapter on Resource Budgets for more information

376. Payments of compensation to owners of capital goods destroyed or damaged by acts of war or natural disasters count as capital grants.
377. Major payments in compensation for extensive damage or serious injuries not covered by insurance policies may also count as capital grants – departments should consult the Treasury.
378. Pensions bulk transfer payments are treated as capital transactions in the national accounts and pass through resource budgets (albeit offset by the release of the provision) – see chapter on pensions.

Provisions in Respect of Capital Grants

379. Where departments take provisions in respect of an obligation to pay a capital grant, the take-up, revaluation and release of the provision should score in the Capital Budget, as well as the grant itself. If so, then normally the payment of the grant itself should be offset by the release of the provision.

Cost of Capital Credit on Provisions in Respect of Capital Grants

380. Provisions attract a cost of capital credit. That credit in a sense offsets the increase in value of the provision as the discount unwinds year by year. Departments should therefore include the cost of capital credit in their capital budgets.
381. Where a department believes that separating out these cost of capital credits is more trouble than it is worth, the department may include the cost of capital credit in its resource budget along with other cost of capital charges and credits. Departments should make the same choice for all cost of capital credits on capital grants. Having made a choice, departments should not alter it without the agreement of the Treasury.
382. Note that where a liability corresponding to a capital grant is classified as a creditor the corresponding cost of capital credit should score in the resource budget in the normal way, as there is no unwinding of the discount to take into consideration.

Capitalised Provisions

383. Provisions are liabilities of uncertain timing or amount that, as a result of a past event, will more likely than not require the transfer of economic benefits from one party to another. In most cases incurring a liability will lead to a cost in the I&E or OCS of the party recognising the liability.
384. However in some - highly unusual - cases, the recognition of that liability is also the trigger point to recognise access to future economic benefits for the holder of the liability. In those cases it may be appropriate not to show a cost in the I&E / OCS. Instead the accounts would show an increase in fixed assets as well as the liability.

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385. If a department believes that it should be capitalising their provisions in this way they should seek clarification from their usual Treasury Central Accountancy Team contact in the first instance.
386. In cases where HMT’s CA team have agreed that capitalising the provision is the correct treatment in the DRA the capital budget will score the recognition of the liability.
387. When the actual cash payment is transacted this will score in capital DEL too but it will be offset by the release of the provision so there is no further overall net impact on the capital budget.

Resource budget implications

388. The Resource Budget scores the items that score in the OCS in DRAs:
- # Depreciation on the asset,
 - # cost of capital charge on the asset,
 - # cost of capital credit on the liability, and
 - # the unwinding of the discount.

Creditors in respect of capital assets

389. No special treatment applies where a department has a creditor in respect of the acquisition of a capital asset. In other words the capital expenditure scores in the capital budget at the same time as the asset is recognised in the accounts and any cost of capital charges / credits fall on the resource budget as normal. The cash transaction is then a movement in cash and creditors in accounts and outside the budgeting framework.

MoD - single use fighting equipment and dual purpose equipment

390. National Accounts differentiates between single and dual use military equipment. Spending on single use military equipment is classified as current expenditure. Single use military assets are those that could not be used by civilian organisations for the production of goods and services (i.e. weapons and equipment that supports and delivers such weapons).
391. Expenditure on dual use military equipment is treated as capital in National Accounts. Dual assets are those that could be used by civilian organisations for the production of goods and services such as airfields, docks, roads and hospitals. Expenditure on almost all fixed structures will be treated as capital expenditure in the national accounts as is that on types of equipment which have alternative non-military uses - such as transport equipment, computers and communication equipment and hospital equipment.
392. This distinction is not however maintained in the capital budget, and all spending by MOD on both single and dual use asset that leads to an increase in their fixed assets scores in the capital budget in the normal manner. However in order to ensure that the national accounts record

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spending correctly, and HMT can budget effectively this distinction must be maintained, and recorded separately.

CHAPTER 7 – INCOME AND THE CAPITAL BUDGET

393. This chapter covers the treatment of Capital income in budgets. The same rules apply to NDPBs as to Departments. A separate chapter deals with income and the resource budget. The chapter on loans covers departments' income in respect of loans.
394. The chapter sets out which income benefits the Capital Budget, comments on the timing of income and explains when departments may retain income above the level set in the SR.

Income that may normally be set against Budgets

395. The following items of capital income may normally be set against capital budgets within the terms set out below. Only income in connexion with DEL programmes scores in capital budget: DEL
- # Income from capital asset sales – the book value scores as income in the capital budget.
 - # Income from sale of stocks that score in the capital budget (see section on stocks in CDEL in chapter 6)
 - # Capital grants from the private sector including developer contributions and capital donations
 - # Income obtained from National Lottery distributing bodies that finances capital expenditure
 - # Capital Grants from the EC
 - # Capital Royalties
 - # Privatisation proceeds (always in AME not DEL)

Further Information on Certain Types of Income

Disposal of Capital Assets

396. When a department or NDPB disposes of an asset, the net book value of this asset scores as negative capital DEL. Any profit or loss on disposal, i.e. the difference between net book value and actual sale value scores in the Resource Budget.

Income from National Lottery Distributing Bodies

397. The Government's income from the National Lottery is a tax. The spending by the National Lottery distributing bodies counts as expenditure in AME.
398. Where a Government department or NDPB that is not a National Lottery distributing body obtains income from a distributing body to finance spending in the Capital Budget DEL it should take the income into budgets as negative Capital Budget DEL

Capital Grants from the EC

399. Income from the EC may be netted off Capital Budget DEL if it is in support of DEL spending and if it supports capital expenditure.

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400. It is government policy that departments should fully take up the UK's structural funds allocation, and that EC money should be used where it supports programmes that are value for money.
401. Because EC income in practice costs the Exchequer about £0.71 in the £1 it is particularly important that departments ensure that they claim discretionary EC income only in support of programmes that are good value for money.

Royalties - Capital or Current?

402. It may be difficult to tell whether a one-off payment covering a number of years is for the sale of an asset or an upfront payment in respect of a number of years' royalty. Similarly, it may be hard to test whether a payment spread over a number of years is for the sale of an asset or a current royalty.
403. The tests used by commercial or GAAP accountants applying Financial Reporting Standard 5 - *Reporting the Substance of a Transaction*, will be a guide as to whether a capital asset has been sold or rented out. For larger cases, departments should consult the Treasury to ensure that they are treating the income in accordance with the national accounts.
404. In general:
- # a sale leading to a current receipt - royalty for the use of an asset - would be a sale offering the user a right to use the asset for a period of time, but underlying ownership of the asset or resource would stay with the vendor. Changes in the value of the asset would not normally affect the user as they would not be able to sell on their rights; but
 - # capital income - sale of an asset - would be when the buyer had obtained:
 - ~ all significant rights or other access to benefits relating to that asset; and
 - ~ all significant exposure to the risks inherent in those benefits.
405. Ownership rights would typically include unimpeded use of the asset, right to resell the asset and benefit or suffer from changes in the value of the asset. Typically, capital income comes as a single receipt at the time of sale, but the cash receipt may come in tranches (deferred consideration). Where the asset has been sold outright, the income is capital and the whole of the income is to be treated as negative public expenditure.

Privatisation Proceeds

406. Privatisation proceeds score in AME, even where the asset or business being sold was on a DEL programme.

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Proceeds from Disposal of Shares in Public Private Partnerships (PPPs)

407. Sale of shares in a **private sector PPP** is the disposal of a financial asset by the department. As a form of privatisation, the income scores as a benefit to the Capital Budget: AME.
408. Sale of shares in a **public sector PPP** is a form of public sector borrowing from the market, whether it is undertaken by the PPP or by the department. So any cash received by the borrower is not a benefit to budgets. (Market borrowing by a public corporation is a cost in budgets; departmental spending financed by borrowing is a cost in budgets.)

Timing of Recording of Income

409. In general, departments should record capital income for budgets at the same time as they record it for accounts.
410. Income from capital transfers (ie grants, developer contributions and donations received) other than income from the EC should be recorded for budgeting purposes at the time that the income falls due, that is, when the cash is due to be paid. That may be different from the recording in DRAs if exceptionally the accrual of the income has been related to work done at a quite different time.
411. Capital transfers from the EC should be recorded for budgets in line with DRAs. Departments are encouraged, where appropriate, to accrue income from the EC to match the payments that the income finances. The reason for the different treatment is that where income from the EC finances a payment to a third party it is treated for the national accounts as a direct payment from the EC to the third party recipient. By accruing the income to the date of the payment it is easier to derive the national accounts number.

When departments may retain additional negative DEL income

412. In some cases capital income does no more than cover the costs of replacing the asset disposed of. For example, a department might sell one office block and spend the money on moving into another that suits it better.
413. In other cases, income can be large in comparison with the needs for replacement, or there may be no replacement. Example are selling an invention in the open market, or when a department moves from an expensive building into a cheaper one. In these cases the Government has to balance two considerations:
- # Departments should be encouraged to obtain such income by being allowed to retain and spend it; and
 - # Government funds should be prioritised across the whole range of spending to where they would do most good.

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414. And we need to keep the rules simple.
415. Departmental budgets are set in the SR net of negative CDEL income. The SR settlement should be informed by the expected level of negative CDEL income. So, the SR process should be used to identify the expected level of Department's income, any expected changes, and an assessment of the potential for new income. The SR settlement will include an explicit statement of the expected level of income in the years of the SR period. And Departments should reflect that level of income in their Departmental Investment Strategies.
416. Departments should therefore ensure that their SR proposals and Departmental Investment Strategies set out their asset management and disposal strategy. That strategy should reflect a number of strands, including:
- # The **Lyons review** into the better management of public sector assets recommended that departments and their sponsored bodies, as part of their wider business and improved asset management strategies, should seek to dispose of capital assets that are no longer required as a contribution to the Government's objective of securing £30 billion of asset disposal by 2010;
 - # Departments should set out how they might alter their mix of capital assets, to retain high levels of efficiency;
 - # Departments should not hold on to assets unnecessarily – the cost of capital charge is an incentive to dispose of unneeded assets; and
 - # The Treasury encourages Departments to engage in **Wider Market** activities. Not only does the income they generate support public spending, but also undertaking pioneering or inventive activity can enhance the skill set of civil servants, and can lead to more innovative provision of public services. The SR provides an opportunity for challenging departments' expected level of such activities and encouraging departments to exploit spare capacity. At this stage in the evolution of the Wider Markets initiative, the Treasury believes that it creates a helpful incentive for Departments to be allowed to keep wider markets income classified as negative DEL, and will set Departmental Expenditure Limits in this spirit.
417. Departments will be allowed to keep the negative DEL income that they obtain in the SR period up to the amount that was taken into account in the SR. Income cannot be predicted wholly accurately, and the Treasury wishes to encourage departments to find new income streams where appropriate. Departments may therefore in any year retain negative CDEL income up to 20% above the level envisaged for that year as part of the SR settlement and set out in their DIS without an adjustment to budgets.
418. If departments expect to obtain more income than provided for above, they should talk to the Treasury about whether they may retain all or

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part of the income without an adjustment to budgets. When considering proposals, the Treasury will wish in particular to encourage Wider Markets activities and Lyons asset disposals where opportunities could not be foreseen at the time of the SR and other cases where the additional income represents the results of positive management action, as opposed to under-forecasting.

CHAPTER 8 – LOANS TO THE PRIVATE SECTOR

419. This chapter applies to loans to the private sector and overseas bodies. For loans to public corporations see the PCs chapter.
420. Loans are payments made to another party where the expectation is that the payment will be wholly repaid, normally with interest, and normally to a fixed regular payment schedule.
421. Loans need to be distinguished from deposits:
- # Policy lending is where the department lends money as an act of policy. So, for example, we lend to students or to certain sorts of business because we wish to support them in this way; and
 - # Deposits are also a form of lending, but are made because the public body has spare cash and needs to put it somewhere. Typically deposits are placed with a bank in order to obtain the maximum risk-weighted rate of interest. There is no intention to support the institution holding the deposit.
422. This chapter is concerned with policy lending only. The making and withdrawing of deposits do not score in budgets, though deposits themselves may attract a cost of capital charge.

Loans other than Student Loans

423. The budget treatment is:
- # the Resource Budget will score:
 - ~ an appropriate cost of capital charge (which may differ substantially from the standard 3.5% depending on the circumstances),
 - ~ less interest income,
 - ~ new provisions for bad debts and increases or decreases in the value of provisions, and
 - ~ bad debts less the release of provisions (these two transactions may offset each other);
 - # the Capital Budget will score:
 - ~ net lending (i.e. transactions in loan principal).
424. Normally, lending scores in DEL. Where exceptionally a loan scheme is in AME (e.g. Social Fund), generally the associated resource transactions will score in Resource AME.
425. For loans made to the private sector or for equity invested in the private sector a higher cost of capital will normally be appropriate than the cost of capital used for the department's standard assets. Departments are asked to agree a suitable cost of capital charge with their spending team in HMT for each scheme of loans or equity investments.

Student Loans – Main provision

426. Student loans score in the following way, that follows entirely the accounting.
427. Resource Budget DEL:
- # The following items score as expenditure:
 - ~ set-up and revaluation of provision in respect of the implied subsidy the student receives on the loan (i.e. the difference between the discount rate and interest receivable)
 - ~ unwinding of the discount on provisions
 - ~ inflation adjustment
 - ~ cost of capital charge on the asset
 - # The following items score as income
 - ~ interest income receivable
 - ~ amount credited to the OCS from the provision for the subsidy
428. The accounts should be recorded so as to ensure that there is only a cost in year 1, with interest receivable and the amount credited to the OCS from the balance sheet covering the unwinding of the discount, cost of capital charge and the inflation adjustment in subsequent years.

Student Loans - provision for bad debts

429. In addition to the main provision the accounts and budgets should recognise a separate provision for bad debt, recorded as described in the section on provisions in this guidance. Moreover any bad debts that are realised are deemed to be policy write offs, and as such are treated as debt write offs by mutual consent. So they should be recorded in a way that allows them to be identified as capital transfers to the private sector (see COINS recording guidance).

CHAPTER 9 – NON-DEPARTMENTAL PUBLIC BODIES

Coverage of this chapter

430. This chapter applies to the budgeting of all bodies in the central government sector (as defined by the Office for National Statistics) other than Government departments (including executive agencies), and NHS producer trusts (England) and bodies referred to in the following two paragraphs. It applies whether or not the Cabinet Office has designated a body as a Non Departmental Public Body (NDPB - see the NDPB section in Chapter 1). So in this chapter we are using "NDPB" as convenient shorthand, rather than in the strict Cabinet Office sense of the word, although the majority of bodies to which the chapter applies will be true NDPBs.
431. Some smaller NDPBs, typically **advisory bodies**, are treated as part of the department for expenditure control and are within the resource accounting boundary. They would naturally fall to be budgeted for like the department itself and so there is no need for the guidance in this chapter to apply. Similarly, the **Crown NDPBs** that are on vote for their income and expenditure will also fall naturally to be budgeted for like departments, and so there is no need for this chapter to apply.
432. This chapter does not apply to **public corporations**. Most **trading funds** are public corporations, but some may be central government bodies. This chapter applies to any trading fund that is a central government body.

Overview

433. NDPBs' resource consumption and capital expenditure score in the departments' resource and capital DEL in the same way as the department's own spending. So departments should normally use the output from the NDPB's own accruals accounts as the basis for working out the NDPB's impact on budgets. That should help to ensure that non-cash items in particular are recorded.
434. Budgets include expenditure that NDPBs finance themselves from income that is not negative DEL, use of reserves or borrowing (where, exceptionally, permitted).
435. The grant in aid paid by the department and any other financing facilities made available by the department are outside the department's budget.

Planning and Monitoring

436. Departments are expected to set their NDPBs firm Resource and Capital DEL budgets for the year ahead. Departments are generally advised to set firm or indicative budgets for forward years to help NDPBs plan.
437. Departments should monitor in-year both:
- # the NDPB's draw-down of cash grant in aid; and

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the NDPB's expenditure in budgets.

NDPB Income and Receipts

438. The NDPB's impact on the department's Resource Budget DEL is made up of its gross resource consumption /less its negative DEL income. Similarly, the Capital Budget DEL is net only of negative DEL income. Whether NDPB income / receipts are negative DEL follows the same rules as for departmental receipts (see separate chapters). So, for example, charges for the sales of goods and services are typically negative DEL and the receipt of taxes are typically not. Expenditure financed in cash terms by non-budget income scores gross in budgets.
439. Where a NDPB obtains income that is not negative DEL, the department may arrange for the NDPB to pass the cash to the department for surrender to the consolidated fund. Alternatively, the cash may be retained by the NDPB and offset the NDPB's need for cash grant in aid. Either way, income that is not negative DEL does not convey spending authority.

Borrowing

440. Normally, NDPBs are not allowed to borrow. Where exceptionally they are allowed to borrow the spending financed by borrowing scores gross in budgets. This applies whatever the source of borrowing (department, market, European Investment Bank). The cash raised by borrowing does not score as negative DEL.

Corporation Tax

441. Exceptionally, some NDPBs pay Corporation Tax. Such payments are non-budget, because payments within central government of taxes on income are consolidated out. NDPBs should not devote resources to tax minimisation or tax planning.

Co-Funded NDPBs

442. Where an NDPB receives grant-in-aid from more than one department then the budgeting treatment should follow one of three models. The treatment should be agreed with the relevant Treasury spending team. The models are represented diagrammatically in the Appendix to this chapter.
443. The three models are:
444. **Model A: Vote to Vote.** Department A makes a voted cash payment to Department B. It is for the departments concerned to decide whether Department A's payment should cover a share of depreciation and cost of capital charges. Department B is the sponsor of the NDPB and pays it a single grant-in-aid, including an element in respect of the payment made by Department A. Department B takes responsibility for the budgetary impact of the NDPB's expenditure. The NDPB's expenditure should score in department B's Budgets (resource / capital and DEL/AME as appropriate). Department B's grant-in-aid to the NDPB scores outside the budget in the normal way. Department A's payment

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to department B scores in department A's DEL as a cost, and in department B's DEL as a benefit – thereby sharing the budgetary impact.

445. In the numerical examples:

- # Department A contributes £100. There are no non-cash costs associated with these activities; and
- # The NDPB's total spending in DEL from all sources is £950 and it needs cash of £850.

Department A's budget	Department B's Budget		Department B's grant in aid to the NDPB
	Departmental element	NDPB element	
£100	-£100	£950	£850

446. **Model B: Direct funding of the NDPB.** Department B is the sponsor of the NDPB. Department A may fund the NDPB direct (i.e. without going through Department B's Estimate). It is for the departments concerned to decide whether Department A's cash payment should cover a share of depreciation and cost of capital charges. If Department A's payment provides more cash than the NDPB needs, Department B can adjust the cash that it provides accordingly. The whole of the NDPB's resource consumption (net of any negative DEL income) should score in the sponsor department B's Resource budget, and capital expenditure in the Capital Budget. As in Model A, Department B's grant-in-aid does not score in its budget, but Department A scores its payment to the NDPB in its budget. Exceptionally, when the NDPB receives the payment from Department A, it should be treated as negative DEL.

Department A's budget	Department B's Budget		Department B's grant in aid to the NDPB
	Departmental element	NDPB element	
£100	-	£950 - £100 = £850	£750

447. **Model C: Virtual NDPBs.** Departments could agree that where funding from each department is clearly attributable to a specific programme of work, for budgeting purposes the NDPB should be divided into two virtual NDPBs, one answerable to Department A and the other to Department B. Each department funds its share of the NDPB, including non-cash items such as capital charges: here, each department shows the costs of a virtual NDPB, being its share of the NDPB's activities. Each department would include in its resource budget the NDPB's resource consumption in respect of the activities it carries out for that department, and would include the depreciation and

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cost of capital charge for the assets used for the department's policies. Each department therefore also scores its grant-in-aid outside its budget.

Department A's budget (NDPB element)	Department A's grant in aid to the NDPB	Department B's Budget (NDPB element)	Department B's grant in aid to the NDPB
£100	£100	£850	£750

448. How to choose between the models:

- # **Models A and B** both have the same budgeting impact (the minor department's payment to the NDPB scores in that department's budget and benefits the sponsoring department's overall budget) but the Estimates mechanics are different:
 - ~ **Model A** should generally be favoured as it is the most transparent way of sharing the appropriate budgetary costs between departments and least likely to go wrong when ensuring that all the NDPB's expenditure is budgeted for in one department. Where a department favours models b or c they should discuss this with their spending team.
 - ~ **Model B** is only appropriate where department A's contribution is minimal as there is the risk of confusion with the exceptional negative DEL treatment of a payment from a department to an NDPB.
- # **Model C** will be difficult to realise if the NDPB does not clearly delineate which functions are pursued for which department. If departments follow Model C, the various departments need jointly to establish a mechanism to ensure that the whole of the NDPB's resource consumption appears in the resource budgets of the various departments when added together. The NDPB should be asked to produce a budget reconciliation, showing its total effect on DEL and how this is apportioned amongst the various departments.

Certain Levy-Funded Bodies

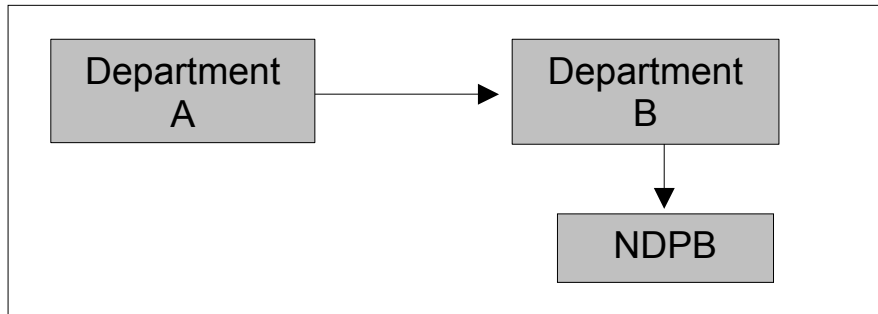
449. The spending of a number of levy-funded bodies, defined against the criteria in Appendix 4 to Chapter 1, is in AME, rather than DEL.

Certain MoD NDPBs

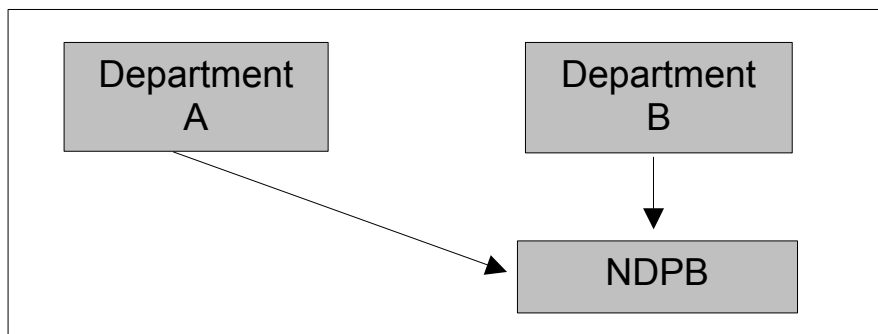
450. Certain small MoD NDPBs score in budgets on the basis of the grant in aid paid to them under a temporary derogation from normal budgeting rules. This treatment is kept under review.

**APPENDIX 1 TO CHAPTER 9:
DIAGRAMS REPRESENTING THE MODELS FOR CO-
FUNDED NDPBs**

Model A



Model B



Model C

