

The interim projections for the public finances published in this Pre-Budget Report show that the Government is meeting its strict fiscal rules over the economic cycle:

- the current budget since the start of the current economic cycle in 1997-98 shows an annual average surplus up to 2006-07 of 0.1 per cent of GDP, showing the Government is meeting the golden rule on the basis of cautious assumptions; and
- public sector net debt is projected to be low and stable over the forecast period stabilising below 39 per cent of GDP, below the 40 per cent ceiling set in the sustainable investment rule.

The 2006 *End of year fiscal report* is published alongside this Pre-Budget Report, underlining the Government's commitment to transparency in fiscal policy by providing detailed information on the public finances in 2004-05 and 2005-06.

## INTRODUCTION

**B.1** Chapter 2 describes the Government's fiscal policy framework and shows how the projections of the public finances presented in the Pre-Budget Report are consistent with meeting the fiscal rules. This chapter explains the latest outturns and the fiscal projections in more detail. It includes:

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

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

**B.3** The Pre-Budget Report updates the projections of the public finances contained in Budget 2006 to take account of subsequent developments in both the public finances and the world and UK economies. The projections represent an interim forecast update and are not necessarily the outcome the Government is seeking.

**B.4** As described in Chapter 2, an *End of year fiscal report* is published alongside this Pre-Budget Report. The report underlines the Government's commitment to transparency in fiscal policy by providing detailed retrospective information on the state of the public finances in 2004-05 and 2005-06, including their performance against the fiscal rules and against published forecasts and plans. The information set out in the *End of year fiscal report* supplements the historical and provisional outturn data published in this annex.

## MEETING THE FISCAL RULES

**B.5** Table B1 shows five-year projections for the current budget and public sector net debt, the key aggregates for assessing performance against the golden rule and the sustainable investment rule respectively. Outturns and projections of other important measures of the public finances, including net borrowing and cyclically-adjusted fiscal balances, are also shown.

**B.6** As explained in Chapter 2, the Government's judgement is that the current economic cycle started in 1997-98. Based on the assumptions used in these projections the economy will return to its trend level, ending the current cycle, in early 2007.

**Table B1: Summary of public sector finances**

	Per cent of GDP							
	Outturn		Estimate	Projections				
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
<b>Fairness and prudence</b>								
Surplus on current budget	-1.6	-1.2	-0.6	-0.1	0.3	0.5	0.6	0.8
Average surplus since 1997-1998	0.3	0.1	0.1	0.0	0.1	0.1	0.1	0.2
Cyclically-adjusted surplus on current budget	-1.6	-1.0	-0.4	-0.1	0.3	0.5	0.6	0.8
<b>Long-term sustainability</b>								
Public sector net debt <sup>1</sup>	35.0	36.4	37.5	38.2	38.6	38.7	38.7	38.5
Core debt <sup>1</sup>	34.6	35.8	36.7	37.4	37.8	38.0	38.0	37.8
Net worth <sup>2</sup>	28.8	27.0	25.7	24.9	24.9	24.6	24.6	24.6
Primary balance	-1.7	-1.4	-1.1	-0.6	-0.2	0.0	0.1	0.3
<b>Economic impact</b>								
Net investment	1.7	1.8	2.2	2.2	2.2	2.2	2.2	2.2
Public sector net borrowing (PSNB)	3.3	3.0	2.8	2.3	1.9	1.7	1.5	1.3
Cyclically-adjusted PSNB	3.2	2.8	2.6	2.2	1.9	1.7	1.5	1.3
<b>Financing</b>								
Central government net cash requirement	3.2	3.2	3.2	2.5	2.1	2.1	1.8	1.9
Public sector net cash requirement	3.2	3.2	2.9	2.4	2.0	2.0	1.6	1.7
<b>European commitments</b>								
Treaty deficit <sup>3</sup>	3.2	2.8	2.7	2.2	1.9	1.7	1.5	1.3
Cyclically-adjusted Treaty deficit <sup>3</sup>	3.1	2.6	2.5	2.2	1.9	1.7	1.5	1.3
Treaty debt ratio <sup>4</sup>	40.5	42.7	43.7	44.1	44.2	44.2	44.0	43.6
Memo: Output gap	0.0	-0.4	-0.2	0.0	0.0	0.0	0.0	0.0

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

<sup>2</sup> Estimate at end December; GDP centred on end December.

<sup>3</sup> General government net borrowing on a Maastricht basis.

<sup>4</sup> General government gross debt measures on a Maastricht basis.

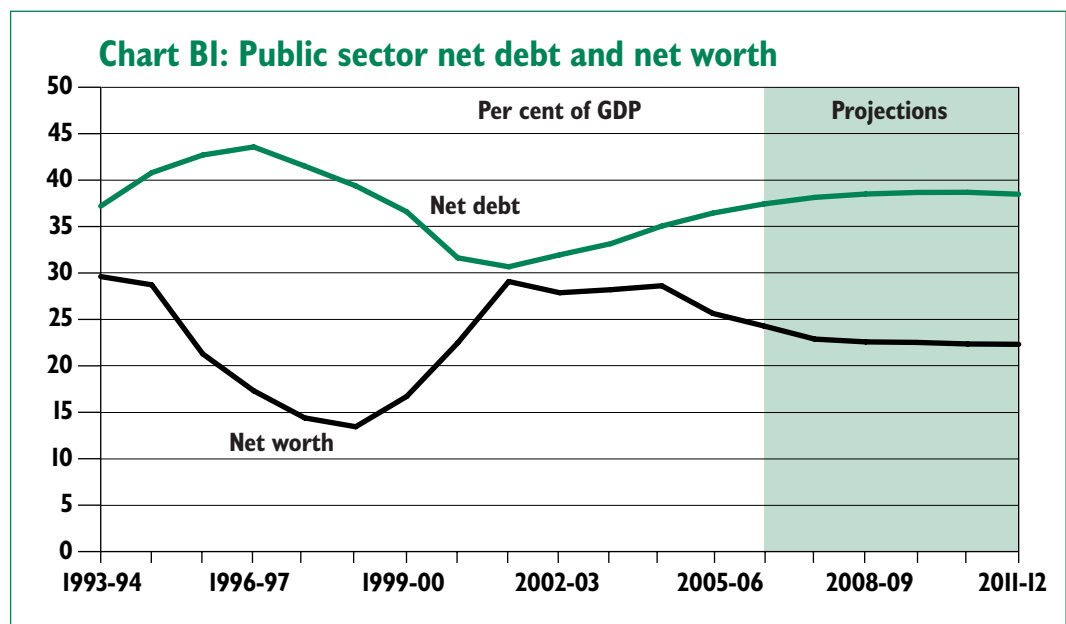
**The golden rule** **B.7** The Government's judgement is that the current cycle started in 1997-98. Based on assumptions used in these projections the economy will return to its trend level, ending the current cycle in early 2007. The projections show that the Government is meeting the golden rule, on the basis of cautious assumptions, with an average annual surplus on the current budget over this economic cycle of 0.1 per cent of GDP. On this basis, and based on cautious assumptions, the Government is meeting the golden rule and there is a margin against the golden rule of £8 billion in this cycle.

**B.8** Based on cautious assumptions, the Government will continue to meet the golden rule after the end of this economic cycle with the current budget returning to surplus by 2008-09.

**The sustainable investment rule B.9** The sustainable investment rule is also forecast to be met over the current economic cycle. In 1996-97, public sector net debt stood at 44 per cent of GDP. The tough decisions on taxation and expenditure taken by the Government, including the decision to use the proceeds from the auction of spectrum licenses to repay debt, reduced net debt to just over 30 per cent of GDP by the end of 2001-02. It is now projected to grow slowly, as the Government borrows modestly to fund increased investment in public services, reaching 37.5 per cent of GDP by the end of the current economic cycle, £33 billion below the 40 per cent level. It remains below 39 per cent for the remainder of the forecasting period, and falls to about 38½ per cent in 2011-12. The projections for core debt, which exclude the estimated impact of the economic cycle, rise to a maximum of 38.0 per cent of GDP. This is consistent with the fiscal rules, and with the key objective of intergenerational fairness that underpins the fiscal framework.

**Net worth B.10** Net worth is the approximate stock counterpart of the current budget. Modest falls in net worth are expected for the remainder of the projection period from the high level of 28.8 per cent of GDP in 2004-05. At present, net worth is not used as a key indicator of the public finances, mainly as a result of the difficulties involved in accurately measuring many government assets and liabilities.

**B.11** Chart B1 shows public sector net debt and net worth as a per cent of GDP from 1993-94 to 2011-12.



**Net investment B.12** As a result of decisions taken in the 2004 Spending Review, public sector net investment is projected to rise from 1¼ per cent of GDP in 2003-04 to 2¼ per cent from 2006-07 onwards. This increase is sustainable and fully consistent with the Government’s long-term approach and the fiscal rules, since net debt is being held at a stable and prudent level, below 40 per cent of GDP.

**Net borrowing B.13** Public sector net borrowing is expected to fall in every year of the forecast period from 3.0 per cent of GDP in 2005-06 to 2.8 per cent in 2006-07, and then to a level of 1.3 per cent of GDP by 2011-12.

**Financing B.14** The central government net cash requirement was 3.2 per cent of GDP in 2005-06. It is projected to stay at this level in 2006-07, and to then fall to 1.9 per cent of GDP by 2011-12.

**European commitments B.15** Table B1 shows the Treaty measures of debt and deficit used for the purposes of the Excessive Deficit Procedure – Article 104 of the Treaty. The Pre-Budget Report projections meet the EU Treaty reference value for general government gross debt (60 per cent of GDP) by a considerable margin. The Treaty deficit on a cyclically-unadjusted basis fell to 2.8 per cent in 2005-06 and is forecast to fall further over the projection period. In addition, the cyclically adjusted level of general government net borrowing is 2.5 per cent of GDP in 2006-07 and is 2.2 per cent of GDP or below from 2007-08 onwards. The projections are therefore consistent with the Government's prudent interpretation of the Stability and Growth Pact.

## CHANGES TO THE FISCAL BALANCES

**B.16** Table B2 compares the latest estimates for the main fiscal balances with those in Budget 2006.

**Table B2: Fiscal balances compared with Budget 2006**

	Outturn <sup>1</sup>	Estimate <sup>2</sup>	Projections			
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
<b>Surplus on current budget (£ billion)</b>						
Budget 2006	-11.4	-7.1	1	7	10	12
Effect of revisions and forecasting changes	-3.7	-1.0	-5	-5 1/2	-5	-4
Effect of discretionary changes	0.0	0.2	2	2 1/2	2	2
<b>PBR 2006</b>	<b>-15.1</b>	<b>-7.9</b>	<b>-1</b>	<b>4</b>	<b>7</b>	<b>10</b>
<b>Net borrowing (£ billion)</b>						
Budget 2006	37.1	35.8	30	25	24	23
Changes to current budget	3.7	0.8	3	3	3	1 1/2
Changes to net investment	-3.3	0.1	-1	-1 1/2	-1	-1
<b>PBR 2006</b>	<b>37.5</b>	<b>36.8</b>	<b>31</b>	<b>27</b>	<b>26</b>	<b>24</b>
<b>Cyclically-adjusted surplus on current budget (per cent of GDP)</b>						
Budget 2006	-0.3	0.4	0.7	0.7	0.7	0.8
<b>PBR 2006</b>	<b>-1.0</b>	<b>-0.4</b>	<b>-0.1</b>	<b>0.3</b>	<b>0.5</b>	<b>0.6</b>
<b>Cyclically-adjusted net borrowing (per cent of GDP)</b>						
Budget 2006	2.4	1.9	1.6	1.6	1.6	1.5
<b>PBR 2006</b>	<b>2.8</b>	<b>2.6</b>	<b>2.2</b>	<b>1.9</b>	<b>1.7</b>	<b>1.5</b>
<b>Net debt (per cent of GDP)</b>						
Budget 2006	36.4	37.5	38.1	38.3	38.4	38.4
<b>PBR 2006</b>	<b>36.4</b>	<b>37.5</b>	<b>38.2</b>	<b>38.6</b>	<b>38.7</b>	<b>38.7</b>

<sup>1</sup> The 2005-06 figures were estimates in Budget 2006

<sup>2</sup> The 2006-07 figures were projections in Budget 2006.

**B.17** The revisions to the public sector current budget in this Pre-Budget Report are due to a combination of expenditure and receipts effects. Expenditure is higher in 2005-06 and in all subsequent years. Receipts are lower in 2005-06, higher in 2006-07 and, mainly due to lower projections of North Sea revenues, lower from 2007-08 onwards.

**B.18** Overall, the current budget has been revised from a deficit of £11.4 billion to a deficit of £15.1 billion in 2005-06 and from a deficit of £7.1 billion to a deficit of £7.9 billion in 2006-07. In 2007-08 the deficit is £1 billion compared to a surplus of £1 billion in the Budget 2006 projections. The current balance is projected to return to surplus in 2008-09.

**B.19** Public sector net investment has been revised down by £3.3 billion in 2005-06, is unchanged in 2006-07, and is slightly lower in subsequent years. These reductions in projected net investment partially offset the reductions in the current budget, but overall net borrowing has been revised up.

## FORECAST DIFFERENCES AND RISKS

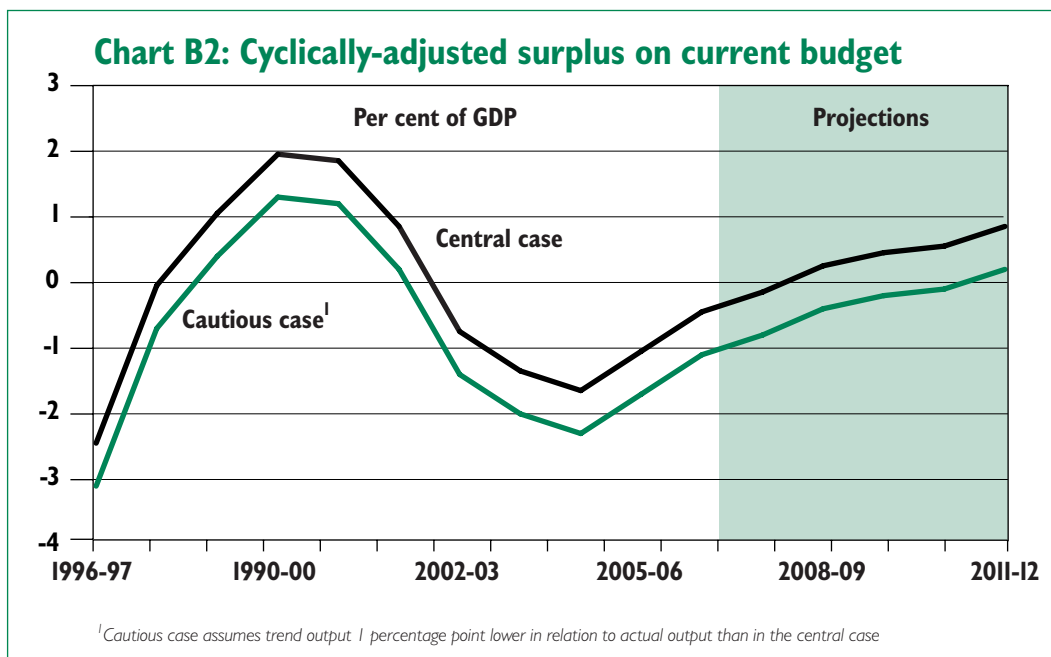
**B.20** The fiscal balances represent the difference between two large aggregates of expenditure and receipts, and forecasts are inevitably subject to wide margins of uncertainty. Over the past ten years, the average absolute difference between year-ahead forecasts of net borrowing and subsequent outturns has been about 1 per cent of GDP. This difference tends to grow as the forecast horizon lengthens. A full account of differences between the projections made in Budget 2004 and Budget 2005, and the subsequent outturns is provided in the *End of year fiscal report*, published alongside the 2006 Pre-Budget Report.

**B.21** As explained in Annex A, growth is forecast to continue at close-to-trend rates throughout the forecast horizon. UK GDP is expected to rise by  $2\frac{3}{4}$  per cent in 2006 as a whole, above the Budget 2006 forecast range. Growth in 2007 is forecast to be above trend at  $2\frac{3}{4}$  to  $3\frac{1}{4}$  per cent. The rebalancing of growth that has taken place since 2005 is expected to continue with private consumption growing at rates slightly slower, and business investment slightly faster, than the economy overall.

**B.22** Risks to the 2006 Pre-Budget Report economic outlook are broadly balanced. There are potential downside risks to the private consumption forecast, but significant upside risks to business investment growth. Surveys of consumers' saving intentions suggest that the pick-up in the household saving ratio over the past year could continue and exceed the 2006 Pre-Budget Report forecast. Offsetting that, developments in the housing market have been somewhat stronger than expected and could be associated with higher consumption growth. Despite business investment growth having been revised up in the Pre-Budget Report forecast, there are still significant upside risks. In particular, corporate profitability remains strong and financing conditions remain benign. Both factors could support stronger growth in business investment.

**B.23** The use of cautious assumptions audited by the National Audit Office (NAO) builds a margin into the public finance projections to guard against unexpected events. One of the key audited assumptions is that for the trend rate of output growth, which is assumed to be  $\frac{1}{4}$  per cent below the neutral view. This means that the rate of economic growth used to forecast the public finances is the bottom end of the projection range. For example, in this Pre-Budget Report, the forecast for economic growth used in the public finance projections over the period 2006-07 to 2011-12 averages  $2\frac{1}{2}$  per cent,  $\frac{1}{4}$  per cent below the central case. By 2011-12 the level of GDP used in the public finances forecast is about  $1\frac{1}{4}$  per cent below the central view.

**B.24** A further important source of potential error results from misjudging the position of the economy in relation to trend output. To minimise this risk, the robustness of the projections is tested against an alternative scenario in which the level of trend output is assumed to be one percentage point lower than in the central case. Chart B2 illustrates the Pre-Budget Report projection for this cautious case.



**B.25** The Government has used the cautious case and cautious NAO audited assumptions to build a safety margin in the public finances against unexpected events. This was combined with the decision to consolidate the public finances when the economy was above trend, which has resulted in the current low debt level. This has allowed the Government to safeguard the increase in investment in priority public services, allow the automatic stabilisers to work fully during a period of global economic uncertainty, and meet in full the UK's international commitments, while continuing to meet the fiscal rules.

## ASSUMPTIONS

**B.26** The fiscal projections are based on the following assumptions:

- the economy follows the path described in Annex A. The fiscal projections assume that trend growth will be 2½ per cent to 2011-12. In the interests of caution, these projections continue to be based on the assumption that trend output growth will be ¼ percentage point lower than the Government's neutral view;
- there are no tax or spending policy changes beyond those announced in or before this Pre-Budget Report, and the indexation of rates and allowances. Consistent with the *Code for fiscal stability*, the forecast does not take account of measures proposed in this Pre-Budget Report for consultation or other proposals where final decisions have yet to be taken;
- firm Departmental Expenditure Limits (DEL) are as set out in the 2004 Spending Review to 2007-08, adjusted for the impact of policy decisions and reclassifications;
- total Annually Managed Expenditure (AME) programmes to 2007-08 have been reviewed in this Pre-Budget Report;

- as is normal, HM Treasury is setting out its assumptions for public sector current expenditure for the period beyond the current Spending Review. These are unchanged from Budget 2006 and roll forward into 2011-12. Public sector current expenditure is forecast to grow by 2.0 per cent in real terms in 2008-09 and by 1.9 per cent in 2009-10, 2010-11, and 2011-12. This means that, on average, public sector current expenditure is forecast to grow by 2<sup>1</sup>/<sub>4</sub> per cent per year in real terms between 2006-07 and the end of the 2007 Comprehensive Spending Review period; and
- net investment is assumed to remain at 2<sup>1</sup>/<sub>4</sub> per cent of GDP in 2008-09 and subsequent years.

**Table B3: Economic assumptions for the public finance projections**

	Percentage changes on previous year						
	Outturn	Estimate	Projections				
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Output (GDP)	2	2 3/4	2 3/4	2 1/2	2 1/2	2 1/2	2 1/2
Prices							
CPI	2	2 1/2	2	2	2	2	2
GDP deflator	2	2 3/4	2 3/4	2 3/4	2 3/4	2 3/4	2 3/4
RPI <sup>1</sup> (September)	2 3/4	3 1/2	3 1/4	2 3/4	2 3/4	2 3/4	2 3/4
Rossi <sup>2</sup> (September)	2	3	2 1/4	2 1/4	2 1/4	2 1/4	2 1/4
Money GDP <sup>3</sup> (£ billion)	1,238	1,305	1,378	1,449	1,524	1,603	1,685

<sup>1</sup> Used for revalorising excise duties in current year and uprating income tax allowances and bands and certain social security benefits in the following year.

<sup>2</sup> RPI excluding housing costs, used for uprating certain social security benefits.

<sup>3</sup> Not seasonally adjusted.

**B.27** The projections for 2006-07 are based on all available data within HM Treasury and other government departments involved in producing tax and spending forecasts.

**B.28** The key assumptions underlying the fiscal projections are audited by the NAO under the three-year rolling review process. Details of the audited assumptions are provided in Box B1.

**The audited assumptions**

**B.29** For this Pre-Budget Report, the Comptroller and Auditor General audited the change to the Treasury's post-2006 cautious trend output growth assumption used for the public finances forecasts, which it has revised to continue at 2<sup>1</sup>/<sub>2</sub> per cent a year. The Comptroller and Auditor General found that the Treasury's revised underlying growth rate assumption is below the range of external forecasts of the long term growth rate. It is also at or below the average of external forecasters' medium term growth projections. The review concluded that on this basis the revised Treasury assumption is reasonable and cautious.

**B.30** The Comptroller and Auditor General audited the Treasury's equity price assumption and found that the assumption of linking equity price growth to that of money GDP has a theoretical and hence reasonable basis, though in practice, the relationship is unlikely to be valid at all times. The review also concluded that for the 2003 to 2006 period, the assumption proved to be a cautious one for most of the projections of the public finances made in the three years, as outturn equity prices exceeded the Treasury's forecasts.

**B.31** The Comptroller and Auditor General also audited the assumption on the consistency of the price indices used to project the public finances with the CPI, which is used in the definition of the inflation target. The review confirmed that over the period 2003 to 2006 the series were, and that for the future they remain, consistent with each other and with the CPI.

**Box BI: Key assumptions audited by the NAO<sup>a</sup>**

<b>Trend GDP growth<sup>g</sup></b>	<b>2½ per cent a year.</b>
<b>Dating of the cycle<sup>e</sup></b>	<b>The end date of the previous economic cycle was in the first half of 1997.</b>
<b>Privatisation proceeds</b>	<b>Credit is taken only for proceeds from sales that have been announced.</b>
<b>UK claimant unemployment<sup>d</sup></b>	<b>Rising slowly to 1.01 million in 2007-08, from recent levels of 0.96 million.<sup>h</sup></b>
<b>Interest rates<sup>f</sup></b>	<b>3-month market rates change in line with market expectations (as of 24 November).</b>
<b>Equity prices<sup>g</sup></b>	<b>FTSE All-share index rises from 3148 (close 24 November) in line with money GDP.</b>
<b>VAT<sup>b,c,e</sup></b>	<b>The VAT gap will rise by 0.5 percentage points per year from a level that is at least as high as the estimated outturn for the current year.</b>
<b>Consistency of price indices<sup>g</sup></b>	<b>Projections of price indices used to project the public finances are consistent with CPI.</b>
<b>Composition of GDP<sup>c</sup></b>	<b>Shares of labour income and profits in national income are broadly constant in the medium term.</b>
<b>Funding<sup>c</sup></b>	<b>Funding assumptions used to project debt interest are consistent with the forecast level of government borrowing and with financing policy.</b>
<b>Oil prices<sup>e</sup></b>	<b>\$60.3 a barrel in 2007, the average of independent forecasts, and then constant in real terms.</b>
<b>Tobacco<sup>f</sup></b>	<b>The underlying market share of smuggled cigarettes will be set at least at the latest published outturn. For Budget 2006, a share of 14 per cent is used for 2006-07 onwards.</b>

<sup>a</sup> For details of all NAO audits before the 2003 Pre-Budget Report, see Budget 2003, 9 April 2003 (HC500).

<sup>b</sup> Audit of Assumptions for the 2003 Pre-Budget Report, 10 December 2003 (HC35).

<sup>c</sup> Audit of Assumptions for the 2004 Budget, 17 March 2004 (HC434).

<sup>d</sup> Audit of Assumptions for the 2005 Budget, 16 March 2005 (HC452).

<sup>e</sup> Audit of Assumptions for the 2005 Pre-Budget Report, 5 December 2005 (HC707).

<sup>f</sup> Audit of Assumptions for the 2006 Budget, 22 March 2006 (HC937).

<sup>g</sup> Audit of Assumptions for the 2006 Pre-Budget Report, 6 December 2006 (HC).

<sup>h</sup> This is a cautious assumption based on the average of external forecasts and is not the Treasury's central economic forecast.

## PRE-BUDGET REPORT POLICY DECISIONS

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**B.32** Consistent with the requirements of the *Code for fiscal stability* the updated projections take into account the fiscal effects of all firm decisions announced in the 2006 Pre-Budget Report or since Budget 2006. The fiscal impact of these measures are set out in Tables B4 and B5, these include increasing air passenger duty rates, measures to protect tax revenues, and direct payments to schools.

**B.33** AME expenditure measures have been added to total AME in 2006-07 and 2007-08, but in subsequent years are included within the spending envelope assumptions described in paragraph B26.

**B.34** Consistent with the *Code for fiscal stability*, the projections do not take account of decisions where the impact cannot yet be quantified, of measures proposed in this Pre-Budget Report, or where final decisions have yet to be taken. These include:

- further extensions to maternity and paternity leave; and
- further reforms to incapacity benefit.

**B.35** The measures in Table B4 that tackle avoidance and tax fraud represent the estimated direct Exchequer effect of the measure on existing levels of avoidance or fraud activity. Further details explaining how the Exchequer effects of measures are calculated can be found in Appendix A2 of the Financial Statement and Budget Report 2006.

**Table B4: Estimated costs for Pre-Budget Report policy decisions and others announced since Budget 2006<sup>1</sup>**

	£ million			
	2006-07	2007-08	2008-09	2009-10
<b>Increasing employment opportunity for all</b>				
Increase in Housing Benefit disregard	0	-5	-	-
Supporting people into work through extending the job grant	*	-5	-	-
<b>Building a fairer society</b>				
July renewal deadline for Child and Working Tax Credits <sup>2</sup>	0	+60	+20	+10
Tackling Managed Service Companies	0	+350	+450	+250
Film tax reliefs: transitional arrangements	0	-20	-20	*
Life assurance companies reform	0	-15	-20	-10
Simplification of general insurers' reserves	0	0	+130	+150
VAT: partial exemption special method	0	+20	+20	+25
Construction Industry Scheme deduction rates	0	+250	-10	-20
Increasing travellers' allowance from outside the EU	0	-15	-15	-15
<b>Protecting revenues</b>				
Controlled Foreign Companies: repeal of public quotation exemption <sup>3</sup>	+20	+125	+160	+160
Tackling avoidance using structured finance arrangements	+10	+15	+15	+15
Countering corporation tax avoidance	+110	+180	+195	+195
Life assurance companies: valuation rules	+70	+95	+95	+95
Stamp duty land tax anti-avoidance	+25	+75	+70	+70
Countering CGT avoidance	0	+70	+130	+120
<b>Protecting the environment</b>				
Air passenger duty rates <sup>4</sup>	+165	+1,000	+1,100	+1,200
Fuel duties: revalorise main rates from 7 December 2006	-190	0	0	0
Fuel duties: maintain the differential for rebated oils from 7 December 2006	-20	0	0	0
Rebated oils: changes to excepted vehicle schedule	0	-5	0	0
Extension of the Landlords Energy Saving Allowance	0	0	-10	-10
<b>Other policy decisions</b>				
Direct payments to schools	0	-155	-	-
<b>TOTAL POLICY DECISIONS</b>	<b>+190</b>	<b>+2,020</b>	<b>+2,310</b>	<b>+2,235</b>

\* Negligible

- Included within the current spending growth assumption from 2008-09 onwards.

<sup>1</sup> Costings shown relative to an indexed base.

<sup>2</sup> The savings in AME spending as a result of this measure are included within the current spending growth assumption from 2008-09 onwards.

<sup>3</sup> Alongside the revenue raised by this measure, forecast tax revenues have been adjusted as a result of the European Court of Justice ruling on the taxation of Controlled Foreign Companies and the Government's response to it, as described in Chapter 5. The impact on tax revenues of this adjustment is estimated as:

	2006-07	2007-08	2008-09	2009-10
	-15	-100	-175	-250

<sup>4</sup> The costing assumes revalorisation annually from 1 April 2008.

**Rates and allowances B.36** The income tax personal allowances will increase in line with inflation in 2007-08, as will the national insurance contributions (NICs) thresholds and limits. There will be no change to NICs rates for employers and employees, or to the Class 4 rate paid by the self-employed. The flat rate of Class 2 NICs paid by the self-employed and the special rates of Class 2 for share fisherman and for volunteer development workers will increase in line with inflation, as will the rate of Class 3 contributions. Tables B5 and B6 set this out in greater detail.

**Table B5: National insurance contribution rates 2007-08**

Earnings <sup>1</sup> £ per week	Class I rates		Self employed NICs		
	Employee (primary) NIC rate <sup>2</sup> per cent	Employer (secondary) NIC rate <sup>3</sup> per cent	Profits <sup>1</sup> £ per year	Class 2 £ per week	Class 4 per cent
Below 87 (LEL)	0	0	Below 4,635 (SEE)	0 <sup>5</sup>	0
87 to 100 (PT/ST)	0 <sup>4</sup>	0	4,635 to 5,225 (LPL)	2.20	0
100 to 670 (UEL)	11	12.8	5,225 to 34,840 (UPL)	2.20	8
Above 670	1	12.8	Above 34,840	2.20	1

<sup>1</sup> The limits are defined as LEL - lower earnings limit; PT - primary threshold; ST - secondary threshold; UEL - upper earnings limit; LPL - lower profits limit; UPL - upper profits limit; SEE - small earnings exception.

<sup>2</sup> The contracted-out rebate for primary contributions in 2007-08 is 1.6 per cent of earnings between the LEL and UEL for contracted-out-salary-related schemes (COSRS) and contracted-out money purchase schemes (COMPS).

<sup>3</sup> The contracted-out rebate for secondary contributions is 3.7 per cent of earnings between the LEL and UEL for COSRS and 1.4 per cent for COMPS. For COMPS, an additional age-related rebate is paid direct to the scheme following the end of the tax year. For appropriate personal pensions, the employee and employer pay NICs at the standard, not contracted-out rate. An age and earnings-rebate is paid direct to the personal pension provider following the end of the tax year.

<sup>4</sup> No NICs are actually payable but a Class I NIC is treated as having been paid in respect of earnings between the LEL and PT to protect benefit entitlement.

<sup>5</sup> The self-employed may apply for exception from paying Class 2 contributions if their earnings are less than, or expected to be less than, the level of the small earnings exception.

**Table B6: Income tax allowances 2007-08**

	£ per year		
	2006-07	2007-08	Increase
Personal allowance			
age under 65	5,035	5,225	190
age 65-74	7,280	7,550	270
age 75 and over	7,420	7,690	270
Married couple's allowance <sup>1</sup>			
aged less than 75 and born before 6 April 1935	6,065	6,285	220
age 75 and over	6,135	6,365	230
minimum amount <sup>2</sup>	2,350	2,440	90
Income limit for age-related allowances	20,100	20,900	800
Blind person's allowance	1,660	1,730	70

<sup>1</sup> Tax relief for this allowance is restricted to 10 per cent.

<sup>2</sup> This is also the maximum relief for maintenance payments where at least one of the parties is born before 6 April 1935.

**B.37** As set out in Table B7, the child element of the Child Tax Credit will be increased by £80 to £1,845 per year from 6 April 2007, in line with earnings growth. All the elements of Working Tax Credit rise in line with inflation (the increase in the RPI in the year to September 2006), as do the disabled child elements of Child Tax Credit. The rates of Child Benefit and Guardian's Allowance will also increase in line with inflation.

**Table B7: Working and Child Tax Credit rates and thresholds**

	£ per year		Increase
	2006-07	2007-08	
<b>Working Tax Credit</b>			
Basic Element	1,665	1,730	65
Couple and lone parent element	1,640	1,700	60
30 hour element	680	705	25
Disabled worker element	2,225	2,310	85
Severe disability element	945	980	35
50 plus element, 16–29 hours	1,140	1,185	45
50 plus element, 30+ hours	1,705	1,770	65
Childcare element			
maximum eligible cost for one child	£175 per week	£175 per week	-
maximum eligible cost for two or more children	£300 per week	£300 per week	-
<i>per cent of eligible costs covered</i>	80%	80%	-
<b>Child Tax Credit</b>			
Family element	545	545	-
Family element, baby addition	545	545	-
Child element	1,765	1,845	80
Disabled child element	2,350	2,440	90
Severely disabled child element	945	980	35
<b>Income thresholds and withdrawal rates</b>			
First income threshold	5,220	5,220	-
<i>First withdrawal rate (per cent)</i>	37%	37%	-
Second income threshold	50,000	50,000	-
<i>Second withdrawal rate (per cent)</i>	7%	7%	-
First threshold for those entitled to Child Tax Credit only	14,155	14,495	340
Income disregard	25,000	25,000	-

## FISCAL AGGREGATES

**B.38** Tables B8 and B9 provide more detail on the projections for the current and capital budgets.

**Table B8: Current and capital budgets**

	£ billion						
	Outturn	Estimate	Projections				
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
<b>Current budget</b>							
Current receipts	485.3	517.9	554	586	616	647	681
Current expenditure	483.9	508.1	537	562	588	615	643
Depreciation	16.5	17.6	19	20	21	22	23
<b>Surplus on current budget</b>	<b>-15.1</b>	<b>-7.9</b>	<b>-1</b>	<b>4</b>	<b>7</b>	<b>10</b>	<b>14</b>
<b>Capital budget</b>							
Gross investment <sup>1</sup>	38.9	46.5	48	51	54	57	60
Less depreciation	-16.5	-17.6	-19	-20	-21	-22	-23
Net investment	22.4	28.9	30	31	33	35	36
<b>Net borrowing</b>	<b>37.5</b>	<b>36.8</b>	<b>31</b>	<b>27</b>	<b>26</b>	<b>24</b>	<b>22</b>
<b>Public sector net debt - end year</b>	<b>462.7</b>	<b>503.9</b>	<b>540</b>	<b>573</b>	<b>605</b>	<b>636</b>	<b>665</b>
Memos:							
Treaty deficit <sup>2</sup>	35.1	34.8	31	27	26	24	22
Treaty debt <sup>3</sup>	529.1	570.1	608	641	674	705	735

<sup>1</sup> Includes asset sales, for a breakdown see table B21.

<sup>2</sup> General government net borrowing on a Maastricht basis.

<sup>3</sup> General government gross debt on a Maastricht basis.

**Table B9: Current and capital budgets**

	Per cent of GDP						
	Outturn	Estimate	Projections				
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
<b>Current budget</b>							
Current receipts	39.2	39.7	40.2	40.4	40.4	40.4	40.4
Current expenditure	39.1	38.9	38.9	38.8	38.6	38.4	38.2
Depreciation	1.3	1.4	1.4	1.4	1.4	1.4	1.4
<b>Surplus on current budget</b>	<b>-1.2</b>	<b>-0.6</b>	<b>-0.1</b>	<b>0.3</b>	<b>0.5</b>	<b>0.6</b>	<b>0.8</b>
<b>Capital budget</b>							
Gross investment <sup>1</sup>	3.1	3.6	3.5	3.5	3.5	3.5	3.5
Less depreciation	-1.3	-1.4	-1.4	-1.4	-1.4	-1.4	-1.4
Net investment	1.8	2.2	2.2	2.2	2.2	2.2	2.2
<b>Net borrowing</b>	<b>3.0</b>	<b>2.8</b>	<b>2.3</b>	<b>1.9</b>	<b>1.7</b>	<b>1.5</b>	<b>1.3</b>
<b>Public sector net debt - end year</b>	<b>36.4</b>	<b>37.5</b>	<b>38.2</b>	<b>38.6</b>	<b>38.7</b>	<b>38.7</b>	<b>38.5</b>
Memos:							
Treaty deficit <sup>2</sup>	2.8	2.7	2.2	1.9	1.7	1.5	1.3
Treaty debt ratio <sup>3</sup>	42.7	43.7	44.1	44.2	44.2	44.0	43.6

<sup>1</sup> Includes asset sales, for a breakdown see table B21.

<sup>2</sup> General government net borrowing on a Maastricht basis.

<sup>3</sup> General government gross debt on a Maastricht basis.

**B.39** Following a deficit of 3 per cent of GDP in 1996-97, current budget surpluses of more than 2 per cent were recorded in 1999-2000 and 2000-01. These surpluses allowed the Government to use fiscal policy to support monetary policy during the economic slowdown in 2001 and 2002, and as a result the current budget moved into deficit. The current budget is expected to remain in deficit until 2007-08 and to move back into surplus in 2008-09, with increasingly larger surpluses in later years, reaching 0.8 per cent in 2011-12.

**B.40** The current budget surplus is equal to public sector current receipts less public sector current expenditure and depreciation. The reasons for changes in receipts and current expenditure are explained in later sections. Depreciation is higher throughout the forecast period as a result of revisions to outturn data for 2005-06 and earlier years.

**B.41** Table B8 also shows that net investment is projected to increase from £22.4 billion in 2005-06 to £30 billion in 2007-08 as the Government seeks to rectify historical underinvestment in public infrastructure. These increases are sustainable and the Government is still able to meet its strict fiscal rules, as debt is being held below 39 per cent of GDP, within the 40 per cent limit imposed by the sustainable investment rule.

## RECEIPTS

**B.42** This section looks in detail at the projections for public sector tax receipts. It begins by looking at the main determinants of changes in the overall projections since Budget 2006, before looking in detail at changes in the projections of individual tax receipts. Finally, it provides updated forecasts for the tax-GDP ratios.

### Changes in total receipts since Budget 2006

**B.43** The forecast for public sector current receipts for 2006-07 has been revised up by £1½ billion since Budget 2006. However, before allowing for discretionary changes, receipts are lower by around £1½ billion per year from 2007-08 to 2009-10, before returning to the Budget 2006 forecast level in 2010-11. The total changes throughout the forecast are lower than would be expected given changes in the level of money GDP and its components, mostly due to lower receipts from North Sea taxes following revised production and expenditure forecasts and a stronger dollar-sterling exchange rate. Including discretionary measures, current receipts remain higher than the Budget 2006 profile throughout the forecast.

**B.44** Table B10 provides a breakdown of the causes of these revisions since Budget 2006. Revisions are split between discretionary changes, and non-discretionary changes to North Sea revenues, those arising from changes to money GDP and its components, and other forecasting changes.

**Table B10: Changes in current receipts since Budget 2006**

	£ billion				
	Estimate	Projections			
	2006-07	2007-08	2008-09	2009-10	2010-11
Effect on receipts of non-discretionary changes in:					
North Sea taxes	0	-3	-2	-1	-1
Money GDP and components	2	2	1 1/2	1 1/2	2
Other forecasting changes	-1	-1/2	-1 1/2	-1 1/2	-1
<b>Total before discretionary changes<sup>1</sup></b>	<b>1 1/2</b>	<b>-1 1/2</b>	<b>-2</b>	<b>-1 1/2</b>	<b>0</b>
Discretionary changes <sup>1</sup>	0	2	2 1/2	2	2
<b>Total change<sup>2</sup></b>	<b>1 1/2</b>	<b>1/2</b>	<b>1/2</b>	<b>1</b>	<b>2 1/2</b>

<sup>1</sup> Includes measures announced since Budget 2006.

<sup>2</sup> Total may not sum due to rounding.

**North Sea taxes B.45** The impacts of movements in North Sea revenues from changes in the dollar oil price, the dollar-sterling exchange rate, production, capital and operating expenditure are analysed in Box B2.

**Money GDP and components B.46** The impact of money GDP and its components is to add about £2 billion to receipts in each year of the forecast. This is largely the result of stronger employment growth assumed through the forecast period and from the government and housing components of the VAT tax base.

**Other forecasting changes B.47** A large number of different factors contribute to other forecasting changes and together are expected to reduce current receipts by an average of about £1 billion per year to the end of the forecast period.

## Tax by tax analysis

**B.48** Table B11 shows outturn data for cash receipts in the first seven months of 2006-07 and estimated receipts for the remainder of the year, along with percentage changes over the corresponding period in 2005-06. These growth rates can vary considerably across the year, reflecting the rules for payment of each tax and the various time lags. Table B12 shows the changes to the projections of individual taxes since Budget 2006, while Table B13 contains updated projections for the main components of public sector receipts for 2005-06, 2006-07 and 2007-08.

**Table B11: Net taxes and national insurance contributions 2006-07**

	£ billion			Percentage change on 2005-06		
	Outturn <sup>1</sup>	Estimates		Outturn <sup>1</sup>	Estimates	
	Apr-Oct	Nov-Mar	2006-07	Apr-Oct	Nov-Mar	Full year
<b>HM Revenue &amp; Customs</b>						
Income tax, NICs and capital gains tax <sup>2</sup>	126.9	107.1	234.0	5.7	8.1	6.8
Value added tax	45.3	30.9	76.2	4.7	4.3	4.5
Corporation tax <sup>2</sup>	30.3	17.1	47.5	17.8	6.1	13.3
Petroleum revenue tax	1.6	0.7	2.3	39.1	-22.1	12.6
Fuel duties	13.8	9.9	23.7	-0.4	3.2	1.1
Inheritance tax	2.1	1.5	3.6	9.1	8.0	8.7
Stamp duties	7.6	5.1	12.7	25.6	5.7	16.7
Tobacco duties	4.9	3.2	8.0	0.7	0.8	0.7
Alcohol duties	4.6	3.4	8.0	0.3	2.3	1.2
Other Customs duties and levies	5.1	3.8	8.9	1.7	2.4	2.0
<b>Total HMRC</b>	<b>242.1</b>	<b>182.6</b>	<b>424.7</b>	<b>7.0</b>	<b>6.4</b>	<b>6.7</b>
Vehicle excise duties	3.1	2.0	5.1	-3.3	11.9	2.3
Business rates	14.8	6.7	21.5	6.0	13.1	8.1
Council tax	14.8	7.7	22.5	4.0	8.3	5.4
Other taxes and royalties	7.6	5.7	13.3	6.1	2.9	4.7
<b>Net taxes and national insurance contributions</b>	<b>282.4</b>	<b>204.8</b>	<b>487.1</b>	<b>6.6</b>	<b>6.6</b>	<b>6.6</b>

<sup>1</sup> Provisional.

<sup>2</sup> Net of tax credits scored as negative tax in net taxes and national insurance contributions.

**Table B12: Changes in current receipts by tax since Budget 2006**

	£ billion		
	2005-06	2006-07	2007-08
Income tax (gross of tax credits)	-1.1	2.0	1.9
Income tax credits	0.2	0.0	0.0
National insurance contributions	0.1	-1.1	-0.2
Non-North Sea corporation tax <sup>1</sup>	-0.3	-0.7	-0.7
North Sea revenues	0.0	0.1	-2.8
Capital taxes <sup>2</sup>	0.2	0.2	0.7
Stamp duty	0.0	0.6	0.5
Value added tax	-0.8	-0.3	-0.5
Excise duties <sup>3</sup>	-0.1	-0.5	0.1
Other taxes and royalties <sup>4</sup>	0.0	0.3	1.2
<b>Net taxes and national insurance contributions</b>	<b>-1.8</b>	<b>0.6</b>	<b>0.2</b>
Other receipts and accounting adjustments	1.0	0.8	0.4
<b>Current receipts</b>	<b>-0.8</b>	<b>1.4</b>	<b>0.6</b>

<sup>1</sup> National accounts measure: gross of enhanced and payable tax credits.

<sup>2</sup> Capital gains tax and inheritance tax.

<sup>3</sup> Fuel, alcohol and tobacco duties.

<sup>4</sup> Includes business rates, council tax and money paid into the National Lottery Distribution Fund, as well as other central government taxes.

**Box B2: North Sea Revenues**

The significant increase in oil prices since the start of 2004 has led to large rises in the profitability of North Sea companies. The net rate of return for UK Continental Shelf companies was close to 40 per cent in the first half of 2006, substantially above the 13 per cent return recorded by other non-financial companies. Given the upward shift in the expected price of oil in the medium term, oil and gas companies should continue to register strong profit figures over the forecast period.

North Sea revenues for 2006-07 are expected to be close to their Budget projection at just over £10 billion. Oil prices are likely to average around \$9 a barrel higher than the \$57.4 assumed in Budget 2006 and this would be expected to result in higher tax revenues. However, while North Sea profits remain very strong, the further boost to taxable profits from higher than expected dollar oil prices is being offset by a stronger dollar-sterling exchange rate (which reduces the rise in the sterling price of oil), lower than anticipated production, higher capital investment and increased operating expenditure.

The forecast for North Sea revenues assumes a further rise in receipts to £10.7 billion in 2007-08, but this is a much more modest increase than assumed in the Budget 2006 forecast and reflects developments in prices and production as well as continued downward pressure on profits from higher capital and operating expenditure. The projections for North Sea revenues use the NAO audited assumption on oil prices. In line with the average of independent forecasts, oil prices are expected to be \$60.3 a barrel in 2007, around \$2 higher than assumed in the Budget 2006 forecast. However, the stronger dollar-sterling rate means that oil prices in sterling are lower from 2007 onwards than assumed in Budget 2006.

Investment in the North Sea has continued to increase and is now substantially higher than the capital expenditure projections incorporated into the North Sea revenues forecast prior to the announcement of the increase in the Supplementary Charge. This demonstrates the continuing attractiveness and competitiveness of the North Sea as a place to invest. However, despite the highest levels of investment this decade, North Sea production has been lower than expected in 2006. This seems mainly due to rising maintenance requirements for North Sea infrastructure, with further pressure created by increased global competition for equipment and skilled personnel pushing up costs as operators everywhere try to maximise production. Production is expected to rise in 2007, with a number of new developments, including the Buzzard field coming on stream. However, the overall level of production is expected to be significantly lower than assumed in the Budget 2006 forecast reflecting the lower starting point and more modest increases expected by operators. Beyond 2007-08, production is expected to gradually return to its previously assumed levels, helped by the higher levels of capital expenditure. This reduces the shortfall in revenues relative to the Budget 2006 forecast.

**Table B13: Current receipts**

	£ billion		
	Outturn 2005-06	Estimate 2006-07	Projection 2007-08
<b>HM Revenue and Customs</b>			
Income tax (gross of tax credits)	135.0	146.1	155.8
Income tax credits	-4.5	-4.6	-4.4
National insurance contributions	85.5	88.5	94.3
Value added tax	72.9	76.2	80.1
Corporation tax <sup>1</sup>	42.4	48.0	53.8
Corporation tax credits <sup>2</sup>	-0.5	-0.6	-0.6
Petroleum revenue tax	2.0	2.3	1.9
Fuel duties	23.4	23.7	25.2
Capital gains tax	3.0	4.0	4.9
Inheritance tax	3.3	3.6	4.1
Stamp duties	10.9	12.7	13.8
Tobacco duties	8.0	8.0	8.0
Spirits duties	2.3	2.3	2.4
Wine duties	2.3	2.4	2.5
Beer and cider duties	3.2	3.3	3.4
Betting and gaming duties	1.4	1.4	1.4
Air passenger duty	0.9	1.1	2.0
Insurance premium tax	2.3	2.3	2.4
Landfill tax	0.7	0.8	0.9
Climate change levy	0.7	0.7	0.7
Aggregates levy	0.3	0.3	0.3
Customs duties and levies	2.3	2.3	2.3
<b>Total HMRC</b>	<b>398.0</b>	<b>424.7</b>	<b>455.4</b>
Vehicle excise duties	5.0	5.1	5.5
Business rates	19.9	21.5	22.3
Council tax <sup>3</sup>	21.4	22.5	23.8
Other taxes and royalties <sup>4</sup>	12.7	13.3	14.5
<b>Net taxes and national insurance contributions<sup>5</sup></b>	<b>457.0</b>	<b>487.1</b>	<b>521.4</b>
Accruals adjustments on taxes	1.6	3.2	2.3
Less own resources contribution to European Commission (EC) budget	-4.3	-4.4	-4.4
Less PC corporation tax payments	-0.2	-0.2	-0.2
Tax credits adjustment <sup>6</sup>	0.6	0.6	0.7
Interest and dividends	6.2	5.3	6.1
Other receipts <sup>7</sup>	24.4	26.2	27.9
<b>Current receipts</b>	<b>485.3</b>	<b>517.9</b>	<b>553.8</b>
<i>Memo:</i>			
North Sea revenues <sup>8</sup>	9.6	10.4	10.7

<sup>1</sup> National Accounts measure: gross of enhanced and payable tax credits.

<sup>2</sup> Includes enhanced company tax credits.

<sup>3</sup> Council tax increases are determined annually by local authorities, not by the Government. As in previous years, council tax figures are projections based on stylised assumptions and are not Government forecasts.

<sup>4</sup> Includes VAT refunds and money paid into the National Lottery Distribution Fund.

<sup>5</sup> Includes VAT and 'traditional own resources' contributions to EC budget.

<sup>6</sup> Tax credits which are scored as negative tax in the calculation of NTNIC but expenditure in the national accounts.

<sup>7</sup> Includes gross operating surplus and rent; net of oil royalties and business rate payments by local authorities.

<sup>8</sup> Consists of North Sea corporation tax, petroleum revenue tax and royalties.

**Income tax and NICs** **B.49** Cash receipts of income tax and national insurance contributions (NICs) are expected to be £0.9 billion above their Budget 2006 projection. It is usually better to aggregate income tax and NICs when considering in-year trends because most employers make combined payments and a correct allocation between the receipt streams can only be made after the end of the financial year when HMRC receive the employers' end of year returns. PAYE and NIC receipts from wages and salaries are expected to be close to their Budget forecast in 2006-07. The upward revision to the projection stems from higher than expected self assessment receipts and tax on savings income, and lower income tax repayments.

**B.50** PAYE and NIC receipts in 2006-07 have been constrained by the continued subdued growth in average earnings, but have benefited from a stronger rise in employment growth than anticipated and from the buoyancy of the financial sector. This sector has a higher proportion of taxpayers who pay tax at the higher rate than other sectors of the economy. With continued evidence of robust activity growth in the financial sector, strong growth in bonuses should boost income tax and NIC receipts in the latter part of 2006-07. The pick up in cash receipts growth over the remainder of the year also reflects changes in the timing of personal pension rebates. Around 90 per cent of the expected full year total in 2006-07 has already been paid out, while in 2005-06 only around 50 per cent had been paid out by October.

**B.51** The strong growth in working age population in recent years which has been accompanied by a sustained rise in employment has led to an upward revision to the contribution to trend growth from the rise in the working age population. This leads to stronger future increases in employment than previously assumed. In addition to higher tax on savings income from the interest rate assumption audited by the NAO, this has helped offset negative effects in 2007-08 from slower growth in self-employment income and from the higher than anticipated increase in RPI inflation this year. This means that tax thresholds and allowances will increase by more than expected in April 2007.

**Non-North Sea corporation tax** **B.52** Total corporation tax receipts in the first seven months of 2006-07 were 18 per cent higher than in the comparable period a year ago. As in 2005-06, and as forecast, this is largely due to continued strong growth in receipts from the banking and oil sectors. An analysis of trends in North Sea revenues can be found in Box B2. The growth in receipts from the industrial and commercial sectors has also increased. However, non-North Sea corporation tax receipts are expected to be £0.7 billion below the Budget 2006 estimate for 2006-07, largely reflecting weaker receipts from the life assurance sector. Weaker than expected receipts from this sector are likely to be related to the fall in bond prices in early 2006.

**B.53** Non-North Sea corporation tax receipts are expected to record growth of almost 15 per cent for 2006-07 as a whole. The slowdown in overall corporation tax growth over the rest of 2006-07 mainly reflects changes in the timing of instalment payments for oil companies. In January 2007, oil companies should pay a third of their liabilities on their 2006 profits, while in January 2006 oil companies paid half of their liability on 2005 profits.

**B.54** The strong growth in implied 2006 liabilities also boosts 2007-08 non-North Sea receipts, which are expected to grow by 13 per cent. With the economy back on trend and profit growth in the financial sector expected to return to its long run trend from 2007 onwards, onshore corporation tax is expected to grow broadly in line with the economy from 2008-09 onwards.

**Capital gains tax and inheritance tax** **B.55** The forecast for capital gains tax incorporates a further year of strong receipts growth in 2006-07, helped by solid growth in equity prices in 2005-06. Most capital gains tax is collected in the final quarter of the financial year. Capital gains tax receipts rose by over 30 per cent in 2005-06, boosted by the rise in the equity and housing markets in 2004-05 and the continuing effects from the disposal of business assets following the maturing of the business asset taper relief. The rebound in the housing market during 2006 will increase receipts of both capital gains tax and inheritance tax from 2007-08, given tax payment lags.

**Stamp duties** **B.56** Receipts of stamp duty land tax have recorded robust year-on-year growth in the first seven months of 2006-07. This reflects both the pick up in the housing market in the UK as a whole and that price rises in London properties, which are more likely to be subject to higher rates of duty, have recently started to outpace other parts of the country. In addition, the commercial property market remains buoyant. Year-on-year growth in stamp duty land tax receipts is expected to moderate over the rest of 2006-07 and into 2007-08. In the near-term, this largely reflects that a rebound in property transactions in the latter half of 2005-06 will make the annual comparisons look less favourable. Further ahead, house price inflation is expected to moderate to rates in line with income growth as the monetary environment tightens. Receipts from stamp duty on shares have benefited from the continued rise in equity markets in 2006, but this has been partly offset by a fall in the number of equity trades subject to stamp duty.

**VAT receipts** **B.57** VAT receipts in 2005-06 were affected by a combination of weak consumer spending, changes in the composition of consumer spending and an increase in the VAT gap, particularly from an increase in Missing Trader Intra-Community (MTIC) fraud.

**B.58** However, VAT receipts in the first seven months of 2006-07 have picked up and were 4.7 per cent higher on a year earlier. VAT receipts have benefited from the stronger than expected economy. This has helped boost the VAT tax base, particularly from the government and housing components. However, despite the pick up in consumer spending growth there has been a further fall in the proportion of consumer spending subject to VAT at the standard rate, reflecting shifts towards spending subject to reduced rates such as on energy bills, or to exempt housing costs, and away from standard rated items such as consumer durables. Changes in relative prices are likely to be part of the explanation with the prices of energy and housing rising relative to durable goods, with the latter affected by strong domestic and global competition. Although consumer durable spending has picked up from its pronounced weakness in 2005, it remains weaker than overall spending.

**B.59** As noted in Chapter 5, HMRC have strengthened their strategy against MTIC fraud and operational indicators suggest this has led to a significant fall in MTIC-related activity during 2006-07. Growth in VAT receipts is expected to pick up further in 2007-08, helped by the continuation of slightly above trend growth in the economy into 2007.

**Excise duties** **B.60** Fuel duties are expected to be £0.3 billion lower in 2006-07 than forecast in Budget 2006. This partly reflects the delay in the revalorisation of fuel duties from 1 September until this Pre-Budget Report. In addition, high oil prices and their impact on pump prices have continued to affect the demand for fuel. This reduces fuel duty receipts, which are charged on a per litre basis. With receipts from both spirits and beer down on a year earlier in the first seven months of 2006-07, alcohol duties are expected to be £0.2 billion below their Budget 2006 projection, with stronger growth forecast to return in 2007-08. Tobacco receipts in 2006-07 are expected to be close to their Budget 2006 forecast. The forecast for 2007-08 onwards incorporates an updated estimate of the impact on receipts from the smoking ban on consumption in enclosed workplaces. The projection assumes a loss of revenues of £0.2 billion in 2007-08 and around £<sup>1</sup>/<sub>2</sub> billion in each subsequent year.

**Council tax B.61** Council tax increases are determined annually by local authorities, not by the Government and the council tax figures for 2007-08 onwards are based on stylised assumptions and are not government forecasts. Increases are based on the arithmetic average of council tax increases over the past 3 years. Since changes to council tax are broadly balanced by changes to locally financed expenditure, they have little material impact on the current balance or on net borrowing.

**Other taxes and receipts B.62** Other taxes and royalties are expected to be over £1 billion higher in 2007-08 than projected in Budget 2006. This mainly reflects the rise in air passenger duties from February 2007, although VAT refunds are also expected to be higher than previously forecast. Other receipts are also expected to be higher, primarily because of the inclusion of renewable obligation certificates as receipts in the 2006 Blue Book. These add to both receipts and expenditure and hence are neutral for the overall fiscal balances.

### Tax-GDP ratio

**B.63** Table B14 shows projections of receipts from major taxes as a per cent of GDP, and Table B15 sets out current and previous projections of the overall tax-GDP ratio, based on net taxes and national insurance contributions. Chart B3 shows the tax-GDP ratio from 1981-82 to 2011-12.

**B.64** The tax-GDP ratio is expected to be lower throughout the forecast than assumed in the Budget 2006 projections. This is primarily due to higher money GDP. Revisions in the 2006 Blue Book raised estimates of both real GDP and GDP deflator inflation for recent years.

**B.65** The tax-GDP ratio stabilises at 38.1 per cent from 2008-09 onwards. The rise over the next two years is mainly due to increases in the income tax and corporation tax to GDP ratios. The rise in the income tax to GDP ratio largely arises from the normal fiscal forecasting convention on tax allowances and fiscal drag. The sharp rise in the non-North Sea corporation tax to GDP ratio in recent year reflects the recovery in profitability, particularly in the financial sector. The ratio is expected to flatten off during 2008-09, with both the overall economy and financial company profitability expected to grow in line with trend.

**Table BI4: Current receipts as a proportion of GDP**

	Per cent of GDP						
	Outturn	Estimate	Projections				
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Income tax (gross of tax credits)	10.9	11.2	11.3	11.5	11.6	11.7	11.8
National insurance contributions	6.9	6.8	6.8	6.9	6.9	6.9	6.9
Non-North Sea corporation tax <sup>1</sup>	2.8	3.1	3.3	3.4	3.3	3.4	3.4
Tax credits <sup>2</sup>	-0.4	-0.4	-0.4	-0.4	-0.3	-0.3	-0.3
North Sea revenues <sup>3</sup>	0.8	0.8	0.8	0.8	0.8	0.7	0.7
Value added tax	5.9	5.8	5.8	5.8	5.8	5.7	5.7
Excise duties <sup>4</sup>	3.2	3.0	3.0	2.9	2.9	2.8	2.8
Other taxes and royalties <sup>5</sup>	6.9	7.0	7.2	7.2	7.1	7.1	7.2
<b>Net taxes and national insurance contributions<sup>6</sup></b>	<b>36.9</b>	<b>37.3</b>	<b>37.8</b>	<b>38.1</b>	<b>38.1</b>	<b>38.1</b>	<b>38.1</b>
Accruals adjustments on taxes	0.1	0.2	0.2	0.2	0.1	0.1	0.1
Less EU transfers	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3
Other receipts <sup>7</sup>	2.5	2.4	2.5	2.5	2.5	2.5	2.5
<b>Current receipts</b>	<b>39.2</b>	<b>39.7</b>	<b>40.2</b>	<b>40.4</b>	<b>40.4</b>	<b>40.4</b>	<b>40.4</b>

<sup>1</sup> National accounts measure, gross of enhanced and payable tax credits.

<sup>2</sup> Tax credits scored as negative tax in net taxes and national insurance contributions.

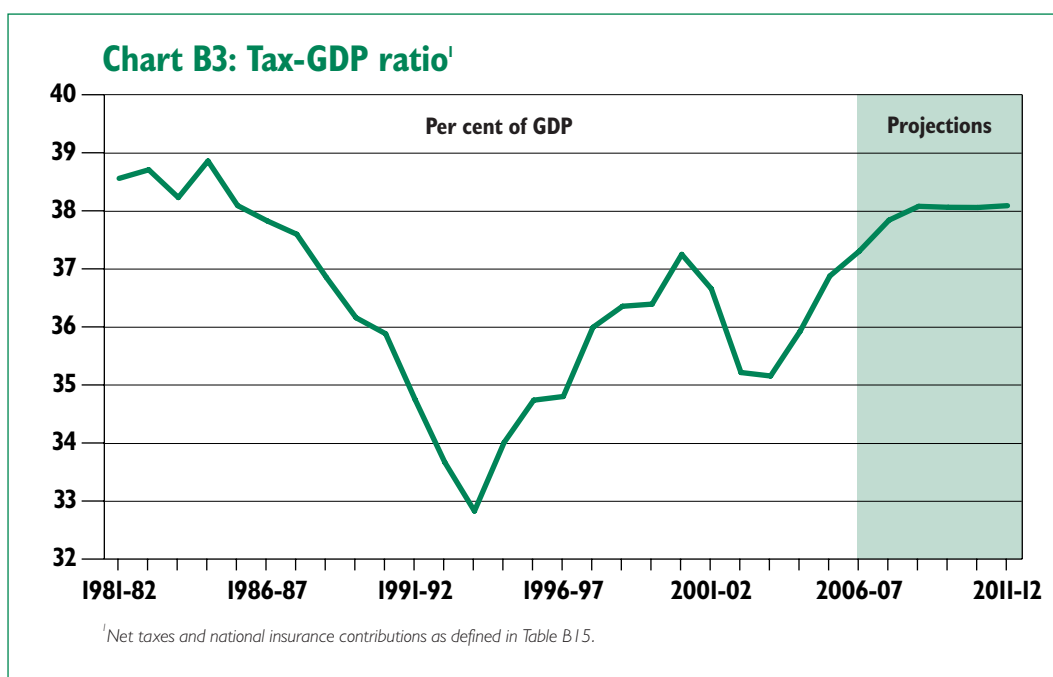
<sup>3</sup> Includes oil royalties, petroleum revenue tax and North Sea corporation tax.

<sup>4</sup> Fuel, alcohol and tobacco duties.

<sup>5</sup> Includes council tax and money paid into the National Lottery Distribution Fund, as well as other central government taxes.

<sup>6</sup> Includes VAT and 'own resources' contributions to EC budget. Cash basis.

<sup>7</sup> Mainly gross operating surplus and rent, excluding oil royalties.



**Table B15: Net taxes and national insurance contributions<sup>1</sup>**

	Per cent of GDP						
	Outturn <sup>2</sup>	Estimate <sup>3</sup>	Projections				
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Budget 2006	37.5	38.0	38.5	38.7	38.7	38.7	
<b>PBR 2006</b>	<b>36.9</b>	<b>37.3</b>	<b>37.8</b>	<b>38.1</b>	<b>38.1</b>	<b>38.1</b>	<b>38.1</b>

<sup>1</sup> Cash basis. Uses OECD definition of tax credits scored as negative tax.

<sup>2</sup> The 2005-06 figures were estimates in Budget 2006.

<sup>3</sup> The 2006-07 figures were projections in Budget 2006.

## PUBLIC EXPENDITURE

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

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

### Changes in TME since Budget 2006

**B.68** The main forecasting changes to TME in the 2004 Spending Review period since Budget 2006 are to AME, where the totals for 2006-07 and 2007-08 have been revised up as a result of changes to the forecasts of individual AME components.

**B.69** Discretionary changes to TME since the Budget 2006 forecast reflect the Pre-Budget Report spending measures listed in Table B4. In total these measures increase spending by £0.1 billion in 2007-08. The main change is an increase to DEL on direct payments to schools.

**B.70** The provisional outturn for public sector net investment in 2005-06 was lower than estimated in Budget 2006. This is due to higher depreciation figures in the National Accounts, an adjustment to remove capital grants to London and Continental Railways from overall public spending following its reclassification to the public sector, and departmental capital underspends. Projected capital spending for departmental budgets will be updated at the time of the budget.

**Table B16: Total Managed Expenditure 2005-06 to 2007-08**

	£ billion		
	Outturn 2005-06	Estimate 2006-07	Projection 2007-08
<i>Departmental Expenditure Limits</i>			
Resource Budget	277.1	294.5	309.9
Capital Budget	35.8	42.6	45.7
Less depreciation	-10.3	-11.8	-11.5
<b>Total Departmental Expenditure Limits</b>	<b>302.6</b>	<b>325.3</b>	<b>344.2</b>
<i>Annually Managed Expenditure</i>			
Social security benefits <sup>1</sup>	127.4	132.1	139.5
Tax credits <sup>1</sup>	15.4	16.0	15.8
Net public service pensions <sup>2</sup>	0.3	0.9	0.9
National Lottery	1.8	1.7	1.5
BBC domestic services	3.2	3.3	3.4
Other departmental expenditure	3.6	3.3	2.8
Net expenditure transfers to EU institutions <sup>3</sup>	4.4	4.1	6.0
Locally-financed expenditure <sup>4</sup>	25.4	26.4	27.8
Central government gross debt interest	25.8	27.4	28.3
Public corporations' own-financed capital expenditure	6.1	7.0	4.3
AME margin	0.0	0.0	0.0
Accounting adjustments <sup>5</sup>	6.8	7.2	10.6
<b>Total Annually Managed Expenditure</b>	<b>220.3</b>	<b>229.3</b>	<b>240.9</b>
<b>Total Managed Expenditure</b>	<b>522.8</b>	<b>554.6</b>	<b>585.1</b>
<i>of which:</i>			
Public sector current expenditure	483.9	508.1	536.6
Public sector net investment	22.4	28.9	29.8
Public sector depreciation	16.5	17.6	18.6

<sup>1</sup> For 2005-06 to 2007-08, child allowances in Income Support and Jobseekers' Allowance, which, from 2003-04, are paid as part of the Child Tax Credit, have been included in the tax credits line and excluded from the social security benefits line.

<sup>2</sup> Net public service pensions expenditure is reported on a National Accounts basis.

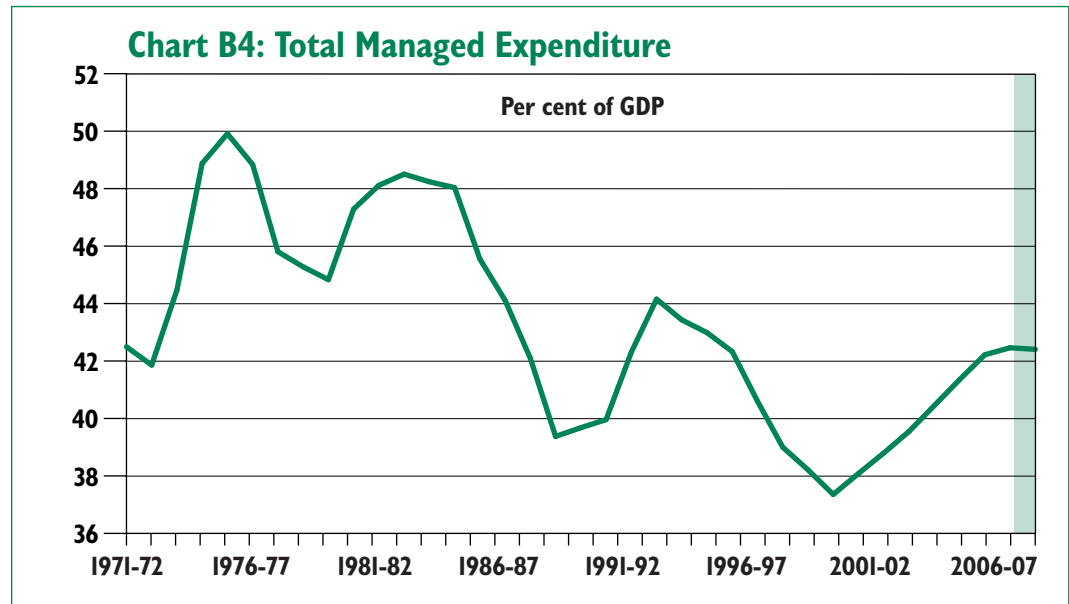
<sup>3</sup> AME spending component only. Total net payments to EU institutions also include receipts scored in DEL, VAT based contributions which score as negative receipts and some payments which have no effect on the UK public sector in the national accounts. Latest estimates for total net payments,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

	2005-06	2006-07	2007-08
Net payments to EU institutions	3.8	2.1	3.8
Net contribution to EC Budget	4.4	2.8	4.5

<sup>4</sup> This expenditure is mainly financed by council tax revenues. See footnote to table B13 for an explanation of how the council tax projections are derived.

<sup>5</sup> Excludes depreciation.

**B.71** Chart B4 shows TME as a per cent of GDP from 1971-72 to 2007-08



**Table B17: Changes to Total Managed Expenditure since Budget 2006**

	£ billion		
	Outturn 2005-06	Estimate 2006-07	Projections 2007-08
<i>Departmental Expenditure Limits</i>			
Resource Budget	-0.5	0.0	0.2
Capital Budget	-1.6	0.1	0.1
Less depreciation	1.7	0.0	0.0
<b>Total Departmental Expenditure Limits</b>	<b>-0.4</b>	<b>0.1</b>	<b>0.4</b>
<i>Annually Managed Expenditure</i>			
Social security benefits	0.0	0.5	1.2
Tax credits	0.0	0.4	0.6
Net public service pensions	-0.1	0.5	0.6
National Lottery	0.0	0.0	0.0
BBC domestic services	0.1	0.0	0.0
Other departmental expenditure	-0.7	-0.3	-0.4
Net expenditure transfers to EU institutions	0.0	-1.3	-0.5
Locally-financed expenditure	-1.2	-1.2	-1.5
Central government gross debt interest	0.1	1.1	0.4
Public corporations' own-financed capital expenditure	3.3	4.0	1.3
AME margin	0.0	-1.0	-2.0
Accounting adjustments	-1.4	-0.5	2.1
<b>Total Annually Managed Expenditure</b>	<b>0.1</b>	<b>2.2</b>	<b>1.9</b>
<b>Total Managed Expenditure</b>	<b>-0.3</b>	<b>2.3</b>	<b>2.3</b>
<i>of which:</i>			
Public sector current expenditure	2.0	1.4	2.4
Public sector net investment	-3.3	0.1	-1.1
Public sector depreciation	0.9	0.8	0.9

## Central Government spending in 2006-07

**B.72** Monthly spending information is only available for central government. Provisional outturn for current expenditure in the first seven months of 2006-07 is 7.1 per cent higher than in the corresponding period in 2005-06. Growth is higher in the year to date than the 2006 Pre-Budget Report estimate for 2006-07 as a whole, as a result of factors which affect the pattern of spending across the year.

**B.73** Debt interest payments for the year to date are 2.1 per cent higher than the same period last year, and are expected to grow more rapidly over the remainder of the year. This is due to the lagged impact of RPI inflation on the uplift of index-linked gilt payments.

**B.74** Provisional outturn data for net social benefit expenditure for the first seven months of 2006-07 show growth of 4.4 per cent over the same period in 2005-06. Growth is expected to moderate over the remainder of the year.

**B.75** Other current expenditure is 8.7 per cent higher for the year to date, above the Pre-Budget Report estimate of 5.3 per cent growth for the year as a whole. Growth is expected to be much lower over the rest of the year, largely because of changes to the timing of grant payments in respect of education and social care. A much higher proportion of these grants scored in the first four months of 2006-07 than in 2005-06, and a much lower proportion will fall in the last two months.

## DEL and AME analysis

**B.76** Table B16 sets out projected spending on DEL and the main components of AME to the end of the 2004 Spending Review period in 2007-08. Table B17 shows changes since Budget 2006.

**B.77** The detailed allocation of DEL is shown in table B18. In line with previous practice, resource and capital DEL in 2006-07 includes an allowance for shortfall, which reflects likely underspending against departmental provision.

**B.78** The main economic assumptions underpinning the AME projections are set out in Box B1 and Table B3. In particular it is assumed that UK claimant count unemployment rises from current levels. This is a cautious assumption for the purposes of the public finances forecast and does not represent the Treasury's central economic forecast. Many of the changes in the forecasts of AME components since Budget 2006 are attributable to higher RPI inflation in 2006.

**B.79** Social security expenditure, before taking discretionary measures into account, is forecast to be higher than expected at Budget 2006. Part of this increase reflects a change in the definition of spending included within the social security heading, to include additional spending of around £0.2 billion per year, which is offset by a reduction in accounting adjustments. In 2006-07 the upward effect on spending caused by higher unemployment has been partly offset by revised estimated profiles of benefit claim figures for the year to date. There are similar effects in 2007-08 but the primary reason for increased spending is the higher than expected RPI level for September 2006 which is used to uprate 2007-08 benefit levels. This is partly offset by a downward adjustment on forecast spending on Pension Credit, reflecting a revision of predicted growth in caseload.

**B.80** Projected expenditure on the Child and Working Tax Credits has been revised upwards since Budget 2006. New information about 2005-06 shows higher levels of entitlement than forecast, which resulted from a number of factors including lower earnings growth among low-income households. This increases subsequent years' expenditure.

**B.81** Net public service pensions figures are reported on a National Accounts basis, which reflects the differences between the payments to pensioners paid out during the year and contributions received for the main unfunded public service pension schemes. Spending is expected to be slightly higher than forecast at Budget 2006. The higher spending in 2007-08 partly reflects the impact of higher than expected RPI inflation in 2006.

**B.82** National lottery figures reflect the latest view on the timing of drawdown by the distributing bodies. The estimates are broadly unchanged from Budget 2006.

**B.83** The decrease in other departmental expenditure largely reflects a change to the budgeting regime, whereby grants to local authorities that were previously classified as financial transactions have now been removed from departments' budgets. This change is offset by a change to accounting adjustments.

**B.84** Net expenditure transfers to EU institutions include the GNI based contribution less the UK abatement. These transfers are expected to be lower in 2006-07 and 2007-08 than expected at Budget 2006. This is explained by downward revisions to the size of the 2006 and 2007 EC budgets, which reduce the contributions required from Member States. The latest EC Budget for 2006 also increases projections of revenue from other sources in 2006, further reducing the contributions required from Member States.

**B.85** Changes to forecasts for local authority self-financed expenditure (LASFE) reflect recent outturns and an improved understanding of the trends in data, reflecting work done with the ONS and the Department for Communities and Local Government (DCLG) to improve data quality. The reclassification of net capital expenditure on housing by the Housing Revenue Account (HRA) to the public corporations (PC) sector has also been a contributing factor. The council tax projections used to derive the LASFE projections for 2007-08 onwards are based on stylised assumptions and are not government forecasts. Forward projections are simply an arithmetic average of national council tax increases for the last three years.

**B.86** Estimates for central government debt interest payments in 2006-07 are greater than at Budget 2006, mainly due to higher RPI inflation affecting the uplift on index-linked gilts and National Savings and Investments savings certificates. Higher than expected interest rates have, to a lesser extent, also increased debt interest payments in 2006-07. Payments in 2007-08 have increased by less than in 2006-07 because the inflationary impact is lower.

**B.87** Public corporations' own financed capital expenditure forecasts have been revised in line with public corporations' latest spending plans. They take account of the effect of the reclassification of HRA capital expenditure to the PC sector, as referred to in paragraph B85. The increase in 2006-07 also reflects the write-off of Nigerian debt agreed with the Paris Club. This is scored as a capital grant by the Export Credits Guarantee Department (ECGD) in the National Accounts at the time the write-off was implemented. It is also scored this way in OECD's Official Development Assistance (ODA) figures, but this does not reflect the underlying trend path of ODA, or the fact that the benefit to Nigeria is spread over several years. The Government is therefore considering with international colleagues whether there is a more appropriate way to report Nigerian debt relief over several years in the ODA figures to enable more accurate monitoring of trends.

**Table B18: Departmental Expenditure Limits - resource and capital budgets**

	£ billion		
	Outturn 2005-06	Estimate 2006-07	Projection 2007-08
<i>Resource Budget</i>			
Education and Skills	24.7	53.3	56.8
Health	76.5	82.0	89.1
of which : NHS	74.3	80.0	87.1
Transport	6.3	6.9	6.7
Department for Communities and Local Government	3.4	3.6	4.3
Local Government	46.2	22.5	22.8
Home Office	12.7	13.1	13.5
Departments for Constitutional Affairs	3.9	4.0	4.0
Law Officers' Departments	0.6	0.7	0.7
Defence	32.3	33.8	32.7
Foreign and Commonwealth Office	1.9	1.9	1.7
International Development	4.5	5.0	5.3
Trade and Industry	5.1	5.8	6.0
Environment, Food and Rural Affairs	2.7	2.9	3.0
Culture, Media and Sport	1.5	1.5	1.6
Work and Pensions	7.8	7.8	7.7
Scotland <sup>1</sup>	20.8	22.3	23.5
Wales <sup>1</sup>	10.9	11.8	12.4
Northern Ireland Executive <sup>1</sup>	6.7	7.2	7.6
Northern Ireland Office	1.2	1.2	1.1
Chancellor's Departments	5.0	5.1	5.0
Cabinet Office	2.2	2.3	2.3
Invest to Save Budget	0.0	0.0	0.0
Reserve	0.0	0.5	2.1
Unallocated special reserve <sup>2</sup>	0.0	0.0	0.0
Allowance for shortfall	0.0	-0.9	0.0
<b>Total Resource Budget DEL</b>	<b>277.1</b>	<b>294.5</b>	<b>309.9</b>
<i>Capital Budget</i>			
Education and Skills	5.7	6.3	7.0
Health	2.2	5.3	6.3
of which : NHS	2.1	5.2	6.2
Transport	5.8	7.4	6.7
Department for Communities and Local Government	5.7	5.8	6.2
Local Government	0.3	0.3	0.2
Home Office	1.0	1.3	1.3
Departments for Constitutional Affairs	0.1	0.2	0.1
Law Officers' Departments	0.0	0.0	0.0
Defence	6.8	7.4	7.6
Foreign and Commonwealth Office	0.1	0.2	0.1
International Development	0.0	0.0	0.0
Trade and Industry	1.4	1.3	1.1
Environment, Food and Rural Affairs	0.9	0.9	0.9
Culture, Media and Sport	0.1	0.4	0.2
Work and Pensions	0.4	0.2	0.1
Scotland <sup>1</sup>	2.3	3.0	3.1
Wales <sup>1</sup>	1.2	1.4	1.6
Northern Ireland Executive <sup>1</sup>	0.9	0.9	1.0
Northern Ireland Office	0.1	0.1	0.1
Chancellor's Departments	0.4	0.3	0.3
Cabinet Office	0.3	0.4	0.3
Invest to Save Budget	0.0	0.0	0.0
Reserve	0.0	0.3	1.3
Allowance for shortfall	0.0	-0.6	0.0
<b>Total Capital Budget DEL</b>	<b>35.8</b>	<b>42.6</b>	<b>45.7</b>
<b>Depreciation</b>	<b>10.3</b>	<b>11.8</b>	<b>11.5</b>
<b>Total Departmental Expenditure Limits</b>	<b>302.6</b>	<b>325.3</b>	<b>344.2</b>
Total education spending	67.7	70.6	75.8

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

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

**B.88** The accounting adjustments reflect the latest adjustments needed to reconcile the budgeting aggregates DEL and AME with the National Accounts definition of TME, removing items that score in DEL or AME but not in TME, and adding in items included in TME but not in DEL or AME. Changes in accounting adjustments reflect classification changes made to TME by the ONS, and budgeting regime changes or changes in the presentation of the AME components, as described above. Recent classification changes that have increased the accounting adjustments include adjustments in respect of renewable obligation certificates and passport fees. Adjustments that have reduced the accounting adjustments include the reclassification of contributions to international development organisations, which are elements of DEL that are now treated as financial transactions, not included in TME, and an adjustment to remove capital expenditure included in the Department for Transport's capital DEL in respect of capital grants to London and Continental Railways (LCR), which since the reclassification of LCR to the public corporation sector of National Accounts, are intra-public sector transactions and so consolidate out in TME. The latter particularly reduces the accounting adjustments in 2005-06 and 2006-07, as shown in the public corporations component of the accounting adjustments in Table B19.

**Table B19: Accounting adjustments**

	£ billion		
	Outturn	Estimate	Projection
	2005-06	2006-07	2007-08
Central government programmes	1.0	1.1	1.2
VAT refunds	10.2	11.0	12.6
Central government non-trading capital consumption	6.1	6.6	7.1
Non-cash items in resource budgets and not in TME	-8.7	-8.9	-9.6
Expenditure financed by revenue receipts	1.3	0.6	0.5
Local authorities	4.6	4.2	5.0
General government consolidation	-6.3	-6.3	-6.5
Public corporations	-0.9	-0.5	0.4
Financial transactions	0.2	0.4	0.5
Other accounting adjustments	-0.8	-0.9	-0.5
<b>Total accounting adjustments</b>	<b>6.8</b>	<b>7.2</b>	<b>10.6</b>

**B.89** Table B20 shows public sector capital expenditure from 2005-06 to 2007-08.

**Table B20: Public sector capital expenditure**

	£ billion		
	Outturn	Estimate	Projection
	2005-06	2006-07	2007-08
Capital Budget DEL	35.8	42.6	45.7
Locally-financed expenditure	1.2	1.5	1.0
National Lottery	1.0	1.0	0.9
Public corporations' own-financed capital expenditure	6.1	7.0	4.3
Other capital spending in AME	0.6	-0.3	-0.2
AME margin	0.0	0.0	0.0
Accounting adjustments	-5.8	-5.2	-3.2
<b>Public sector gross investment<sup>1</sup></b>	<b>38.9</b>	<b>46.5</b>	<b>48.4</b>
Less depreciation	16.5	17.6	18.6
<b>Public sector net investment</b>	<b>22.4</b>	<b>28.9</b>	<b>29.8</b>
Proceeds from the sale of fixed assets <sup>2</sup>	5.9	5.6	5.6

<sup>1</sup> This and previous lines are all net of sales of fixed assets.

<sup>2</sup> Projections of total receipts from the sale of fixed assets by public sector.

**B.90** Table B21 shows estimated receipts from loans and sales of assets from 2005-06 to 2007-08. Since Budget 2006, the ONS has reclassified local authority HRA assets to the public corporation sub-sector. Receipts from these assets continue to be included in this table in order to show a consistent measure over time of sales of public sector fixed assets. The figures for sales of financial assets include proceeds in the final quarter of 2005-06 of £0.3 billion from the sale of part of the Government's shareholding in QinetiQ (formerly the Defence Evaluation and Research Agency). The table only covers general government and so does not include the sale by British Nuclear Fuels Limited (BNFL) of its Westinghouse subsidiary, which was finalised in October 2006. The proceeds from this sale are included in the public corporation column of Table B25. It is anticipated that there will be a public sector neutral transfer of the proceeds to central government. A £0.5 billion BNFL debenture has already been repaid to government from the proceeds.

**Table B21: Loans and sales of assets**

	£ billion		
	Outturn 2005-06	Estimate 2006-07	Projection 2007-08
<b>Sales of fixed assets</b>			
Central government	1.7	1.4	1.4
Local authorities	1.8	1.8	1.8
Housing Revenue Account <sup>1</sup>	2.4	2.4	2.4
<b>Total sales of fixed assets</b>	<b>5.9</b>	<b>5.6</b>	<b>5.6</b>
<b>Total loans and sales of financial assets</b>	<b>-2.7</b>	<b>-2.9</b>	<b>-3.3</b>
<b>Total loans and sales of assets</b>	<b>3.2</b>	<b>2.7</b>	<b>2.3</b>

<sup>1</sup> Capital transactions by local authorities' Housing Revenue Accounts are no longer statistically classified to the local authority subsector and so are shown separately.

## PRIVATE FINANCE INITIATIVE

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

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

**B.93** Table B22 shows a breakdown by department of the estimated capital investment in public services resulting from signed PFI contracts. Table B23 shows the estimated total capital value of contracts that are at preferred bidder stage and are expected to reach financial

close within the next three years. Under PFI, the public sector contracts for services, including the availability and management of facilities, and not assets. Capital investment is only one of the activities undertaken by the private sector in order to supply these services. The figures in Tables B22 and B23 report the capital value of projects in order to show investment on a basis comparable with conventional capital procurement.

**Table B22: Departmental estimate of capital spending by the private sector (signed deals)<sup>1,2,3</sup>**

	£ million	
	Projections	
	2006-07	2007-08
Education and Skills <sup>4</sup>	650	295
Health	1,022	1,005
Transport <sup>5</sup>	1,428	1,097
Department for Communities and Local Government	80	80
Home Office	23	20
Constitutional Affairs	15	2
Defence	556	643
Foreign and Commonwealth Office	5	5
Trade and Industry	2	5
Environment, Food and Rural Affairs	65	63
Culture, Media and Sport	38	12
Work and Pensions	55	55
Scotland	545	472
Wales	0	0
Northern Ireland Executive	86	116
Chancellor's Departments	2	2
<b>Total</b>	<b>4,570</b>	<b>3,869</b>

<sup>1</sup> Investment in assets scored on the public sector balance sheet also score as public sector net investment.

<sup>2</sup> PFI activity in local authority projects is included under the sponsoring central government department.

<sup>3</sup> Figures do not include PFI projects undertaken by public corporations.

<sup>4</sup> Excludes private finance activity in educational institutions classified to the private sector.

<sup>5</sup> Includes estimates of the capital expenditure for the London Underground Limited Public Private Partnership (LUL PPP) PFI contracts in the years that investments are expected to take place.

**Table B23: Estimated aggregated capital value of projects at preferred bidder stage<sup>1,2</sup>**

	£ million	
	Projections	
	2006-07	2007-08
Education and Skills	270	0
Health	1,014	1,290
Transport	20	48
Department for Communities and Local Government	292	0
Defence	2,850	0
Environment, Food and Rural Affairs	609	0
Culture, Media and Sport	63	0
Scotland	1,038	0
Wales	32	29
Northern Ireland Executive	122	44
<b>Total</b>	<b>6,360</b>	<b>1,411</b>

<sup>1</sup> Figures based on Departmental returns.

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

**B.94** Table B24 shows a forecast of the estimated payments for services flowing from signed PFI projects. Actual expenditure will depend on the details of the payment mechanism for each contract. Payments may be lower than those estimated as a result of deductions that can be applied if the supplier fails to meet required performance standards. Variances may also occur as a result of agreed changes to the service requirements that are made during the course of the contract, or because of contractual arrangements that trigger compensation on termination. The fact that capital investment only represents one element of the overall contract means that the figures presented in this table should not be taken to be directly comparable with a public sector debt liability.

**Table B24: Estimated payments under PFI contracts - December 2006 (signed deals)<sup>1</sup>**

£ billion			
Projections			
2006-07	6.6	2019-20	5.6
2007-08	7.0	2020-21	5.7
2008-09	7.4	2021-22	5.4
2009-10	7.7	2022-23	5.3
2010-11	8.0	2023-24	5.3
2011-12	7.9	2024-25	5.3
2012-13	8.0	2025-26	5.2
2013-14	8.2	2026-27	4.9
2014-15	8.2	2027-28	4.7
2015-16	8.3	2028-29	4.3
2016-17	8.3	2029-30	4.0
2017-18	7.5	2030-31	3.7
2018-19	5.5	2031-32	3.4

<sup>1</sup> The figures between 2006-07 and 2017-18 include estimated payments for the LUL PPP PFI contract. These contracts contain periodic reviews every 7.5 years and therefore the service payments are not fixed after 2009-10.

## FINANCING REQUIREMENT

**B.95** Table B25 presents projections of the net cash requirement by sector, giving details of financial transactions that do not affect net borrowing (the change in the sector's net financial indebtedness) but do affect its financing requirement.

**Table B25: Public sector net cash requirement**

	£ billion							
	2006-07				2007-08			
	General government				General government			
	Central government	Local authorities	Public corporations	Public sector	Central government	Local authorities	Public corporations	Public sector
<b>Net borrowing</b>	<b>34.1</b>	<b>0.8</b>	<b>1.9</b>	<b>36.8</b>	<b>30.3</b>	<b>0.5</b>	<b>0.5</b>	<b>31.3</b>
<i>Financial transactions</i>								
Net lending to private sector and abroad	2.7	0.1	-2.3	0.5	3.1	0.1	0.0	3.2
Cash expenditure on company securities	0.1	0.0	-2.6	-2.5	0.1	0.0	0.0	0.1
Accounts receivable/payable	6.0	0.1	-0.1	6.1	2.5	0.2	0.0	2.7
Adjustment for interest on gilts	-1.3	0.0	0.0	-1.3	-4.0	0.0	0.0	-4.0
Miscellaneous financial transactions	-2.3	0.0	1.2	-1.1	-0.2	0.0	-0.6	-0.7
Own account net cash requirement	39.4	1.0	-1.9	38.5	31.8	0.8	0.0	32.6
Net lending within the public sector	1.8	-2.0	0.2	0.0	2.8	-2.0	-0.8	0.0
<b>Net cash requirement<sup>1</sup></b>	<b>41.2</b>	<b>-1.0</b>	<b>-1.7</b>	<b>38.5</b>	<b>34.7</b>	<b>-1.2</b>	<b>-0.9</b>	<b>32.6</b>

<sup>1</sup> Market and overseas borrowing for local government and public corporation sectors.

**B.96** Table B26 updates the financing arithmetic for 2006-07 in line with the updated fiscal forecasts. The central government net cash requirement (CGNCR) for 2006-07 is unchanged, at £41.2 billion, from the Budget 2006 forecast. However, the impact of other factors set out below reduces the net financing requirement for 2006-07 to £59.0 billion, a decrease of £5.5 billion from the revised forecast published on 24 April 2006 that reflected publication of outturn CGNCR for 2005-06.

**B.97** In order to meet the decrease in the financing requirement, the Debt Management Office's (DMO) remit has been revised as follows:

- forecast gross gilt issuance has decreased by £0.5 billion to £62.5 billion. The lower issuance will be met through a reduction in the 'unallocated' gilt issuance programme for the final quarter of 2006-07; and
- the stock of Treasury bills will be reduced by £3.5 billion instead of the increase of £1.5 billion announced on 24 April 2006.

**B.98** The latest financing arithmetic set out in Table B26 also takes account of:

- an increase in the forecast net contribution to financing of £2.2 billion in 2006-07 from National Savings & Investments relative to the forecast at the time of the Budget;
- proceeds of £3.8 billion from the disposal of the Nuclear Liabilities Investment Portfolio (NLIP) held by BNFL. Around half of the NLIP has already been liquidated, and the remainder, consisting of index-linked gilts, will be sold by the DMO into the secondary market by 31 March 2007;
- buy-backs of illiquid gilts in the secondary market by the DMO of £0.2 billion; and
- a reduction of £0.3 billion in the planned short-term financing adjustment for 2006-07.

**B.99** In Budget 2006, the DMO's remit included temporary changes intended to allow greater responsiveness in gilt issuance by the DMO during 2006-07 whilst retaining the Government's firm commitment to transparency and predictability in debt management policy. This remit consisted of: (i) a 'core' gilt issuance programme of £53.0 billion pre-allocated by maturity and type of gilt and which has remained unchanged since Budget; and (ii) an 'unallocated' gilt issuance programme of £10.0 billion to be allocated between maturity and type of gilt each quarter during 2006-07.

**B.100** £7.5 billion of the original 'unallocated' gilt issuance programme has already been allocated, comprising £2.5 billion in each of the first three quarters of 2006-07 (to long-dated conventional gilts and/or index-linked gilts). The remaining £2.0 billion of the revised programme of £9.5 billion will be allocated to long-dated conventional gilts in the fourth quarter of 2006-07.

**B.101** Details of changes to the financing arithmetic and a revised financing table for 2006-07 together with information on the progress of gilt sales so far this year against the DMO's financing remit can be found on the DMO's website at [www.dmo.gov.uk](http://www.dmo.gov.uk).

**Table B26: Financing requirement forecast**

	£ billion		
	2006-07		
	Original Remit March 2006	Revised Remit April 2006 <sup>1</sup>	Pre-Budget Report
<b>Central government net cash requirement</b>	<b>41.2</b>	<b>41.2</b>	<b>41.2</b>
Gilt redemptions	29.9	29.9	29.9
Restructuring nuclear liabilities <sup>2</sup>	0.0	0.0	-3.8
Financing for the Official Reserves	0.0	0.0	0.0
Buy-backs <sup>3</sup>	0.0	0.0	0.2
Planned short-term financing adjustment <sup>4</sup>	-3.1	-3.6	-3.3
<b>Gross Financing Requirement</b>	<b>68.0</b>	<b>67.5</b>	<b>64.2</b>
less			
Assumed net contribution from National Savings and Investments	3.0	3.0	5.2
<b>Net Financing Requirement</b>	<b>65.0</b>	<b>64.5</b>	<b>59.0</b>
<i>Financed by:</i>			
<b>1. Debt issuance by the Debt Management Office</b>			
(a) Treasury bills	2.0	1.5	-3.5
(b) Gilts	63.0	63.0	62.5
<b>2. Other planned changes in short-term debt<sup>5</sup></b>			
Change in Ways & Means	0.0	0.0	0.0
<b>3. Unanticipated changes in short-term cash position<sup>6</sup></b>			
	0.0	0.0	0.0
<b>Total financing</b>	<b>65.0</b>	<b>64.5</b>	<b>59.0</b>
<b>Short-term debt levels at end of financial year</b>			
Treasury bill stock in market hands	21.1	20.6	15.6
Ways & Means	13.4	13.4	13.4
DMO net cash position <sup>7</sup>	0.2	0.2	0.5

<sup>1</sup> The financing arithmetic in Budget 2006 was revised on 24 April 2006 to reflect outturn data for 2005-06.

<sup>2</sup> Proceeds from the disposal of financial assets in the Nuclear Liabilities Investment Portfolio (NLIP) held by British Nuclear Fuels Limited. Around half of the NLIP has already been liquidated, and the remainder, consisting of index-linked gilts, will be sold by the DMO into the secondary market by 31 March 2007.

<sup>3</sup> Purchases of "rump" gilts which are older, small gilts, declared as such by the DMO and in which Gilt-edged Market Makers (GEMMs) are not required to make two-way markets. The Government will not sell further amounts of such gilts to the market but the DMO is prepared, when asked by a GEMM, to make a price to purchase such gilts.

<sup>4</sup> To accommodate changes to the current year's financing requirement resulting from: (i) publication of the previous year's outturn CGNCR; (ii) an increase in the DMO's cash position at the Bank of England; and / or (iii) carry over of unanticipated changes to the cash position from the previous year.

<sup>5</sup> Total planned changes to short-term debt are the sum of: (i) the planned short-term financing adjustment; (ii) Treasury bill sales; and (iii) changes to the level of the Ways & Means advance.

<sup>6</sup> A negative (positive) number indicates an addition to (reduction in) the financing requirement for the following financial year.

<sup>7</sup> There is an increase in the DMO's net cash position at the Bank of England of £0.3 billion (reflecting a move from an end-day target balance of £0.2 billion prior to the implementation of the Bank of England's money market reforms to an average daily target balance of £0.5 billion).

**B.102** Table B27 below sets out the split of gilt issuance between maturity and type of gilt.

**Table B27: Gilt issuance split 2006-07**

	£ billion						
	Allocation of supplementary gilt issuance				Updated financing programme		
		Quarter 1	Quarter 2	Quarter 3	Quarter 4	2006-07	
<b>Planned gilt sales</b>		<b>62.5</b>					
<b>Pre-allocated gilts issuance</b>		<b>53.0</b>					
<i>Of which minimum:</i>							
Conventional	Short	10.0					10.0
	Medium	10.0					10.0
	Long	17.0	2.5	1.3	2.5	2.0	25.3
Index-linked		16.0		1.3			17.3
<b>Total allocated gilt issuance<sup>1</sup></b>		<b>53.0</b>	<b>2.5</b>	<b>2.5</b>	<b>2.5</b>	<b>2.0</b>	<b>62.5</b>

<sup>1</sup> Totals may not sum due to rounding.

## CASH MANAGEMENT PERFORMANCE

**B.103** The Government's cash management objective is to ensure that sufficient funds are always available to meet any net daily central government cash shortfall and, on any day when there is a net cash surplus, to ensure this is used to best advantage for the Exchequer. The Treasury and the DMO work together to achieve this.

**B.104** The role of the Treasury in this regard is to forecast the daily net flows into or out of the National Loans Fund (NLF) and provide the DMO with timely and accurate forecasts of the expected net cash position over time. The DMO's role is to manage by funding and placing as appropriate the net cash positions, primarily by carrying out market operations in light of the forecast. Its objective is to minimise the costs of cash management while operating within a risk appetite approved by Ministers.

**B.105** This risk appetite defines objectively the bounds of appropriate activity in accordance with the Government's approach to cash management as cost minimising rather than profit maximising. The DMO also seeks to avoid actions or arrangements that would undermine the efficient functioning of the sterling money markets, or conflict with the operational requirements of the Bank of England for monetary policy implementation. The combination of the Treasury cash flow forecasts and the DMO market operations characterises the active approach to Exchequer cash management.

**B.106** The Treasury and the DMO jointly reviewed the cash management function in 2004-05.<sup>1</sup> Implementation of the review recommendations began in June 2005 with the development of a quantified internal performance measure to capture the value added from active cash management. No conceptual problems with this quantitative approach, which captures performance against a neutral passive strategy, have been encountered so far.<sup>2</sup> However a quantitative indicator should not be looked at in isolation, since active cash management performance must be evaluated against a series of key performance indicators that together reflect the principles and objectives of the Government. These objectives are:

- the DMO must supply sufficient cash each day to enable the Government to meet its payment obligations. This is fundamental and unconditional;
- cash management operations and arrangements should be conducted in a manner that does not interfere with monetary policy operations;
- cash management operations and arrangements should be conducted without impeding the efficient working of the sterling money markets;
- cash should be raised, or surplus cash placed, as cost effectively as possible subject to policy objectives and constraints;
- the DMO should maintain a system in which costs and risks are transparent, measured and monitored, and the performance of government cash management assessed. The DMO maintains an ethos of cost minimisation rather than profit maximisation; and

<sup>1</sup> The findings and recommendations of this review and the Government's preference for risk are set out in Chapter 5 of the DMO's Annual Review 2004-05, available on the DMO's website [www.dmo.gov.uk/gilts/public/annual/gar0405.pdf](http://www.dmo.gov.uk/gilts/public/annual/gar0405.pdf).

<sup>2</sup> As a precursor to formal adoption of the quantitative approach, a further Cash Management Project was undertaken in October 2005, overseen by a joint HMT and DMO steering group. This was tasked with reviewing the implementation of the earlier review recommendations; ensuring that the new cash management framework continued to support HMT objectives; and with strengthening HMT oversight of the cash management function and placing it on a structured basis. The Project report concluded that the quantitative framework and risk limits proposed in the original Cash Management Review remained valid.

- DMO should establish a credible reputation in the market that leads to both lower costs in the long term and a system that is sustainable.

**B.107** A series of agreed key performance indicators and controls are used to monitor and assess overall performance in meeting the Government cash management objectives. Formal reporting and publication of the performance of active cash management against the key performance indicators will begin with the 2007-08 outturn, and will be considered for the 2006-07 outturn.

## ANALYSIS BY SUB-SECTOR AND ECONOMIC ACTIVITY

**B.108** Table B28 shows a breakdown of general government (GG) transactions by economic category for 2005-06 to 2007-08. Table B29 shows a more detailed breakdown for public sector transactions by sub-sector and economic category. The latest data published by the ONS for 2005-06 reflect imputed transactions in respect of the restructuring of nuclear liabilities and changes to the classification of capital expenditure from the local authorities' Housing Revenue Accounts. These changes have led to significant switches between different parts of the public sector.

**B.109** Liabilities for nuclear decommissioning were transferred from BNFL to the Nuclear Decommissioning Authority (NDA). The NDA took over the tangible fixed assets (reactors etc.) that had a negative value of £15 billion. For the Nuclear Liabilities Investment Portfolio (NLIP) transfer, a capital grant was imputed from BNFL in the PC sub-sector to the Secretary of State for Trade and Industry (in the CG sub-sector) to enable the Secretary of State to "buy" the NLIP. This imputed purchase, though, is a financial transaction, and so does not offset the imputed grant within either CG or GG net borrowing. The transfer of the tangible assets is reflected in National Accounts by imputing a negative capital grant from BNFL to the NDA to enable the NDA to "buy" the reactors. The imputed purchase is negative fixed capital formation, and so the imputed transactions net off within net investment and net borrowing for all sub-sectors. As the reactors have a large negative value, the imputed transaction makes CG fixed capital formation negative.

**B.110** The reclassification of the investment transactions of local authorities' HRA from the local authority to the PC sub-sector has affected the growth rate of GG investment because HRA investment was negative in 2004 and positive in 2005. Its reclassification thus reduced GG investment growth in 2005 with an offsetting positive impact on PC investment growth. This revision largely explains why the latest National Accounts data show that GG investment fell 1<sup>1</sup>/<sub>4</sub> per cent in 2005, compared with growth of 18<sup>1</sup>/<sub>2</sub> per cent reported at the time of Budget 2006, as referred to in Annex A. Government investment is expected to grow strongly in 2006 and 2007, consistent with the Government's aim to deliver world-class public services through sustained investment and far-reaching reform.

**Table B28: General government transactions by economic category**

	£ billion		
	Outturn 2005-06	Estimate 2006-07	Projection 2007-08
<b>Current receipts</b>			
Taxes on income and wealth	180.3	197.8	213.2
Taxes on production and imports	159.6	167.8	178.2
Other current taxes	28.7	30.1	31.8
Taxes on capital	3.3	3.6	4.1
Compulsory social contributions	85.4	89.9	95.5
Gross operating surplus	12.1	13.1	14.0
Rent and other current transfers	2.1	2.1	2.1
Interest and dividends from private sector and abroad	4.5	4.1	5.5
Interest and dividends from public sector	2.5	4.8	5.3
<b>Total current receipts</b>	<b>478.3</b>	<b>513.3</b>	<b>549.6</b>
<b>Current expenditure</b>			
Current expenditure on goods and services	274.6	289.5	307.5
Subsidies	6.8	7.4	7.4
Net social benefits	143.6	149.6	156.5
Net current grants abroad	-0.5	0.5	-0.2
Other current grants	32.7	32.8	36.2
Interest and dividends paid	26.2	27.8	28.8
AME margin	0.0	0.0	0.0
<b>Total current expenditure</b>	<b>483.5</b>	<b>507.7</b>	<b>536.2</b>
Depreciation	12.1	13.1	14.0
<b>Surplus on current budget</b>	<b>-17.2</b>	<b>-7.5</b>	<b>-0.5</b>
<b>Capital expenditure</b>			
Gross domestic fixed capital formation	7.1	27.8	31.4
Less depreciation	-12.1	-13.1	-14.0
Increase in inventories	0.0	0.1	0.1
Capital grants (net) within public sector	13.2	1.4	0.4
Capital grants to private sector	11.4	12.6	13.8
Capital grants from private sector	-1.5	-1.5	-1.5
AME margin	0.0	0.0	0.0
<b>Net investment</b>	<b>18.0</b>	<b>27.4</b>	<b>30.2</b>
<b>Net borrowing<sup>1</sup></b>	<b>35.2</b>	<b>34.9</b>	<b>30.7</b>
<i>of which:</i>			
Central government net borrowing	32.2	34.1	30.2
Local authority net borrowing	3.1	0.8	0.5
<b>Gross debt (Maastricht basis)</b>			
Central government	469.0	511.0	549.9
Local government	60.1	59.1	57.8

<sup>1</sup> Although this is based on the ESA95 definition of general government net borrowing (GGNB), the projections are identical to GGNB calculated on a Maastricht definition.

**Table B29: Public sector transactions by sub-sector and economic category**

	£ billion			
	2005-06			
	General government		Public corporations	Public sector
Central government	Local authorities			
<b>Current receipts</b>				
Taxes on income and wealth	180.3	0.0	-0.2	180.1
Taxes on production and imports	159.3	0.2	0.0	159.6
Other current taxes	8.1	20.5	0.0	28.7
Taxes on capital	3.3	0.0	0.0	3.3
Compulsory social contributions	85.4	0.0	0.0	85.4
Gross operating surplus	6.1	6.0	7.9	20.0
Rent and other current transfers	2.0	0.0	0.0	2.1
Interest and dividends from private sector and abroad	3.4	1.0	1.7	6.2
Interest and dividends from public sector	3.8	-1.3	-2.5	0.0
<b>Total current receipts</b>	<b>451.9</b>	<b>26.4</b>	<b>7.0</b>	<b>485.3</b>
<b>Current expenditure</b>				
Current expenditure on goods and services	166.3	108.4	0.0	274.6
Subsidies	5.0	1.7	0.0	6.8
Net social benefits	128.1	15.5	0.0	143.6
Net current grants abroad	-0.5	0.0	0.0	-0.5
Current grants (net) within public sector	102.1	-102.1	0.0	0.0
Other current grants	32.7	0.0	0.0	32.7
Interest and dividends paid	25.8	0.4	0.4	26.7
AME margin	0.0	0.0	0.0	0.0
<b>Total current expenditure</b>	<b>459.5</b>	<b>23.9</b>	<b>0.4</b>	<b>483.9</b>
Depreciation	6.1	6.0	4.4	16.5
<b>Surplus on current budget</b>	<b>-13.8</b>	<b>-3.5</b>	<b>2.1</b>	<b>-15.1</b>
<b>Capital expenditure</b>				
Gross domestic fixed capital formation	-6.2	13.2	22.0	29.0
Less depreciation	-6.1	-6.0	-4.4	-16.5
Increase in inventories	0.0	0.0	0.0	0.0
Capital grants (net) within public sector	21.3	-8.1	-13.2	0.0
Capital grants to private sector	9.8	1.6	0.1	11.5
Capital grants from private sector	-0.4	-1.1	0.0	-1.5
AME margin	0.0	0.0	0.0	0.0
<b>Net investment</b>	<b>18.4</b>	<b>-0.4</b>	<b>4.4</b>	<b>22.4</b>
<b>Net borrowing</b>	<b>32.2</b>	<b>3.1</b>	<b>2.3</b>	<b>37.5</b>

**Table B29: Public sector transactions by sub-sector and economic category**

	£ billion			
	2006-07			
	General government		Public corporations	Public sector
Central government	Local authorities			
<b>Current receipts</b>				
Taxes on income and wealth	197.8	0.0	-0.2	197.5
Taxes on production and imports	167.6	0.2	0.0	167.8
Other current taxes	8.5	21.7	0.0	30.1
Taxes on capital	3.6	0.0	0.0	3.6
Compulsory social contributions	89.9	0.0	0.0	89.9
Gross operating surplus	6.6	6.5	8.5	21.6
Rent and other current transfers	2.1	0.0	0.0	2.1
Interest and dividends from private sector and abroad	3.5	0.6	1.1	5.3
Interest and dividends from public sector	3.5	1.3	-4.8	0.0
<b>Total current receipts</b>	<b>482.9</b>	<b>30.3</b>	<b>4.6</b>	<b>517.9</b>
<b>Current expenditure</b>				
Current expenditure on goods and services	175.7	113.8	0.0	289.5
Subsidies	5.5	1.9	0.0	7.4
Net social benefits	133.2	16.4	0.0	149.6
Net current grants abroad	0.5	0.0	0.0	0.5
Current grants (net) within public sector	107.2	-107.2	0.0	0.0
Other current grants	32.8	0.0	0.0	32.8
Interest and dividends paid	27.4	0.4	0.4	28.3
AME margin	0.0	0.0	0.0	0.0
<b>Total current expenditure</b>	<b>482.4</b>	<b>25.3</b>	<b>0.4</b>	<b>508.1</b>
Depreciation	6.6	6.5	4.5	17.6
<b>Surplus on current budget</b>	<b>-6.0</b>	<b>-1.5</b>	<b>-0.4</b>	<b>-7.9</b>
<b>Capital expenditure</b>				
Gross domestic fixed capital formation	13.0	14.8	5.0	32.8
Less depreciation	-6.6	-6.5	-4.5	-17.6
Increase in inventories	0.1	0.0	0.0	0.1
Capital grants (net) within public sector	11.0	-9.6	-1.4	0.0
Capital grants to private sector	10.9	1.8	2.4	15.1
Capital grants from private sector	-0.3	-1.2	0.0	-1.5
AME margin	0.0	0.0	0.0	0.0
<b>Net investment</b>	<b>28.1</b>	<b>-0.8</b>	<b>1.5</b>	<b>28.9</b>
<b>Net borrowing</b>	<b>34.1</b>	<b>0.8</b>	<b>1.9</b>	<b>36.8</b>

**Table B29: Public sector transactions by sub-sector and economic category**

	£ billion			
	2007-08			
	General government		Public corporations	Public sector
Central government	Local authorities			
<b>Current receipts</b>				
Taxes on income and wealth	213.2	0.0	-0.2	213.0
Taxes on production and imports	178.0	0.2	0.0	178.2
Other current taxes	9.0	22.9	0.0	31.8
Taxes on capital	4.1	0.0	0.0	4.1
Compulsory social contributions	95.5	0.0	0.0	95.5
Gross operating surplus	7.1	6.9	9.0	23.0
Rent and other current transfers	2.1	0.0	0.0	2.1
Interest and dividends from private sector and abroad	4.0	1.4	0.7	6.1
Interest and dividends from public sector	3.5	1.8	-5.3	0.0
<b>Total current receipts</b>	<b>516.3</b>	<b>33.3</b>	<b>4.1</b>	<b>553.8</b>
<b>Current expenditure</b>				
Current expenditure on goods and services	185.7	121.8	0.0	307.5
Subsidies	5.4	2.0	0.0	7.4
Net social benefits	138.9	17.5	0.0	156.5
Net current grants abroad	-0.2	0.0	0.0	-0.2
Current grants (net) within public sector	114.2	-114.2	0.0	0.0
Other current grants	36.2	0.0	0.0	36.2
Interest and dividends paid	28.3	0.4	0.4	29.2
AME margin	0.0	0.0	0.0	0.0
<b>Total current expenditure</b>	<b>508.5</b>	<b>27.7</b>	<b>0.4</b>	<b>536.6</b>
Depreciation	7.1	6.9	4.6	18.6
<b>Surplus on current budget</b>	<b>0.8</b>	<b>-1.3</b>	<b>-0.9</b>	<b>-1.5</b>
<b>Capital expenditure</b>				
Gross domestic fixed capital formation	15.0	16.3	4.6	36.0
Less depreciation	-7.1	-6.9	-4.6	-18.6
Increase in inventories	0.1	0.0	0.0	0.1
Capital grants (net) within public sector	11.3	-10.8	-0.4	0.0
Capital grants to private sector	11.9	1.9	0.1	13.9
Capital grants from private sector	-0.2	-1.3	0.0	-1.5
AME margin	0.0	0.0	0.0	0.0
<b>Net investment</b>	<b>31.0</b>	<b>-0.8</b>	<b>-0.4</b>	<b>29.8</b>
<b>Net borrowing</b>	<b>30.3</b>	<b>0.5</b>	<b>0.5</b>	<b>31.3</b>

## HISTORICAL SERIES

**Table B30: Historical series of public sector balances, receipts and debt**

	Per cent of GDP								
	Public sector current budget	Cyclically adjusted surplus on current budget	Public sector net borrowing	Cyclically adjusted public sector net borrowing	Public sector net cash requirement	Net taxes and national insurance contributions	Public sector current receipts	Public sector net debt <sup>1</sup>	Public sector net worth <sup>2</sup>
1970-71	6.9		-0.6		1.2	36.5	43.5		
1971-72	4.2		1.1		1.4	35.2	41.6		
1972-73	2.0	2.5	2.8	2.3	3.6	32.8	39.2		
1973-74	0.4	-0.8	4.9	6.1	5.8	32.1	39.8		
1974-75	-0.9	-2.5	6.6	8.1	9.0	34.8	42.5	52.1	
1975-76	-1.4	-1.7	7.0	7.3	9.2	35.5	43.1	53.8	
1976-77	-1.1	-0.6	5.5	5.1	6.4	35.4	43.5	52.3	
1977-78	-1.3	-1.2	4.3	4.2	3.7	34.3	41.7	49.0	
1978-79	-2.5	-2.4	5.1	4.9	5.2	33.3	40.4	47.1	
1979-80	-1.8	-1.7	4.1	4.0	4.7	33.7	40.9	43.9	
1980-81	-3.0	-1.5	4.9	3.4	5.2	35.8	42.7	46.0	
1981-82	-1.3	2.5	2.3	-1.5	3.3	38.4	46.1	46.2	
1982-83	-1.4	2.9	3.0	-1.3	3.2	38.6	45.8	44.8	
1983-84	-2.0	1.8	3.8	0.1	3.2	38.1	44.7	45.1	
1984-85	-2.1	0.9	3.7	0.7	3.1	38.8	44.6	45.3	
1985-86	-1.2	0.5	2.4	0.7	1.6	38.0	43.5	43.5	
1986-87	-1.4	-1.2	2.1	1.9	0.9	37.7	42.4	41.0	
1987-88	-0.4	-1.7	1.0	2.3	-0.7	37.5	41.4	36.8	73.4
1988-89	1.7	-0.9	-1.3	1.3	-3.0	36.8	41.0	30.5	78.9
1989-90	1.5	-1.4	-0.2	2.6	-1.3	36.1	40.2	27.7	70.7
1990-91	0.3	-1.2	1.0	2.6	-0.1	35.8	39.2	26.2	60.2
1991-92	-2.0	-1.5	3.8	3.4	2.3	34.7	38.8	27.4	52.8
1992-93	-5.7	-3.8	7.6	5.7	5.9	33.5	36.9	32.0	39.9
1993-94	-6.4	-4.2	7.8	5.6	7.1	32.6	36.0	37.3	29.2
1994-95	-4.8	-3.4	6.3	4.9	5.3	33.8	37.1	40.8	28.3
1995-96	-3.4	-2.5	4.7	3.9	4.3	34.5	37.8	42.7	20.9
1996-97	-2.8	-2.3	3.5	3.0	2.9	34.8	37.3	43.6	17.0
1997-98	-0.1	0.0	0.8	0.7	0.2	35.9	38.4	41.6	14.3
1998-99	1.2	1.1	-0.5	-0.3	-0.7	36.3	38.5	39.3	13.4
1999-00	2.3	2.0	-1.8	-1.5	-0.9	36.4	38.9	36.6	16.6
2000-01	2.5	1.9	-2.1	-1.5	-3.8	37.2	39.6	31.7	22.6
2001-02	1.0	0.9	0.1	0.3	0.4	36.6	38.6	30.6	29.4
2002-03	-1.1	-0.7	2.3	1.9	2.4	35.2	37.2	32.0	28.0
2003-04	-1.7	-1.3	3.0	2.7	3.5	35.2	37.4	33.2	28.3
2004-05	-1.6	-1.6	3.3	3.2	3.2	35.9	38.0	35.0	28.8
2005-06	-1.2	-1.0	3.0	2.8	3.2	36.9	39.2	36.4	27.0

<sup>1</sup> At end-March; GDP centred on end-March.

<sup>2</sup> At end-December; GDP centred on end-December.

**Table B3I: Historical series of government expenditure**

	£ billion (2005-06 prices)				Per cent of GDP			
	Public sector current expenditure	Public sector net investment	Public sector gross investment <sup>1</sup>	Total Managed Expenditure	Public sector current expenditure	Public sector net investment	Public sector gross investment <sup>1</sup>	Total Managed Expenditure
1970-71	180.5	34.4	55.2	235.7	32.8	6.3	10.0	42.8
1971-72	189.4	30.0	51.8	241.1	33.5	5.3	9.2	42.7
1972-73	197.8	28.9	51.7	249.5	33.4	4.9	8.7	42.1
1973-74	216.6	32.4	57.8	274.4	35.3	5.3	9.4	44.7
1974-75	239.8	34.9	61.7	301.5	39.0	5.7	10.0	49.0
1975-76	244.9	34.2	61.2	306.0	40.1	5.6	10.0	50.1
1976-77	251.7	28.1	56.0	307.7	40.1	4.5	8.9	49.0
1977-78	248.2	19.2	47.4	295.5	38.6	3.0	7.4	46.0
1978-79	255.4	16.7	45.5	300.9	38.6	2.5	6.9	45.5
1979-80	261.7	15.6	44.8	306.5	38.5	2.3	6.6	45.1
1980-81	269.5	12.5	42.2	311.7	41.1	1.9	6.4	47.5
1981-82	281.5	6.7	36.2	317.7	42.9	1.0	5.5	48.4
1982-83	287.7	10.5	39.2	327.0	42.9	1.6	5.9	48.8
1983-84	296.7	12.9	41.4	338.1	42.6	1.9	5.9	48.5
1984-85	304.7	11.3	38.5	343.2	42.9	1.6	5.4	48.3
1985-86	305.2	8.8	33.7	339.0	41.3	1.2	4.6	45.9
1986-87	310.1	5.3	30.4	340.5	40.5	0.7	4.0	44.4
1987-88	313.6	4.8	28.4	342.0	38.9	0.6	3.5	42.4
1988-89	306.0	2.9	26.5	332.5	36.5	0.3	3.2	39.7
1989-90	308.0	10.8	34.1	342.1	36.0	1.3	4.0	40.0
1990-91	310.1	11.7	33.0	343.1	36.4	1.4	3.9	40.3
1991-92	328.3	15.3	33.2	361.6	38.7	1.8	3.9	42.6
1992-93	344.4	15.9	33.4	377.8	40.5	1.9	3.9	44.5
1993-94	354.4	12.6	30.0	384.4	40.4	1.4	3.4	43.8
1994-95	365.6	13.0	30.3	395.8	40.0	1.4	3.3	43.3
1995-96	370.1	13.0	29.9	399.9	39.4	1.4	3.2	42.6
1996-97	370.0	6.7	22.2	392.2	38.5	0.7	2.3	40.8
1997-98	368.4	6.3	21.1	389.6	37.0	0.6	2.1	39.2
1998-99	368.8	7.7	21.9	390.6	36.0	0.7	2.1	38.1
1999-00	375.0	5.6	19.9	395.0	35.3	0.5	1.9	37.1
2000-01	393.2	4.4	18.9	412.2	35.8	0.4	1.7	37.5
2001-02	406.4	12.5	27.1	433.5	36.3	1.1	2.4	38.7
2002-03	424.6	14.0	29.2	453.8	37.0	1.2	2.5	39.5
2003-04	446.5	15.9	31.2	477.8	37.8	1.4	2.6	40.4
2004-05	464.3	20.2	36.0	500.3	38.4	1.7	3.0	41.3
2005-06	483.9	22.4	38.9	522.8	39.1	1.8	3.1	42.2

<sup>1</sup> Net of sales of fixed assets.