

Ministry of Defence Annual Report and Accounts 2010-11

For the year ended 31 March 2011

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House of Commons by Command of Her Majesty

Annual Report and Accounts presented to
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Preface

i. The Ministry of Defence's (MOD) Annual Report and Accounts is an overview of UK Defence and how the MOD has used the resources authorised by Parliament from April 2010 to March 2011.

Part One: Annual Report

ii. The principal activity of the Department is to deliver security for the people of the United Kingdom and the Overseas Territories by defending them, including against terrorism, and to act as a force for good by strengthening international peace and stability. The *MOD Business Plan 2011-15* was published in November 2010 and lists the Department's priorities as:

- to succeed in Afghanistan;
- to continue to fulfil our standing commitments;
- to succeed in other operations we are required to undertake;
- to promote defence exports consistent with export control criteria;
- to implement the Strategic Defence and Security Review (SDSR);
- to deliver the Defence Reform Unit's review; and
- to deliver Defence in the most effective, efficient and sustainable way.

The MOD Business Plan splits this list into 'Major Responsibilities' and 'Structural Reform Priorities'. The Structural Reform Priorities also includes a separate heading on the Armed Forces Covenant, reflecting the importance that the Government places on our Service personnel. This report is structured around the seven priorities contained in the Business Plan, plus an additional chapter for the Covenant.

Further information on the MOD Business Plan is at:

<http://www.mod.uk/DefenceInternet/AboutDefence/CorporatePublications/BusinessPlans/ModBusinessPlans/management>

Further details of the SDSR, Defence Reform and Transparency are available at:

<http://www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/PolicyStrategyandPlanning/DefenceReform/> and <http://www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/Transparency/>

iii. The Defence Board uses the Defence Performance Framework to assess and manage Defence's performance and provide direction and guidance to the Department. The framework, which includes the reporting of performance against the actions articulated in the Structural Reform Plan within the MOD Business Plan, involves a quarterly performance and risk report that is focused on the Defence Board's strategic objectives, and an annual performance and risk report. This allows the Board to assess whether strategy needs to be adjusted and provides oversight of performance in individual areas. The performance section of this report is set out against the priorities articulated in the MOD Business Plan and informed by reporting generated by the Defence Performance Framework.

Part Two: Annual Accounts 2010-11

iv. The MOD prepares accounts for each financial year detailing the resources acquired, held, or disposed of during the year and the way in which it has used them. Accounts are prepared in accordance with directions issued by HM Treasury including the accounting instructions in the Government Financial Reporting Manual. The accounts are audited by the Comptroller and Auditor General who provides an opinion as to whether: the financial statements give a true and fair view and have been properly prepared; expenditure and income has been applied to the purposes intended by Parliament; and the financial transactions conform to the authorities which govern them.

Further Information

v. Further information on the MOD, including Ministerial responsibilities and our organisation and administration is set out in the Defence Framework document which is published on the MOD website at www.mod.uk/DefenceInternet/DefenceFor/Researchers/.

Part One – Annual Report

Foreword by Secretary of State for Defence

The first duty of Government is defence of the realm. The requirement to fight, and win, the wars of today is not optional but necessary to protect national security and meet the national interest. The current operations in Afghanistan and, more recently in Libya remain the priority for the Ministry of Defence (MOD).

2010-11 saw continued progress towards our objective of a stable and secure Afghanistan. We now have the right number of troops there with the right equipment. The Afghans are not yet able to secure their own territory without the presence of coalition troops but the training of the Afghan National Security Forces is progressing ahead of schedule.

Last financial year also saw the deployment of our Armed Forces in Libya alongside a wide international coalition to support UN Resolution 1973 that authorises the use of military force to protect civilians. We could not stand aside to witness the violence that Gaddafi was unleashing on those he had a duty to protect. Nor could we afford to see Libya again become a rogue state in Europe's neighbourhood. The Coalition of Nations is united in our shared determination to enforce UN resolutions, and will continue to protect the Libyan people for as long as it takes.

While the men and women of our Armed Forces fighting on the front-line get first call on MOD resources, we must also ensure that Defence is prepared for the challenges of protecting national security in the future.

This year saw the completion of the first Defence Review since 1998. The Strategic Defence and Security Review (SDSR) set the direction for a reshaping of our Armed Forces to tackle future and emerging threats. Future Force 2020 must be based on a sound and sustainable financial base. So we are now bringing Defence policy, plans, commitments and resources into balance so that we can emerge with a coherent and affordable Defence programme for the future. Much work has been done to re-align the budget, but staying the course will require sustaining the strict cost-control regime I have put in place at the MOD.

The SDSR also called for stronger Defence partnerships with our main allies, whose security interests and military capabilities are closest to our own. Last year we signed a Defence and Security Co-operation Treaty with France taking our co-operation to a new level and offering a number of mutual benefits. Developing partnerships of this kind is the right way forward at a time when resources are constrained.

The SDSR alone will not be enough to solve the problems facing Defence. That is why an early priority of this Government was to launch a full review into how Defence is run. The Defence Reform Unit, led by Lord Levene, looked at how the MOD is structured and managed, and how we can reform the Armed Forces to produce more efficient provision of Defence capability, including the generation and sustainment of operations.

There has been much public focus on equipment and how we procure the capabilities our Armed Forces need, but we should never forget that it is our people, the men and women of our Armed Forces, who are our greatest asset. Without them there is no Defence of the realm. That is why we have set out for the first time a tri-service Armed Forces Covenant so that not only the Government but all of society can help fulfil the moral obligation the nation has to our Armed Forces, their families and our veterans. In the difficult economic circumstances the country faces this will not be easy or straightforward but where we have been able to make early progress we have done so including doubling the Operational Allowance and prioritising mental health treatment.

The people of Britain are rightly proud of our Armed Forces, evident in many public events, up and down the country, where we pay tribute to our Service personnel. We move forward in this time of global uncertainty, confident that our Armed Forces supported by our civilian staff and the people of the United Kingdom, will face the future challenges with the same professionalism, courage and commitment they have shown this year.



The Secretary of State for Defence
The Right Honourable Liam Fox MP

A handwritten signature in black ink, which appears to be 'Liam Fox', written in a cursive style.

Introduction by Chief of Defence Staff and Permanent Secretary



Permanent Under Secretary (PUS) for Defence Ursula Brennan, is pictured at the Ministry of Defence



Chief of the Defence Staff (CDS), General Sir David Richards KCB CBE DSO ADC Gen is pictured at the Ministry of Defence

2010-11 has been a very challenging year for Defence. Continuing conflict in Afghanistan, the need to intervene in North Africa, the Strategic Defence and Security Review, a change of Government, a fundamental examination of the structure of Defence and a period of national financial austerity presented challenges that would have been difficult to manage individually. Coming together, they meant one of the busiest and most demanding years we have faced in decades.

In 2010-11, success in the operation in Afghanistan was the highest priority of the Ministry of Defence. As part of the 48-nation coalition, we now have the resources in place to create the conditions that will

meet the Prime Minister's objective of bringing our combat role in Afghanistan to an end by 2015.

Afghanistan is our main effort, but our personnel also serve in many other important roles, from the continuous at sea deterrent to the personnel on standby to protect our airspace. We have also retained the capability to mount a significant military response to new challenges, as our contribution in Libya has shown. We are asking and expecting a great deal of our sailors, soldiers and airmen, regular and reserve, on the front line and in support. They are more than meeting those expectations.

We have also been demanding, and getting, a great deal from our civilian workforce. The contribution they make, and the commitment to the purposes we serve, is often unrecognised and unsung. All that has been achieved this year is a tribute to the dedication and commitment of our people – both service and civilian. Like their service colleagues, our civilian workforce have continued to deliver in the face of uncertainty about the future size and shape of the Department, and the knowledge that there will be significant job cuts over the next four years.

The Spending Review outcome announced in October made significant reductions in previously planned spending across Government. Defence has to play its part in addressing the national financial position, by living within a budget that will be around 8% lower in real terms by 2014-15. The Strategic Defence and Security Review took some very difficult decisions to help rebalance the defence programme; implementation of these changes will require us to continue to develop and refine our plans to live within our means.

Delivering a coherent and relevant force structure in an uncertain world and with reduced resources will take commitment and determination, but it is also an opportunity: both of these pressures force us to take a hard look at how we do business. Our aim therefore, is to take this opportunity to transform Defence – not just what we do, as set out in the Strategic Defence and Security Review, but also how we do it. The Defence Reform Review led by Lord Levene sets the framework for far reaching change over the coming years.

Supporting our current operations while at the same time making profound changes in the way we work will continue to test our people. The challenges we face are considerable, but we know that when civilians and military staff work together, using the skills and experience of everyone in the team, we are capable of achieving great things.

A handwritten signature in blue ink, appearing to read 'Ursula Brennan'.

A handwritten signature in blue ink, appearing to read 'Sir David Richards'.

Performance and Key Facts – 2010-11

The Defence Aim is:

To deliver security for the people of the United Kingdom and the Overseas Territories by defending them, including against terrorism; and to act as a force for good by strengthening international peace and stability.

The reporting format followed for performance this year is that of the Coalition priorities, as defined in the MOD Business Plan 2011-15. This was published in November 2010 as part of the new Transparency Framework. The framework replaces the previous system of Public Service Agreements and central government targets.

The MOD Business Plan reflects the outcome of the Strategic Defence and Security Review (SDSR) and Spending Review 2010. It sets out the top level vision and priorities for Defence over the period 2011-2015. It informs the Strategy for Defence, Defence Strategic Direction and the Defence Board's strategic objectives. It will be revised annually.

In common with other Departments, the MOD Business Plan contains five sections : Vision, Coalition Priorities, Structural Reform Plan, Departmental Expenditure, and Transparency. Key information about the MOD is provided by a series of 'input' and 'impact' indicators. Input indicators show how the Department's resources are being deployed. Impact indicators provide information on key priorities. In future, the data against these indicators will be captured and reported through the Quarterly Data Summary. This will be published in the Annual Report and Accounts from 2012.

The latest version of the MOD Business Plan can be found at <http://www.number10.gov.uk/wp-content/uploads/MOD-Business-Plan1.pdf>. The current input and impact indicators are set out in the table below.

Indicators

Table 0.1 – Data against Business Plan Indicators

Input		Impact	
Indicator	Data	Indicator	Data
Additional cost of operations in Afghanistan, per Service person deployed	£340,947	Progress toward a stable and secure Afghanistan	88%
Additional cost of new equipment (urgent operational requirements) for operations in Afghanistan, per Service person deployed	£56,632	Number of Service personnel deployed to support civil agencies (e.g. police and fire service) during emergencies	3,241 ¹
Cost of standing military commitments/tasks and contingent operations per committed Service person	This is a new data set and will not be reported until Quarter 2	Number of attaches and advisors deployed in support of conflict prevention and defence diplomacy activities	110 covering 143 countries
Average percentage by which the cost of the MOD equipment programme varies compared to forecasts in year	0.15	Number of Service and MOD civilian personnel deployed on all operations in a year	New data set. Not available until 2012

Table 0.1 – Data against Business Plan Indicators

Input		Impact	
Indicator	Data	Indicator	Data
Cost of major force elements, per ship, per brigade, per aircraft (fixed wing), per helicopter	Ship: £28M ² Brigade: Not available until Jul 11 Aircraft (fixed wing): £6.5M ³ [Helicopters: Not available at this time, to be reported from Quarter 2].	Number of Force Elements (typically ships, aircraft or ground force sub units) showing critical or serious weakness against the total number of Force Elements for Strategy for Defence priorities	8 (30%) ⁴
Cost/Benefit ratio of the major change and efficiency programmes being undertaken by Defence	1.75 ⁵	Average number of months that the MOD equipment programme is delayed in year	0.39 months per project ⁶
Percentage of non-front line costs versus front line costs, split by Service	New data set, to be reported from Quarter 2	Percentage of Service personnel that are deployable	92%
Direct personnel costs, per Service person	£49,000	Percentage change in filling skills top 3 areas where there are insufficient trained Service personnel to meet the specified requirements	Royal Navy: 9/12/47 Army: 31/46/62 RAF: 25/14/15
Direct personnel costs, per MOD civilian	£32,000	Percentage of Service personnel (split by officers and Other ranks) who are satisfied with Service life in general	Officers: 70% Other Ranks: 57% ⁷
Defence spending as a percentage of Gross Domestic Product	Not available until Quarter 2	Overall public favourability of the UK Armed Forces	88% ⁸

Notes

1 This figure includes those held at readiness, number covers the period 1 April 2010 – 31 March 2011

2 FF: £386m / 14, DD: £142M / 5

3 Tornado: £722M/136, Typhoon: £615M/71

4 Defence attributes 27 Force Elements against Strategy for Defence priorities. Out of these 8 are reporting critical or serious weakness which represents 30%.

5 For every £1 spent the MOD gains an additional £1.72 This CBR was calculated from data provided by programmes within Level 1 of the Defence Change Portfolio (DCP). The DCP has very recently been subsumed into the new Defence Transformation Portfolio, and so any future CBR will be calculated for spend to save programmes within Tier 1 of this new Portfolio.

6 Total net slippage of 15 months reported in-year against 38 projects.

7 Key AFCAS 2010 findings, from 31 Mar 2011 Report

8 Polling conducted Mar 11.

Structural Reform Plan

Progress against the actions articulated in the Structural Reform Plan part of the Business Plan is reported monthly and published on the No 10 and the MOD websites. The MOD's Director General Finance can be subject to a monthly review meeting by the Cabinet Office and the Treasury. The Secretary of State and Permanent Secretary can be held to account quarterly for the Department's performance against Structural Reform Plan actions.

Table 0.2 – Progress against Structural Reform Plan Actions

Number of SRP actions¹ to be completed in the period covered by the Annual Report and Accounts²	Number delivered on time	Number missed by < 1 month	Number missed by < 2 months	Number missed by > 3 months	Number of actions completed early
20	18	0	1 ³	1 ⁴	7 ⁵

Notes

- 1 Milestones have been excluded where they match an action
- 2 The data provided is based on the first MOD Business Plan which was published in Nov 10. A refreshed MOD Business Plan was published in May 11 and covers the period Nov 10 – Mar 11
- 3 The publication of the Service Personnel sub-Strategy that included New Employment Model (NEM) principles was delayed by 2 months. It was published in May 11. This was caused by the complexity of SDSR implementation planning.
- 4 The launch of a dedicated 24-hour support line for ex-Service personnel was delayed by 3 months. This was primarily caused by the tender process and negotiations between the Department of Health, Combat Stress and the preferred supplier. The 24-support line was formally launched on 11 Mar 11.
- 5 Actions that were due to be completed in the period covered by subsequent Annual Reports and Accounts.

1. Afghanistan (including other Operations)

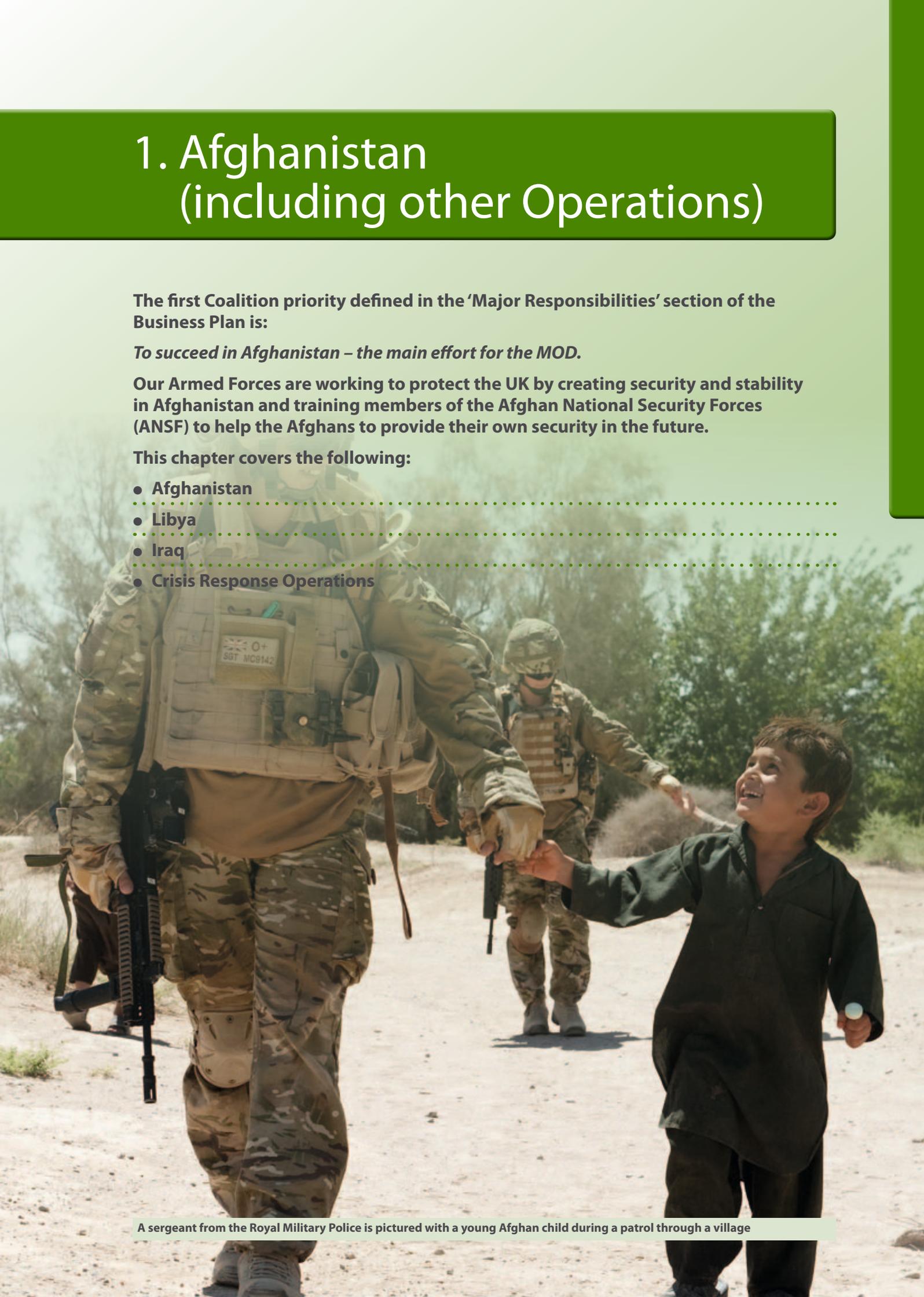
The first Coalition priority defined in the 'Major Responsibilities' section of the Business Plan is:

To succeed in Afghanistan – the main effort for the MOD.

Our Armed Forces are working to protect the UK by creating security and stability in Afghanistan and training members of the Afghan National Security Forces (ANSF) to help the Afghans to provide their own security in the future.

This chapter covers the following:

- Afghanistan
- Libya
- Iraq
- Crisis Response Operations



A sergeant from the Royal Military Police is pictured with a young Afghan child during a patrol through a village

CURRENT OPERATIONS

Afghanistan



Overview

1.1 The campaign in Afghanistan remains the Defence main effort. The UK has continued to play a leading role in the NATO-led International Security Assistance Force (ISAF). ISAF remains NATO's largest ever mission, with 48 nations contributing some 132,200 troops as of March 2011. The international community aims to improve security, to facilitate development and reconstruction and support the Government of Afghanistan as it extends its authority across the country. The UK's aim is that the threat of terrorism to UK national security from Afghanistan no longer requires the deployment of UK combat forces. To achieve this, the MOD is focused on degrading the insurgency, and building the capability of the Afghan National Security Forces (ANSF) so that they, in time, are able to provide security for the population.

1.2 The ISAF mission in Afghanistan is divided into six regional commands with the UK's presence mainly concentrated in central Helmand in Regional Command (South West) (RC(SW)). The current distribution of forces follows the split in June of RC (South) into two regional commands, RC (South) and

RC (South West), to reflect better the size of ISAF in the south following the surge of troops that arrived throughout 2010. An additional 20,000 ISAF troops were deployed to Helmand in 2010, enabling the UK to focus its troops, along with our Danish and Estonian allies, on the three more densely populated districts of central Helmand, whilst handing over the northern and southern districts to US forces. The UK holds a number of senior appointments within ISAF including Deputy Commander ISAF, Chief of Staff ISAF Joint Command, Commander Force Reintegration Cell and Deputy Commander RC(SW).

1.3 Over the course of 2010-11, two formations provided the headquarters for Task Force Helmand. 4 Mechanised Brigade served from April to October 2010 and 16 Air Assault Brigade for the next six months until April 2011. In addition, in January, the UK-led Allied Rapid Reaction Corps deployed to Afghanistan, providing augmentation to ISAF Joint Command. The UK's enduring force level has remained at 9,500 although, as the Defence Secretary announced in February, when our special forces, their enablers and temporary deployments for specific tasks are included, there are regularly well over 10,000 UK Armed Forces in Afghanistan at any one time.

1.4 In addition to our Armed Forces, some 140 MOD civil servants are deployed in support of operations in Afghanistan, providing financial, policy, claims, commercial and media advice, intelligence analysis, and specialised scientific support, as well as assistance through the MOD Police. Civilians have also worked as advisors and mentors, helping to develop the Afghan MOD in Kabul.

Key Achievements

1.5 During the year, Task Force Helmand continued to focus its efforts on counter insurgency through targeting Taliban command and control structures. In July 2010, 1st Battalion The Duke of Lancaster's Regiment undertook Operation Tor Shezada to clear insurgents from the area around Sayedabad to the south of Nad-e Ali, to prevent its use as a base from which to launch attacks. Task Force Helmand has also supported Afghan-led operations, such as Operation Omid Char in October 2010, which was mentored by 1st Battalion Irish Guards but devised and led by the Afghan National Army. This operation successfully secured a key area near Gereshk in Nahr-e Saraj district. Task Force Helmand has, since December 2010, taken on the additional task of ensuring freedom of movement on Highway One in Maiwand District, which links the key economic centres of Helmand and Kandahar.

ISAF and Afghan forces have reversed the insurgents' momentum in many key areas, but this progress is fragile. A difficult 2011 is expected as the insurgency attempts to regain lost ground.

1.6 The increasing role that the ANSF are playing in the planning and leading of operations is essential to ensure that they are able to manage any residual insurgent threat once ISAF combat troops withdraw. The UK provides support to the training and development of the ANSF in three main ways: through embedding staff officers in the NATO Training Mission Headquarters; by providing trainers to training institutions; and through the embedded partnering of deployed ANSF in Helmand Province. Challenges remain in improving the capability of the ANSF but the last year has seen some key achievements: security for the Afghan Parliamentary elections across the country was successfully provided by the ANSF with no major incidents, and in Lashkar Gah, UK partnered ANSF are successfully managing security to the extent that the urban district has been announced as one of the first areas to begin the transition process to Afghan-led security.

1.7 Coordinated and effective cross-Government collaboration in advance of the Lisbon Summit in November enabled the UK Government to make an important contribution and secure agreement across NATO and with the Afghan Government that the process of transition would begin in 2011. The conference also highlighted the need for an agreement on an enduring NATO partnership with Afghanistan. The UK has worked hard to maintain cohesion across the alliance and encourage other nations to meet shortfalls in the requirement for personnel to train the ANSF.

The setting sun provides a backdrop to Afghan National Army (ANA) troops as they set up security on a road they have just searched for improvised explosive devices



Costs

1.8 The net additional cost of military operations in Afghanistan fell from £3.820 Bn in 2009-10 to £3.774 Bn in 2010-11. This includes costs for items such as fluctuations in fuel prices, food for service personnel and additional costs to contractors.

Casualties

1.9 85 Service personnel were killed in Afghanistan between April 2010 and March 2011 (126 in 2009-10), and a further 146 suffered serious or very serious injuries between April 2010 and 31 March 2011 (170 in 2009-10). This brought the total number of deaths from the start of operations in Afghanistan in November 2001 to 31 March 2011 to 363, of whom 319 were classed as killed as a result of hostile action.

Equipment

1.10 The SDSR made it clear that we will continue to provide our Armed Forces with the equipment and protection they need to operate effectively in Afghanistan. We are procuring increasingly bespoke and sophisticated equipment. Our capabilities are widely recognised as being better than ever before.

1.11 We have approved over £250M of new equipment since June 2010, including over £80M on Counter-IED equipment to detect, destroy and avoid IEDs. We are making headway in finding the IEDs before they explode and identifying and targeting the bomb makers and those who finance and direct them. Wolfhound, the new Tactical Support Vehicle and Warthog, the protected all-terrain vehicle, are both providing troops with increased protection. Further deliveries of Mastiff, Ridgback, and Jackal vehicles were also made. We confirmed the procurement of Foxhound to replace Snatch Vixen Plus, and are aiming for the first vehicles to be delivered for training in 2011. The first layer of a new, multi-tiered pelvic protection system was introduced to help mitigate the effects of IED blasts. Other personal equipment delivered in theatre included Head Mounted Night Vision Systems, sets of Mk4 Osprey body armour, and Sharpshooter, the new infantry combat rifle. These were all designed to contribute towards improving the range, reliability and safety of all deployed Service personnel.

The sun sets as ISAF troops in a Husky Armoured Vehicle pass Afghan locals on Route Trident in Helmand, Afghanistan



Libya

1.12 In early March 2011, UK Armed Forces were involved in an operation to evacuate UK nationals and allies from Libya in response to the worsening security situation. Assets deployed included HMS Cumberland, three C130s supported by an E-3D AWACS, and a VC10.

1.13 On 26 February the United Nations passed Security Council Resolution (UNSCR) 1970, which called for an end to all violence. Col Gaddafi failed to comply with this resolution and continued to pose a threat to his own civilians. On 17 March the United Nations passed UNSCR 1973, which authorised the use of all necessary force to protect civilians. The UK played a key role in the initial activity setting up a no-fly zone, and continues to have a leading role in the NATO led operation to enforce the arms embargo and protect civilians.

1.14 In support of UNSCR 1973, HMS Liverpool and HMS Cumberland conducted maritime interdiction operations. RAF Typhoon, Tornado GR4, E-3 Sentry, Sentinel R1, Nimrod R1, VC10, Tristar and C130 aircraft have all been in action. Initial clearance of air defence was undertaken by Tomahawk Land Attack Missiles (TLAM), launched from a Trafalgar Class submarine.

1.15 As of 31 March 2011, RAF aircraft had flown over 176 sorties. UK forces have made a significant contribution to the total flying hours of the coalition, damaging Gaddafi's land, air and air to air capabilities whilst taking the utmost care to minimise civilian casualties.

1.16 The net additional cost of military operations in support of United Nations Resolution 1973 in 2010-11 was £21.6M; this covers the period 19-31 March. The current estimate of the costs for the six months from mid-March to mid-September is some £120M. This excludes costs of capital munitions expended. We estimate the cost of replenishing

munitions may be up to £140M, based upon current consumption rates. These costs will be met from the Reserve rather than the core Defence budget. The costs of Libya will be included in the Department's Spring Supplementary Estimates in January 2012.

Iraq

1.17 UK Service personnel continued to make a major contribution to progress in Iraq. The number of UK Service personnel in Iraq has reduced significantly from 4,100 in 2009 to 135, including the UK contribution to NATO forces in the country.

1.18 The UK-led Iraq Training and Assistance Mission (Navy) at Umm Qasr Naval Base has continued to develop the capability of the Iraqi Navy to maintain the sovereignty and integrity of Iraqi territorial waters, in particular protecting Iraq's offshore oil infrastructure and the security of merchant vessels. This task began in 2003, and is covered by the UK-Iraq Training and Maritime Support Agreement. This agreement marks the transition from a mission focused on large-scale support of the Iraqi Security Forces in Basra to a more normalised bilateral defence relationship. In November 2010 the Iraqi Council of Ministers requested a six month extension of the agreement. In addition, Royal Navy patrols of the Iraqi offshore oil infrastructure concluded on 22 May 2011.

1.19 The UK has supported the NATO Training and Assistance Mission (Iraq) under which the UK has the lead for the delivery of the Iraqi Officer Education and Training programme, with the aim of creating a self-sustaining Iraqi officer training capacity at the Military Academy in Ar Rustamiyah, Baghdad.

Crisis Response Operations

1.20 The UK military has continued to play a full part in global crisis response operations, both as part of an international response and on the basis of providing national assistance. In August 2010, the MOD supported the Government's response to severe flash flooding in Pakistan, deploying RAF C-17 Globemaster and C-130 Hercules to deliver humanitarian relief. In November 2010, Royal Navy ships were involved in disaster relief operations following a tropical storm in St Lucia. In February 2011, a small-scale military deployment supported the FCO-led evacuation of UK Nationals from Egypt.

2. Standing Commitments

The second Coalition priority defined in the 'Major Responsibilities' section of the Business Plan is:

To continue to fulfil our standing commitments, including strategic intelligence, the strategic nuclear deterrent, defence against direct threats to the UK and its overseas territories, counter-terrorism and military aid to the civil authorities.

Carrying out these roles is essential to our security and supports key British interests around the world.

This chapter provides an update on the following:

- Defence of UK Overseas Territories, UK Airspace and Waters
- Deterrence
- Counter Piracy
- Counter Terrorism and Olympics
- Military Aid to the Civil Agencies
- Activity and Concurrency Levels
- Residual Capability
- Other Defence Activity



RFA Fort Victoria passes Mogadishu during OP CAPRI, the Counter-Piracy effort off the Somalian Coast

STANDING COMMITMENTS

Defence of UK Airspace and Waters and UK Overseas Territories

2.1 Quick Reaction Alert aircraft and air surveillance and control facilities continue to be used to defend UK airspace. During 2010 Typhoon fighter aircraft replaced almost all of the Tornado F3 in this role. Police and maritime authorities have primacy in protecting the coastline of the UK, and Defence maintains an appropriate force to provide support to these authorities if required. The UK Government remains fully committed to the defence of UK Territories in the South Atlantic, including South Georgia and the South Sandwich Islands. UK forces remain permanently deployed in the Falklands in a deterrent role. In Cyprus we maintain important military facilities in the Eastern and Western Sovereign Base Areas, which have provided vital support to operations in Afghanistan and Libya.

Deterrence

2.2 In the National Security Strategy and SDSR, the Government reaffirmed the requirement for the nuclear deterrent. Nuclear weapons continue to provide the ultimate guarantee of the UK's security by deterring nuclear blackmail and acts of aggression against the UK's vital interests. They also contribute to the security of NATO, whose continuing requirement for nuclear deterrence was reaffirmed in the Strategic Concept agreed at the Lisbon summit in October 2010.

2.3 The SDSR also stated that the time was now right to offer a new assurance that we will not use, or threaten to use, nuclear weapons against non-nuclear weapons states who have signed the Nuclear Non-Proliferation Treaty (NPT). In giving this assurance, we emphasised the need for universal adherence to the NPT. This assurance would not apply to any state in material breach of those non-proliferation obligations. We also noted that while there is currently no direct threat from states developing capabilities in other weapons of mass destruction, such as chemical and biological, we reserve the right to review this assurance if the future threat, development and proliferation of these weapons make it necessary. Deliberate ambiguity is maintained about precisely when, how and at what scale we would use the deterrent. We will not simplify the calculations of an aggressor by defining more precisely the circumstances in which we might use our nuclear capabilities; hence,

we will not rule in or out the first use of nuclear weapons. But the Government has made clear many times over many years that the UK would only contemplate using nuclear weapons in extreme circumstances of self-defence and in accordance with the UK's international legal obligations.

Counter Piracy

2.4 Despite the increase in international military presence in 2010-11 the number of successful pirate attacks in the Gulf has remained at similar levels to last year. However, the effectiveness of the Internationally Recognised Transit Corridor, protecting the 30,000 shipping moves that pass through the Gulf of Aden each year, has forced the pirates to displace a proportion of their criminal activity into the Somali Basin. They now operate up to 1,300 nautical miles from the Somali coast using mother ships to support several pirate skiffs.

2.5 Defence plays a key role in the international effort and we provide a significant contribution to counter piracy operations off the coast of Somalia, tackling the problem at sea through three co-ordinated counter piracy operations; the European Union's Operation ATALANTA, NATO's Operation OCEAN SHIELD, and the US led Combined Maritime Force. Royal Navy vessels and personnel play an active role in all three multi-national task forces.

2.6 Operation ATALANTA continues to escort humanitarian assistance (through the World Food Programme and African Union Mission in Somalia shipments) to Somalia and counter piracy off the coast of Somalia. The UK provides the Operation Commander and the multinational Operation Headquarters at Northwood as well as providing a frigate in the first quarter of 2011.

HMS Victorious photographed in the Clyde estuary whilst on transit to the Clyde Submarine Base Faslane



2.7 Since the launch of Operation ATALANTA the mission has successfully escorted 96 World Food Programme (WFP) ships into Somalia allowing over 480,000 metric tonnes of food to be delivered. In addition to the European escorts, NATO, China and Russia have undertaken escorts of WFP shipments, allowing over 1 million people to be fed each day. It also provided escorts to 95 other supply ships.

2.8 As well as providing assets to NATO and the Combined Maritime Force, the UK is also providing the Deputy Commander Maritime Forces in Bahrain and was in command of the deployed NATO units until Summer 2010.

2.9 The MOD continues to work with other Whitehall departments and international partners to tackle piracy on many fronts and the conditions from which it arises. Through the Contact Group on Piracy off the Coast of Somalia, the UK has an integral role in enhancing co-ordination between all naval forces and merchant shipping in the region; developing the judicial, penal and maritime capacity of regional states to tackle the threat locally; resolving national and international legal issues; providing clear guidance to the shipping industry on self-protection; and tackling the financial incentives that perpetuate piracy.

Counter Terrorism and the Olympics

2.10 Defence contributes to the four work streams of the Government's counter-terrorist strategy – *Pursue, Prevent, Protect* and *Prepare*. We support *Pursue* through operations overseas to detain terrorists and deal with insurgencies, as well as through intelligence collection and counter-terrorism capacity building for partner nations (which together with conflict prevention work, also supports *Prevent*) and support to overseas law enforcement and security agencies. We support *Protect* by encouraging improved domestic security and co-operation between the Armed Forces and the UK civilian Emergency Services. In the event of a terrorist attack that exceeds the capability or immediate capacity of the UK civilian response, we can provide support to *Prepare* through Military Aid to the Civil Authorities.

2.11 The Department of Culture Media and Sport is responsible overall for the conduct of the Olympics and Paralympics. The Home Office Olympic Security Directorate is responsible for the safety and security of the Games. MOD will be providing a range of support, principally to the Police, in respect of Olympic security, and throughout 2010-11 has been closely engaged in Olympic security planning.

Defence continues to provide military advice and dedicated planning support, through close cross-Departmental liaison and the secondment of military staff officers to key organisations.

Picture shows HMS Cornwall's Royal Marine boarding teams during anti-piracy operations off the coast of Somalia, East Africa



Military Aid to the Civil Authorities

2.12 The Home Secretary is responsible for the safety and security of the UK and its citizens. Under the Civil Contingencies Act 2004, lead Government departments are allocated to deal with the most likely high-impact disruptive events. MOD is not the lead for any civil contingency, but if required can provide support to the lead organisation, through the Military Aid to the Civil Authorities process. We supported the civil authorities in carrying out their functions on over 75 occasions in 2010-11. These ranged from the provision of logistics support to the police and ambulance service to the important transport and other assistance deployed to several parts of the UK during the severe cold weather in December 2010.

2.13 Northern Ireland. Around 4,000 members of the Armed Forces based in the UK are currently stationed in Northern Ireland. Military personnel stationed there regularly deploy on operations overseas. MOD retains a limited commitment to deploy troops in support of the Police Service of Northern Ireland in the event of widespread and sustained public disorder, although this has not been called on since 2005. MOD also provides specialist support to the civil power, mostly through Explosive Ordnance Disposal. The threat from Northern Ireland related terrorism remains a security concern.

2.14 Counter Narcotics. From April 2010 to March 2011, the Royal Navy has assisted in the seizure of around 500 kilos of narcotics, predominantly cocaine. A prime success was achieved by HMS Manchester which, during a patrol in the Caribbean in October 2010, intercepted a consignment of 240 kilos of cocaine. Had these narcotics reached UK

streets they would have been worth, at that time, about £12 million. Counter-narcotics operations are almost always conducted in conjunction with other international authorities and law enforcement agencies. The MOD worked closely in support of the Serious Organised Crime Agency which leads the UK efforts in disrupting criminal narcotics trafficking worldwide. UK forces in Afghanistan, acting under NATO, continue to provide operational and logistical support to Afghan forces mounting counter narcotics operations as part of the counter-insurgency campaign.

2.15 Fisheries Protection. The River Class Offshore Patrol Vessels of the Fishery Protection Squadron supported the Marine Management Organisation with the equivalent of 672.5 days of fishery patrols. During 2010-11, 1,400 fishing vessels were boarded of which 11 were detained at a UK port for further investigation. The squadron detected 172 fishing infringements during the reporting period. Progress continues in the development of joint operations and in working with other EU member states to improve the efficiency and effectiveness of their patrol assets.

2.16 Search and Rescue. The MOD search and rescue service exists to help military aircrew in difficulty. It also contributes to the UK's integrated national search and rescue framework. Helicopter cover for most of the UK, and a large area of the surrounding sea, is provided 24 hours a day by the RAF and RN from eight helicopter bases, augmenting the service provided by a civilian company from a further four bases under contract to the Maritime Coastguard Agency. The RAF also maintains four RAF mountain rescue teams in the north of the UK, expert in dealing with aircraft crashes in remote areas. The UK Aeronautical Rescue Co-ordination Centre at RAF Kinloss co-ordinates the response of all UK search and rescue aircraft and mountain rescue teams and hosts the UK Mission Control Centre for the global satellite-based distress beacon detection system. Search and Rescue cover is also provided by the RAF from RAF Akrotiri in Cyprus and in the Falkland Islands. In 2010-11 Defence Search and Rescue services were called out 2,050 times (2,418 in 2009-10) and came to the aid of 1,647 people. Statistics on Military Search and Rescue incidents, callouts and people moved can be found on the UK Defence Statistics 2010 website at: <http://bravo.dasa.r.mil.uk/modintranet/UKDS/UKDS2010/c5/table501.php>

2.17 Explosives Ordnance Disposal. MOD provides 24 hours-a-day Explosive Ordnance Disposal (EOD) support to the Police in the UK. This includes the provision of operational scientific expertise to deal with complex devices. Routine

co-ordination of EOD tasking is conducted by the Joint Service EOD Operations Centre at Didcot which allocates Royal Navy, Army or RAF teams to an incident by matching the requirement to a particular capability. EOD teams are stationed at various locations through the UK and responded to over 2,485 callouts in 2010-11 (2,850 in 2009-10).

Activity and Concurrency Levels

2.18 The overall proportion of the Armed Forces engaged on current operations, military tasks or duties in the UK increased slightly this year to 26% (up from 24% in 2009-10). The proportion of regular forces deployed on operations and undertaking other Military Tasks has also marginally risen (up one percent) and is now at 15%. The rise is, in part, due to increased activity in the Gulf region and more recently the provision of support to the NATO operation in Libya. Table 2.1 sets out the percentage of regular Armed Forces undertaking operations and undertaking Military Tasks during 2010-11.

2.19 The **Royal Navy** has continued to make a significant contribution to wider UK security by supporting operations and commitments in Iraq, the Gulf, Horn of Africa, Mediterranean and the North and South Atlantic. The year has seen a highly successful final phase of the MOD's contribution to Iraqi Navy training through the UK Training and Maritime Support Agreement. This will draw down in the near future.

2.20 Naval Forces have assisted with the evacuation of Libya, helped protect World Food Programme shipping, delivered the United Kingdom's continuous at sea nuclear deterrent patrols, maintained the standing commitment in Diego Garcia, provided security of territorial waters and economic zones, led counter-piracy operations off the Horn of Africa as part of NATO, European Union and coalition initiatives and supported the civil authorities for search and rescue, fishery protection, and counter-drugs activities. In keeping with previous years 3 Commando Brigade once again undertook challenging and rigorous activities against the Taliban in Afghanistan.

2.21 The announcement was made of a three year contract for an interim Ice Patrol Ship HMS PROTECTOR, to deliver the Government's security and environmental objectives within the ant-Arctic; her first patrol will take place during the austral summer of 2011. This year the overall percentage of Naval Service personnel deployed on operations and undertaking other Military Tasks has been relatively stable at a mean of 16%.

Table 2.1 – Percentage of Regular Armed Forces undertaking operations and undertaking Military Tasks during 2010-11:

	Deployed on Contingent Operations				Undertaking Military Tasks			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Royal Navy	7%	7%	8%	7%	11%	12%	8%	6%
Army	8%	9%	8%	9%	7%	8%	8%	9%
Royal Air Force	5%	5%	5%	6%	5%	5%	5%	5%
Overall	7%	8%	7%	8%	7%	8%	7%	8%

Notes:

1. Figures are rounded up to whole figures.
2. Percentages are quarterly averages and reflect the burden of activity imposed by the operations and other Military Tasks undertaken by each service. Figures are based on man-day equivalents.
3. A list of Military Tasks can be found on the Department's website (www.mod.uk).

2.22 The **Army** has again had significant numbers of troops deployed worldwide on operations, the majority of whom have been in Afghanistan. Support to the UN has continued through a variety of global operations, including Cyprus, Democratic Republic of Congo and Sudan. All standing commitments were met with Land Forces permanently stationed in Northern Ireland, Cyprus, Brunei, Nepal, the Falkland Islands and Ascension Island, Gibraltar and the British Indian Ocean Territory.

2.23 As set out in more detail above, the Army has maintained its support to the NATO-led ISAF in support of the Government of Afghanistan. As a result the ANSF have grown and British Forces, partnered with forces from the Afghan National Army and Police, have temporarily extended their operations to secure a greater freedom of movement. Defence remains committed to providing long-term sustainable support to the Afghan National Development Strategy, particularly on governance, rule of law, human rights and poverty reduction.

2.24 Elsewhere, Land Forces have continued to contribute to the Government's Counter-Terrorism strategy by delivering military advice and assistance across all four strands (Pursue, Protect, Prepare, Prevent), including training assistance to a number of high priority countries in capabilities such as border security, Counter-Terrorist detention, public order, and aviation security. The percentage of Army personnel deployed on operations and undertaking other Military Tasks has remained at an average of 16%.

2.25 The **Royal Air Force** has remained committed overseas particularly in the Gulf region, Afghanistan, Gibraltar and Pakistan. Security co-operation and strengthening of international peace and stabilisation and support to wider British

interest have been delivered through support to arms control, defence diplomacy, NATO counter intelligence operations and defence export activities. Strategic intelligence was provided in liaison with Government Communications Headquarters, the Joint Aerial Reconnaissance Intelligence Centre and Defence Intelligence and Security Centre.

2.26 The high level of commitment of air transport and support helicopter fleets has continued. Standing commitments to nuclear deterrence (through the Nuclear Emergency Response Organisation) and transport security have continued to be met, along with other Defence Military Tasks that encompass search and rescue, counter drugs activities, airborne surveillance and control.

2.27 The RAF also contributed to permanent commitments in Northern Ireland, the Falkland Islands and Cyprus, and a range of other Military Tasks including the integrity of UK waters and airspace. More recently the draw on the Air Force has been significant, assisting with the evacuation of British National and Entitled Personnel from Libya – in concert with Maritime forces – and the follow on task to establish a No Fly Zone in support of UNSCR 1973. Overall the percentage of RAF personnel deployed on operations and undertaking other Military Tasks was an average of 11% of trained strength.

2.28 Looking to the **Future** the SDSR has allowed the MOD to identify the Armed Forces required over the next ten years, and the changes that are required to deliver them. Drawing on the Military Tasks and Planning Assumptions, an outline force structure has been designed that Defence aims to deliver for the 2020s. The new Defence Planning Assumptions envisage that the Armed Forces in the future will be sized and shaped to conduct:

- an enduring stabilisation operation at around brigade level (up to 6,500 personnel) with maritime and air support as required, while also conducting:
- one non-enduring complex intervention (up to 2,000 personnel), and
- one non-enduring simple intervention (up to 1,000 personnel); or alternatively:
- three non-enduring operations if we were not already engaged in an enduring operation; or:
- for a limited time, and with sufficient warning, committing all our effort to a one-off intervention of up to three brigades, with maritime and air support (around 30,000, two-thirds of the force deployed to Iraq in 2003).

Residual Capability

2.29 Contingent forces are held for unforeseen emergencies or to reinforce existing operations. This could include the UK's contribution to a multinational operation. But the forces are held principally to allow Defence to respond to scenarios in which the UK acts alone to protect national security interests, for example to conduct hostage rescue or Counter Terrorism operations. High readiness forces include a balanced range of highly capable land, air and maritime capabilities. But the range of forces available has been reduced as Defence does not plan for, or expect, forces to be simultaneously engaged in completing and supporting current operations at the level and intensity they have in recent years and at the same time be ready for the full range of potential contingent operations set out in Defence Planning Assumptions.

2.30 The readiness of the Armed Forces for contingent operations beyond Afghanistan has improved gradually over the past year and is expected to continue to improve. The MOD's priority remains to recuperate some key capabilities and then, as conditions allow, further contingent capability.

2.31 The **Joint Force Headquarters** (JFHQ) continues to provide the standing command and control capability at the heart of the United Kingdom response to emerging crises. It holds an Operational Liaison and Reconnaissance Team (OLRT) of eight personnel at four hours notice to brief. The remainder of the JFHQ (up to 47 personnel) is held at 24 hours notice to move and

would be allocated forces as necessary. The JFHQ has again maintained a high level of operational activity over the year, providing the UK Joint Force Headquarters for the evacuation of UK nationals from Libya, support to the evacuation of UK nationals from Egypt and broader crisis planning as a result of the recent wave of popular protest across the broader Middle East and North Africa.

2.32 In addition OLRTs have deployed on a number of occasions during the year to provide information and advice and to inform the decision-making process. JFHQ maintained theatre awareness or conducted directed tasks by deploying specialists to a range of countries including the Lebanon, Israel, Jordan, Sudan, Nepal and Bangladesh. It interacted with European Union, Netherlands, France, Sweden and USA counterpart headquarters staffs and worked with British Forces Cyprus and several single-Service headquarters. JFHQ draws on wider expertise from other organisations, including the Foreign and Commonwealth Office, the Department for International Development, Civilian Police, International Committee of the Red Cross, single Service staffs, cultural advisors and the Stabilisation Unit and as part of this relationship JFHQ was the framework HQ for a PJHQ hosted Integrated Approach Exercise.

Other Defence Activity

Conflict Prevention and Defence Diplomacy

2.33 The SDSR committed the Government to a more integrated approach to dealing with conflict, through development of a strategy for Building Stability Overseas. This will bring together our diplomatic, development and defence resources to deliver more focussed effort in those fragile and conflict-affected countries where the risks are high, our interests are most at stake and where we know we can have an impact. The strategy will be published later in 2011. One of the key resources for delivering this integrated effort is the cross government 'Conflict Pool' which continues to balance its programming between conflict prevention and stabilisation activity. Through 2010-11, MOD continued to work closely with DFID and the FCO on conflict prevention and capacity building in Africa, Wider Europe, Middle East, and South Asia, and through the Strategic Support to International Organisations thematic programme. In total, the Government has invested around £180m on the Conflict Pool in 2010-11, with MOD leading activity totalling around £60m.

2.34 In Africa MOD has helped develop peace support operations capacity at sub-regional and national level by providing training to African Armed Forces, to improve their ability to take part in peacekeeping missions and contribute units to the future African standby force. One of the Africa programme's key objectives for the period 2008-11 is to support the development of the African Peace and Security Architecture. MOD's work in developing the capabilities of the African Union (AU) continues to play a key role. Maintaining the fragile Comprehensive Peace Agreement in Sudan remains difficult following the referendum and creation of South Sudan. The UK and the wider international community played a lead role in the period leading up to the referendum, including through structured engagement with the Sudan Armed Forces and the Sudan People's Liberation Army. In the Niger Delta, the UK has continued to support a Joint Maritime Security Training Centre to improve Nigerian inshore operational capability. MOD has also continued to provide strategic support to the Sierra Leone security sector, investing in assisting the development of stable and democratic governance, overseeing accountable security services and a reduction in regional militia.

2.35 In the Middle East, MOD has continued to use Conflict Pool funding to build the capacity of the security forces of the Palestinian Authority, as developing the security sector will be critical to the viability of a future Palestinian state. The MOD has continued to provide technical assistance to the US Security Co-ordinator through the British Support Team. The MOD has continued to build capacity in the Lebanese Armed Forces. UK mentoring has improved the capacity of the Lebanese to command and control their border management and to support the development of the Lebanese Armed Forces Internal Security Facility, which now runs comprehensive internal security courses.

2.36 UK Conflict Prevention spending in the Wider Europe region continues to focus on government capacity and accountability, and on security and justice sector reform. In Kosovo, the Conflict Pool funds two key posts in the NATO Advisory Team, overseeing the development of the Kosovo Security Force from Initial Operational Capability (achieved in 2009) to Full Operational Capability by 2012. In Bosnia the EUFOR mission, which has an executive UN mandate for as long as it is required, is committed to providing a safe and secure environment, supported by a small number of UK conflict pool funded staff posts. The UK-funded Peace Support Operations Training Centre in Sarajevo continues to provide high quality training to officers from countries in the region. In

Serbia, the funding of a documentary television series about the NATO partnership for peace has enhanced the reputation of NATO among the population by developing their understanding of its aims, objectives and remit. In Ukraine, the UK's Special Defence Adviser is assisting the Ukrainian MOD with its reforms. The Special Defence Adviser also works in Georgia, where he is assisting with the establishment of NATO's Professional Development Programme for civilians working in defence. In Armenia a retired British Major General has assisted the Armenian MOD with planning and writing its first Strategic Defence Review.

2.37 Through the Strategic Support to International Organisations thematic programme, the MOD has assisted in the development of the Armed Forces of partner nations throughout 2010-11 by providing defence education and training to 11 countries. Through the wider Conflict Pool programme, MOD also continued to contribute to capacity-building for peace support operations, especially through 'train the trainer' schemes, notably the British Military Advisory Training Team in the Czech Republic. These teams help other countries become self-sufficient, capable of providing for their own security in an accountable and democratic framework, and contribute personnel to peace support operations.

2.38 MOD continued to support the development of the Stabilisation Unit through the provision of military officers and civil servants to its staff. The Stabilisation Unit, which is jointly owned by MOD, FCO and DFID and funded through the Conflict Pool, provides specialist, targeted assistance in countries emerging from violent conflict where the UK is helping to achieve a stable environment that will enable longer-term development to take place. During 2010-11 the Stabilisation Unit has promoted a greater unity of purpose through cross-Government planning and better understanding of stabilisation. Throughout the year Military Stabilisation Support Group (MSSG) continued to work closely with the Stabilisation Unit providing military expertise to operations and exercises globally.

2.39 In addition, the MOD Defence Assistance Fund has continued to support activities to meet wider defence diplomacy aims and objectives. Defence education and training, short term training teams, staff talks, exchange visits and other activities contribute to the development of strong bilateral defence relationships that help mitigate potential security challenges and support current and potential operations.

NATO

2.40 The UK also continues to support the NATO Response Force (NRF), making regular force contributions, including the Maritime Component Command from January to June 2011. In support of these command elements the UK has committed throughout 2010-11, an Anti-Submarine Warfare Escort ship; a Mine Counter Measures Vessel; twelve air defence/ground attack aircraft; between two and five Airborne Early Warning aircraft and two Air to Air refuelling aircraft. These air and maritime elements are currently committed to NATO's Operation UNIFIED PROTECTOR. The UK also acted as the lead nation for Chemical Biological Radioactive Nuclear (CBRN) from January to June 2010. This consisted of the component command and force elements including survey detection and analysis. These contributions were found from the Joint NBC Regiment; other nations, primarily the Czech Republic also contributed force elements. The UK has also contributed a number of ships to NATO's counter-piracy mission (Operation OCEAN SHIELD).

Common Security and Defence Policy (CSDP)

2.41 Following the ratification of the Lisbon Treaty in December 2009, the UK has continued to take a leading role in developing CSDP. A number of the senior posts within the European External Action Service have been filled but the structures continue to be developed. The UK continues to ensure that the EU is focused on delivery of more capable, coherent and effective policy and activity that remains supportive of, and complementary to, NATO.

2.42 In addition to Operation ATALANTA we continued to support Operation ALTHEA in Bosnia-Herzegovina and the EU Training Mission in Somalia. The UK provided one of the two EU Battlegroups on standby for the EU Battlegroup roster between January and July 2010. The UK is also providing the EU Operational Headquarters in support of the Nordic Battlegroup from PJHQ in Northwood from January to June 2011.

UN Peace Keeping Operations

2.43 The MOD supported three UN Peacekeeping Operations in 2010-11, providing some 290 UK military personnel to missions in Cyprus, the Democratic Republic of Congo, and Sudan. We also supplied staff officers to the UN Assistance Mission in Afghanistan, the UN Assistance Mission for Iraq, and the UN Political Office for Somalia.

The United Nations

2.44 The UK maintained its commitment to UN-mandated peace support operations, with some 10,000 troops committed in Afghanistan and Cyprus. In addition, the UK provided individual staff officers to UN missions in Africa. Elsewhere, MOD provided training assistance to other countries in order to increase their ability to contribute to UN missions and, alongside the FCO and DFID, contributed to bespoke projects that improve the deployability of international forces and the effectiveness of UN peacekeeping as a whole. At the higher level, the UK had direct involvement in, and provided support to, the UN's Department of Peacekeeping Operations (DPKO) and the Department of Field Support (DFS) in New York. MOD also attended the annual G8++ International Peace Support Operations Clearing House, where we work alongside international partners to address shortfalls in peace support operations capability.

2.45 The UK continued to work to assist the DPKO, primarily through the secondment of UK military personnel. In addition, the UK, as a permanent member of the UN Security Council, remains committed to supporting implementation of reforms at the strategic level to enable the DPKO and DFS to be more effective. MOD has also encouraged better co-operation between the UN and regional organisations such as NATO, the EU and the African Union. Finally, MOD has been active in promoting UNSCRs and has been particularly successful in its application of UNSCR 1325 – Women, Peace and Security. This year the UK revised its national action plan on UNSCR 1325. As part of this process, MOD identified a number of new actions, these include:

- Deployment of female engagement teams into Afghanistan
- Cultural (including gender) training for the Armed Forces
- Deployment of Cultural Advisers into Afghanistan
- Work to further incorporate reference to UNSCR 1325 into MOD doctrine

Arms Control and counter proliferation

2.46 The National Security Risk Assessment identified that the risk from hostile acts by terrorists and states would be greatly increased if weapons of mass destruction, advanced military technologies, and the systems used to deploy them reached the

wrong hands. The following paragraphs summarise the way in which MOD has contributed significantly to meeting HMG's wider arms control and counter-proliferation objectives and thus reducing such risks. MOD has also continued to play an important role in working with partners across Government and our international allies to ensure that arms control and counter-proliferation initiatives strengthen our security.

Nuclear Arms Control

2.47 MOD has continued to work closely with the FCO, DECC and international colleagues in building consensus across all three Pillars of the Nuclear Non-Proliferation Treaty (NPT). MOD supported the Review Conference team, both at the UN and from London and directly contributed to the successful outcome of the Review Conference in May 2010 which, for the first time, agreed an Action Plan across all three pillars: non-proliferation, peaceful uses of nuclear technology, and nuclear disarmament.

2.48 The UK's verification research with regard to nuclear warhead dismantlement, on which MOD has been leading with Norway and the non-Governmental organisation "VERTIC", underlined our practical commitment to a world without nuclear weapons and reaffirmed our position as the most forward leaning of the nuclear weapon states.

2.49 The MOD has continued to fulfil its international obligations as the National Authority responsible for the UK's commitment to the Comprehensive Test Ban Treaty. The MOD continues to influence international discussions on and to build capacity for an effective future verification regime that is mindful of Defence interests. We continue to support HMG efforts with the international community to bring swift entry into force.

2.50 The UK has continued to support calls for negotiations on a Fissile Material Cut-off Treaty to commence in the Conference on Disarmament. The MOD has continued to work actively to understand the implications of such a future treaty, to inform and influence the preliminary international discussions, and to prepare the UK in order to protect HMG's national security and nuclear proliferation interests.

Chemical and Biological Arms Control

2.51 MOD and its agency, Defence Science and Technology Laboratories, continued to provide technical expertise in support of UK efforts to strengthen the Chemical Weapons Convention

and the Biological and Toxin Weapons Convention (BTWC). MOD also continued to implement chemical and biological non-proliferation projects under the UK Global Threat Reduction Programme, which delivers the UK's commitment to the G8 Global Partnership against the spread of weapons and materials of mass destruction. MOD successfully completed its assistance programme in support of the chemical weapons destruction facility at Shchuch'ye in the Russian Federation. MOD has implemented a variety of major construction and procurement projects at Shchuch'ye, managing funds worth over £90m contributed by the UK, Canada, France and 10 other international donors.

2.52 MOD is continuing to develop its biological non-proliferation programme, in close co-operation with the US and Canada, and with expert UK agencies (e.g., Health Protection Agency, Veterinary Laboratories Agency, Food and Environment Research Agency). The programme aims to reduce the risks of proliferation of biological expertise, weapons and materials, including by providing former weapons scientists with civil employment and improving biological security and safety internationally. Projects include training in bio-safety, modern diagnostics and disease surveillance, covering both human and animal diseases; surveillance of key crop pathogens; technical advice and training for laboratories holding dangerous pathogens; and participation in a regional workshop in support of BTWC implementation. Current priority areas are Central Asia, the Caucasus, and Middle East/North Africa. Further information on the UK Global Threat Reduction Programme can be found in the 2010 annual report at: http://www.decc.gov.uk/en/content/cms/what_we_do/uk_supply/energy_mix/nuclear/nonprolif/global_threat/annual_report/annual_report.aspx

Ballistic Missile Defence

2.53 The SDSR reaffirmed our commitment to the NATO Ballistic Missile Defence (BMD) programme. The UK has no plans to develop or acquire a national BMD capability. At the November 2010 NATO summit, the UK supported the decision to expand the scope of the NATO BMD capability to protect all NATO populations, territory and forces against the increasing threat posed by proliferation of ballistic missiles and to explore opportunities for increased cooperation with Russia in this area. We continue to provide support to the US BMD system by providing access to data from RAF Fylingdales and RAF Menwith Hill. We also continue to work closely with the US and our other NATO allies to develop our understanding of BMD and the range of related political, technical and operational issues associated

with tracking and intercepting a ballistic missile in flight. The research activities that we are carrying out with our scientific and industry partners continues to provide the UK with a better understanding of BMD-related technologies, as well as offering UK industry the opportunity to contribute to international programmes.

Conventional Arms Control

2.54 There has been little progress to resolve Russia's unilateral suspension of the Treaty on Conventional Forces in Europe (CFE) in December 2007, even with increased US led diplomatic efforts. CFE is, in effect, stalled. The activities associated with the updating of the Vienna Document 1999 have continued as has Open Skies Treaty activity, which included the UK accompanying Russian and Georgian personnel on missions to their respective countries. During the year, the UK hosted four inbound verification missions from other states and led or participated in 36 outbound verification missions.

Arms Trade Treaty

2.55 The UK remains committed to securing a strong Arms Trade Treaty under which all states apply common criteria in assessing whether or not to export conventional arms. The MOD has contributed significantly to UK efforts to secure a robust Treaty, which will help regulate the worldwide arms market and prevent weapons reaching the hands of terrorists, insurgents and human rights abusers. Negotiations have started with three Preparatory Committee meetings at the UN. It is still early days, but progress has been encouraging with a common acknowledgement of the need for better regulation of the arms trade. The main challenges, however, will be faced in the run up to the 2012 Negotiating Conference as we seek to secure a robust and effective Treaty.

Export Controls

2.56 MOD strongly supports the UK's contribution to multilateral export control regimes and arrangements, which covers conventional weapons and associated technologies, and equipment and technology that could potentially contribute to a nuclear, biological or chemical weapons programme. MOD has provided technical input to UK efforts to strengthen the Control Lists of the Wassenaar Arrangement, Nuclear Suppliers Group, the Missile Technology Control Regime, and the Australia Group.

2.57 During 2010-11 MOD provided advice to the Department of Business, Innovation and Skills on the potential effect of proposed exports on the defence and security of the UK and our allies, and, in respect of export licence applications,

assessments of the risk of diversion of the goods concerned to an undesirable end-user. The 'Annual Report on Strategic Export Controls' contains further details of licensing decisions and the Government's performance in processing export licence applications. The 2010 report covering license issues during 2009 is available at:

<http://www.fco.gov.uk/resources/en/pdf/about-us/our-publications/sec-annual-report-2010>. The report for 2010 will be published in Summer 2011.

Disarmament

2.58 The Convention on Cluster Munitions came into Force for the UK on 1 August 2010. The UK became the 32nd state to ratify and the Convention entered into force for the UK on 1 November 2010. The Convention is recognised as one of the most significant disarmament treaties of recent years, prohibiting the use, production, transfer and stockpiling of cluster munitions. The Cluster Munitions (Prohibitions) Act 2010 received Royal Assent on 25 March 2010 and gives effect in UK law to these prohibitions. The Act has created the criminal offences in UK law that enforce the Convention's prohibitions and prevents prohibited activity from taking place within the UK and by any UK national, wherever they may be. The UK's last cluster munitions were withdrawn from service in May 2008 and disposal programmes are in place with substantial numbers already destroyed. Disposal of these munitions will be completed within the Convention's mandated deadline for destruction within eight years of entry into force: this will be 2018 for the UK.

Space Security

2.59 The increasingly congested and contested nature of outer space is a growing concern for global security and stability. Reliance on space permeates many facets of military capability and civilian infrastructure. The MOD continues to support the FCO in aiding the EU to facilitate international agreement on an International Code of Conduct for Outer Space Activities that will build confidence, predictability and enhance cooperation. The MOD is also supporting the development of the Cabinet Office led National Space Security Strategy.

Cyber Security

2.60 The MOD is working closely with the Cabinet Office and other agencies to develop and deliver the National Cyber Security Programme. As part of this we are mainstreaming cyber into the planning and conduct of military operations, and have appointed a senior officer to drive the necessary transformation across defence. Cyber security is a global issue, and the MOD is working with key Allies and NATO to improve our collective response.

3. Other Operations (Contingent)

The third Coalition priority defined in the 'Major Responsibilities' section of the Business Plan is:

To succeed in other operations we are required to undertake, by providing a defence contribution to UK influence, by defending our interests by projecting power strategically and through expeditionary operations, and by providing security for stabilisation.

This chapter provides an update on Funded Readiness.



Type 42 destroyer HMS Edinburgh on her way from Stanley to Fitzroy in the Falkland Islands

Funded Readiness

3.1 The MOD has a graduated readiness system in place to ensure that the right force elements (such as a ship, an Army brigade, or an aircraft) are ready to deploy to conduct the range of missions that may be required by the Government. Through regular Planning Rounds MOD's Head Office sets requirements for the three Services in terms of the force elements needed, the readiness at which they need to be held, and allocates the resources to achieve this. Underpinning this mechanism are specific parameters for manning levels, equipment, logistic support, and collective training (the training that units do together to ensure they can fight effectively as part of a larger force). Measuring and aggregating readiness is complex, not least because it is based on a judgement of what is required to enable the Armed Forces to respond to a wide range of potential challenges.

A Royal Air Force Typhoon pilot enters the cockpit as the sun sets over Gioia del Colle, southern Italy



3.2 The Armed Forces' readiness targets are measured against the ability to prepare, deploy, fight and recover against the full range of potential operations. In recent years, however, the Armed Forces have focused on preparing for and sustaining operations in Iraq and Afghanistan. In so doing, they have provided substantial forces at immediate readiness for those operations, deployed them to and sustained them in theatre, and recovered them to their home bases at the end of their tours. The net additional costs incurred in this are met from the central Government reserve and amounted to £3.891 in 2010-11. The Armed Forces have also continued to generate and sustain high quality, properly trained force elements for other Standing Military Tasks such as maintenance of the nuclear deterrent and the provision of garrisons in Permanent Joint Operating Bases worldwide.

3.3 This year as part of the Defence Performance Framework we changed the way Readiness is reported to enable us to focus on what can be achieved with all the Force Elements combined rather than with each Force Element individually. Previously Readiness reporting was based on 103 Force Elements which were individually weighted. The weightings produced percentages of Force Elements that showed critical or serious weaknesses. Under Defence Plan 2010 Force Elements were regrouped and Front Line Commands asked to report against Strategy for Defence priorities; weightings were removed. This led to more accurate reporting against the funded position and a better indication of where critical and serious weakness remains.

3.4 In 2010-11 we have continued to focus resources on those capabilities and force elements most heavily drawn on for Afghanistan. This is a conscious and measured decision in support of our Strategy for Defence and our main effort: Afghanistan.

4. Defence Exports

The fourth Coalition priority defined in the 'Major Responsibilities' section of the Business Plan is:

To promote defence exports consistent with export control criteria; as part of a defence diplomacy programme to strengthen British influence and help support British industry and jobs.

Lead responsibility for promoting Defence Exports lies with the Department of Business, Innovation and skills. However, exports reduce the cost of military equipment to the UK taxpayer, help us preserve strategically important Defence capabilities and increase our influence. Defence Exports are therefore one of the Coalition's top priorities for Defence.



A Typhoon Multi Role Fighter is serviced on the tarmac prior to takeoff at RAF Coningsby

Defence Exports

4.1 Defence exports help to reduce the cost to the taxpayer of MOD acquisition programmes by extending production runs, and help maintain highly skilled jobs in the defence and aerospace industry. Promoting exports as part of defence diplomacy initiatives enhances the UK's relationships with international partners by improving their capabilities, and acts as a lever to achieving the UK's international objectives.

4.2 UK Trade and Industry Defence and Security Organisation (UKTI DSO), part of the Department for Business, Innovation and Skills, have responsibility for promoting UK industry abroad. This year the MOD has provided support to UKTI DSO export campaigns in a number of ways. MOD Ministers, Service Chiefs of Staff, and senior MOD officials promote the UK's military capabilities to their overseas equivalents in support of UKTI DSO campaigns when it is appropriate. The MOD provides demonstrations and briefings both in the UK and abroad to promote UK capabilities, including events such as Farnborough Air Show. This year the Department has provided International Defence Training including specific packages in support of export campaigns.

4.3 As stated in the Green Paper "Equipment, Support, and Technology for UK Defence and Security", the MOD has often in the past set its equipment requirements at a level so high that the resulting system exceeded the needs and budget of potential export customers. We are now beginning to embed "exportability" into MOD projects by considering export potential at the earliest phase of the MOD's acquisition cycle. An example of embedding exportability is the Global Combat Ship (GCS). In considering the MOD's requirement for the Royal Navy's next generation surface combatants to replace the Type 22 and 23 frigates, the MOD is seeking to establish the requirements of potential foreign partners so that these can be incorporated into the programme where practicable. This will make the GCS highly exportable without compromising the needs of the UK.

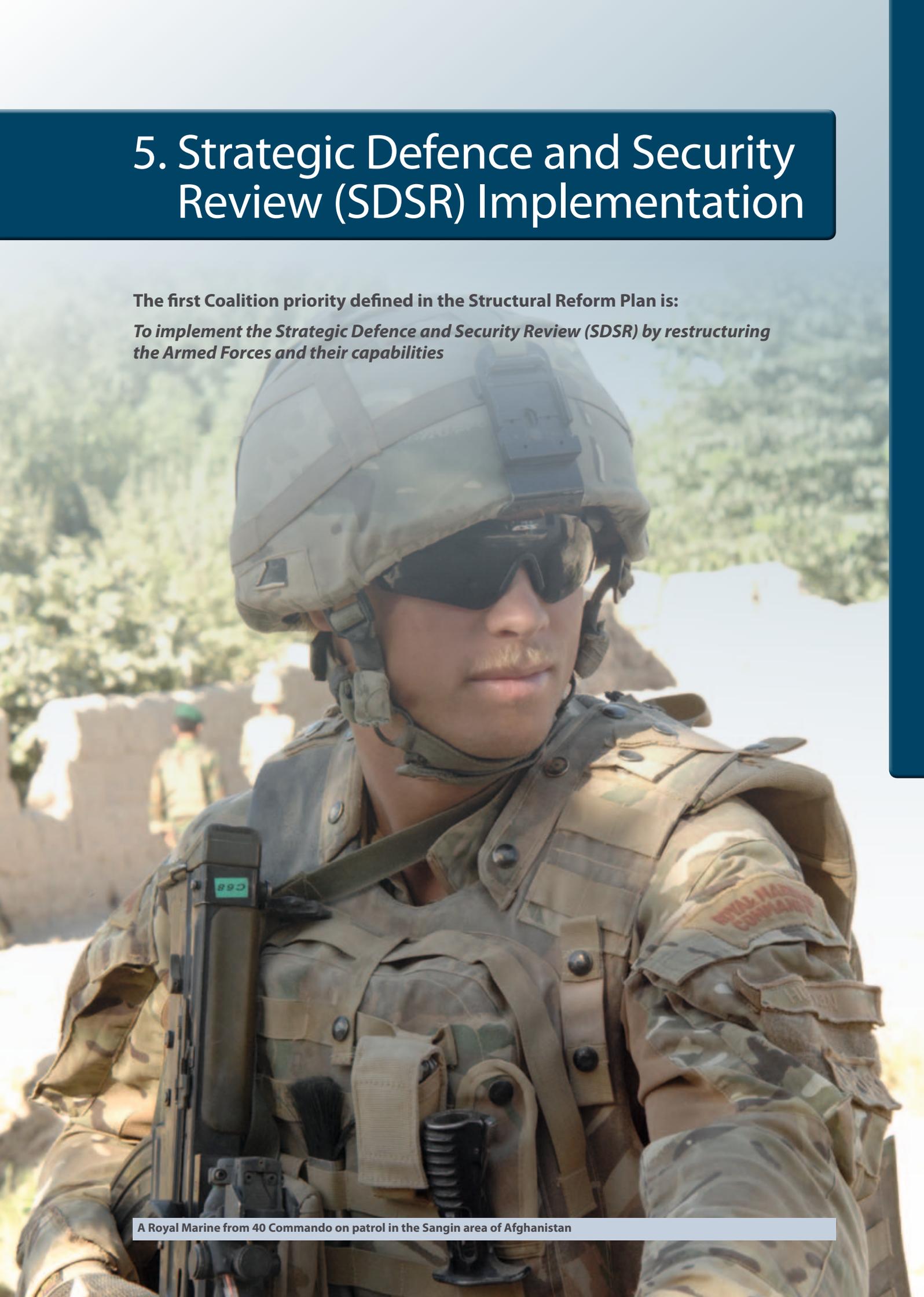
4.4 The MOD has been involved in demonstrating the capabilities of the Hawk trainer aircraft including hosting international delegations at RAF Valley to view the Royal Air Force's Advanced Flying Training. The Department has provided International Defence Training and in 2010-2011, 13 international students have been trained on the Hawk T1 at RAF Valley and four on the Typhoon, whilst the Royal Navy is currently delivering an extensive five-year training programme to the Royal Saudi Naval Force in support of the Saudi Hunter Project for the replacement crews of the three AL JAWF class (SANDOWN) Mine Hunters.

4.5 We have also supported a number of campaigns to export Typhoon. In 2010-11 the RAF has provided Typhoon demonstrations, flight evaluations and briefings to potential export customers, both in the UK and abroad. MOD Ministers, Service Chiefs and other senior officers have been involved in promoting Typhoon to foreign counterparts. The Department also currently provides International Defence Training as part of a Typhoon export package. This is generally perceived to be a significant attraction to overseas customers if they can also purchase RAF flying training.

5. Strategic Defence and Security Review (SDSR) Implementation

The first Coalition priority defined in the Structural Reform Plan is:

To implement the Strategic Defence and Security Review (SDSR) by restructuring the Armed Forces and their capabilities



A Royal Marine from 40 Commando on patrol in the Sangin area of Afghanistan

HMS Cumberland's Lynx helicopter



SDSR Implementation

5.1 The National Security Strategy and SDSR White Paper were published in October 2010. The SDSR was the first time that a UK government had taken decisions on its defence, security, intelligence, resilience, development and foreign affairs capabilities in the round. It set out the ways and means to deliver the ends set out in the National Security Strategy, and linked judgements on where to direct effort and focus the available resources, to choices on which risks and policies to prioritise. It set a clear target for the national security capabilities the UK will need by 2020, including Future Force 2020, and charts a course for getting there.

The SDSR outcome:

- Maintains our forces' geographical reach and ability to operate across a spectrum from high-intensity intervention to enduring stabilisation activity;
- Fully protects capabilities required for Afghanistan;
- Allows the UK to keep to our NATO commitment to spend at least 2% of our Gross Domestic Product on Defence;
- Delivers a broadly coherent strategic outcome within the time and resource constraints, and in parallel with the Government's Spending Review.

5.2 The Government has been clear that while the SDSR made substantial progress towards ensuring that we match our policy assumptions with our spending settlement, there is still more to be done. Ongoing initiatives include a review of

military basing, a reserves review and the changes being made under Defence Reform. The Department also continues to address the balance of defence priorities and budget over the long-term. This will inform the next planning round and help to build up to a sustainable Defence programme.

5.3 The SDSR also announced that the Department will be saving significant amounts from contract re-negotiations with defence industry. Good progress has been made, but negotiations are still ongoing.

5.4 Planning the delivery and implementation of the SDSR began in Autumn 2010 and is continuing into 2011. It is a significant undertaking to deliver on all of the commitments we have made due to the scale and complexity of the changes envisaged. Some decisions – for example, near-term force level reductions have been implemented quickly. Others – for example, future basing, present a considerable challenge, requiring extensive planning and longer term implementation.

5.5 The implementation of the SDSR is being taken forward using the Department's reformed strategic planning process. This approach ensures that, through a simplified set of classified, resource-informed planning documentation, the strategic direction provided by SDSR reaches every part of the Department, while implementation is constantly monitored and corrective action taken where necessary.

5.6 The Department has to deliver a volume of change over the coming period, on a scale perhaps unprecedented in UK Defence. For this reason we have established the 'Transforming Defence' initiative to ensure that all aspects of change – SDSR implementation, delivery of Spending Review 2010 Efficiency, major business change and Defence Reform Unit review implementation – are co-ordinated and driven in the same direction. A new Defence Operating Board, chaired jointly by the 2nd PUS and Vice Chief of the Defence Staff, now meets on a weekly basis to oversee delivery of Transforming Defence; and the Secretary of State for Defence also convenes a Steering Group to provide Ministerial oversight of progress. We also report progress on a regular basis in the context of the MOD Business Plan, and to the National Security Council.

5.7 While we can assure implementation of much of this through 'light touch' oversight, some programmes and initiatives are of particular importance to the overall implementation of the SDSR. To provide the additional assurance of delivery and senior oversight necessary for these, we have

created a Defence Transformation Portfolio (DTP), encompassing those programmes and initiatives falling within the 'Transforming Defence' umbrella.

5.8 Against the key commitments for which the MOD is responsible, we have delivered the following:

- HMS ARK ROYAL has been decommissioned. The SDSR concluded that our aircraft carrier capability should be based around a single new operational carrier with the second planned to be kept at extended readiness. The new carrier will embark Carrier Variant Joint Strike Fighters and helicopters.
- Initial Gate for the development study on 'cats and traps' for the future Carrier programme was achieved in April. The Queen Elizabeth-class carrier, operating the most modern combat jets, will give the UK the ability to project military power more than 700 nautical miles over land as well as sea, from anywhere in the world. This capability will give the UK long term political flexibility to act without depending on agreement from other countries to use their bases for any mission we want to undertake. It will also give us in-built military flexibility to adapt our approach over the 50 years of the carrier's working life.
- The Royal Navy's fleet of frigates and destroyers has been reduced by four to 19. The SDSR announced that we would retain a surface fleet of 19 frigates and destroyers, providing military flexibility across a variety of operations, from full-scale naval warfare, to providing maritime security (for example protecting trade and energy supplies) and projecting UK influence (for example through their visible presence or supporting building the capacity of regional partners). These will include six Type 45 destroyers and the current Type 23 frigates. As soon as possible after 2020 the Type 23 will be replaced by Type 26 frigates, designed to be easily adapted to change roles and capabilities depending on the strategic circumstances. Four of the Navy's oldest frigates, the Type 22s, have been removed from the line.
- RFA Largs Bay, an amphibious support ship, has been decommissioned. The SDSR explained that we would operate sufficient amphibious shipping to land and sustain ashore a Royal Marine Commando Group together with its equipment, and that accordingly we would decommission one of the Bay-class ships.

Soldiers from the 3rd Battalion the Parachute Regiment (3PARA) splash through a ford in a Jackal Armoured Vehicle



- We are on track to deliver the Army's new Multi-Role Brigades, which will consist of around 6,500 personnel and provide a wide range of capabilities, allowing them to operate successfully across the variety of possible conflicts that could arise over the next decades. The multi-role brigades will include: reconnaissance forces to gain information even in high-threat situations; tanks, which continue to provide a unique combination of protection, mobility and firepower; and infantry operating from a range of protected vehicles. The brigades will be self supporting, having their own artillery, engineer, communications, intelligence, logistics and medical support. Territorial Army personnel will be fully integrated into the new structures, in both specialist roles and reinforcing combat units.
- 40% of our Challenger 2 Main Battle Tanks are no longer in use, although we are still considering the future of the surplus tanks. This is consistent with our assessment of likely adversaries and future types of conflict. However, the tank will continue to provide a unique capability in roles from escorting convoys in high-threat IED

environments, deterring belligerents, through to warfighting alongside international partners.

- 35% of our AS90 armoured artillery vehicles are also no longer in use, although, again we are still considering the future of the surplus equipment. Precision ammunition allows us to strike targets with one round rather than using tens of unguided rounds. We have therefore reduced the number of artillery pieces.
- The Harrier jet has been taken out of service. The SDSR announced that the future fast jet fleet will consist of Typhoon and Joint Strike Fighter aircraft with around one third at high readiness. These are two of the world's most capable combat aircraft, able to operate in the future high-threat airspace while providing air defence and precision ground attack and combat capabilities. In the transitional period, we will retain a reduced Tornado fleet, but have removed Harrier from service. Retaining the Tornado fleet allows a fast jet contribution to be sustained in Afghanistan and support to concurrent operations which would not have been possible if the Harrier were retained instead.
- The Nimrod MRA4 maritime patrol aircraft has not been brought into service. It would have cost up to £200M per year to operate and maintain the aircraft. All nine aircraft have been disposed of, following recovery of equipment and systems that can be used elsewhere. Sentry (our Airborne Warning and Control System) offers some of the maritime patrol capability that MRA4 would have provided but we accept that we will be more reliant on Allies and partners for some forms of maritime protection and for long range search and rescue.
- A new tri-Service Armed Forces Covenant was published on 16 May 2011 alongside the full Government response to the report of the independent Armed Forces Covenant Task Force. At the same time we published 'The Armed Forces Covenant: Today and Tomorrow', which details the current actions being taken to deliver the Covenant and future commitments being implemented over the coming months and years.
- The SDSR welcomed Dr Andrew Murrison's report, 'Fighting Fit: a Mental Health Plan for Service Personnel and Veterans', and strongly endorsed its key themes and recommendations. Two of the key recommendations have been implemented: a dedicated 24 hour support line for veterans is now in operation and 30 additional mental health nurses have been commissioned in Mental Health Trusts to ensure that the right support is provided to veterans.
- The Secretary of State for Defence and the French Defence Minister exchanged and ratified the Defence Co-operation Treaty on 9 May.

5.9 Progress on delivery against our SDSR commitments will continue to be published in our monthly update on the MOD Business Plan. Implementation of this work may result in further costs in 2011-12, particularly as the value of surplus equipment and inventory is adjusted.

6. Armed Forces Covenant

The second Coalition priority defined in the Structural Reform Plan is:

Rebuild the Armed Forces Covenant, develop the New Employment Model and rebuild and formalise the Armed Forces Covenant which represents a promise of fair treatment, on behalf of the nation, to ensure our Armed Forces and their families are valued and respected, as part of the implementation of the SDSR.



Crowds cheer as soldiers march through Cardiff for the Armed Forces Day 2010 National Event

Armed Forces Covenant

6.1 On 12 May 2010 the Secretary of State committed to producing a new tri-Service Covenant which would “set out our obligations and commitments to the men and women of our Armed Forces, their families and veterans”. A new tri-Service Armed Forces Covenant was published on 16 May. It sets the tone for Government policy aimed at improving the support available for the Armed Forces community. The Armed Forces Covenant is accompanied by a more detailed document ‘The Armed Forces Covenant: Today and Tomorrow’ which sets out the actions currently being taken to support the Armed Forces community and future measures being implemented over the coming months.

6.2 Good progress has been made to date: we have already doubled Operational Allowance, improved Rest and Recuperation leave, launched a scheme to provide further and higher education scholarships for bereaved Service children and enhanced the scheme to enable Service leavers to get a first further or higher education qualification. Progress is also being made on the commitments which are being led by other Government departments, such as the recent introduction of a Service children’s Pupil Premium, the work to provide improved mental health support for veterans and the launch of a ‘Troops to Teachers’ scheme. Further detail on some of these measures can be found later in this report.

6.3 In addition the Armed Forces Bill, currently going through Parliament, contains a clause requiring the Defence Secretary to lay before Parliament an annual Armed Forces Covenant report. The report will set out how the Government is meeting their obligations in key areas including healthcare, housing and education. In producing the report we will continue to call upon the input of the External Reference Group to ensure that it is an accurate, objective assessment of progress in supporting the Covenant. Amendments have been proposed to the Bill to enshrine the principles of the Covenant in law. This is the first time that the Covenant has been recognised in statute.

6.4 The following paragraphs set out in more detail the progress that the MOD has made towards meeting key covenant commitments, and some of the other developments that impact on our Service personnel.

Revised Service Personnel Strategy and New Employment Model

6.5 The Service Personnel Strategy is the Defence Board’s strategy for delivering the people component of capability over the next 20 years. It seeks to achieve its aim through a series of activities which will enable us to:

- Identify, deliver and maintain the authorised full Manning requirement for the Armed Forces:
- Deliver trained personnel, with the right knowledge, skills and mind-set to succeed on operations and in wider Departmental business:
- Support and sustain personnel in ways that ensure they are always prepared for operations, and willing to serve as long as Defence needs them.

6.6 The key to delivering sufficient, capable and motivated personnel lies in ensuring that the demands placed on Service Personnel and their families remain in balance with the benefits and rewards of their service. The Service personnel Strategy includes the development of a New Employment Model that seeks to provide Terms and Conditions of Service (including career structure, pay, pensions, allowances and accommodation options) that better balance the expectations of Service personnel and the demands placed on them and their families.

6.7 One specific aim will be to improve domestic stability, which will have a range of benefits including for spouses’ employment and children’s education. The New Employment Model will recognise that, where mobility is required for service reasons, appropriate support and compensation should be available. A formal programme has been established to take forward this work and is due to report by Summer 2012. The intent is that policy changes will be implemented from 2014 over a period of about 10 years.

Pay and Allowances

Doubling of Operational Allowance

6.8 The doubling of Operational Allowance was announced by the Prime Minister on 10 June 2010, backdated to 6 May 2010. The tax free allowance was increased from £14.51 per day to £29.02, and this means for a typical six month tour in Afghanistan

the payment has increased from £2,640 to £5,281. Payment is in the form of a single lump sum paid on completion of operational service.

Other Allowances

6.9 The SDSR set out a requirement to reduce expenditure on Service allowances by some £250M per year by 2014-15. In introducing these changes we have sought to ensure that no group is disproportionately affected, and have mitigated the impact by phasing in some changes by up to two years. The substantial allowance package that remains will continue to reimburse Service personnel for justifiable expenditure incurred either when on duty or as a result of the unique nature of Service life.

Service Pay

6.10 As part of the Government's 2010 Emergency Budget the Chancellor announced a two-year pay freeze from 2011 for all public sector employees, including the Armed Forces. However, the Government stated that all those earning £21,000 or less should receive a minimum increase to annual salary of £250. In March 2011, the independent Armed Forces' Pay Review Body recommended an increase of £250 for Armed Forces' personnel earning £21,000 or less, which the Government accepted. About 50,000 Armed Forces personnel, including those under training, will receive increased rates of pay as a result. Other recommendations include new targeted measures designed to retain personnel essential to key operational capability, including new levels of Specialist Pay and Financial Retention Incentives. For example, Specialist Pay for explosive ordnance disposal operators was restructured from 1 April 2011 with the introduction of a new level and other levels increased.

6.11 In addition, all Service personnel not at the top of their pay range will continue to receive an increment each year, subject to satisfactory performance. However, the award of performance-related double increments made to a small number of senior officers, at 2, 3, and 4-Star rank, has been suspended for the period of the pay freeze.

Fair Pay Review

6.12 In May 2010 the Government asked Will Hutton to make recommendations to the Chancellor and Prime Minister on promoting pay fairness in the public sector. This work included Armed Forces pay. The final report was published on 15 March 2011. The Government welcomed this report.

6.13 The Armed Forces is one of the few areas within the public sector where average annual salary growth has been higher for those at the bottom of the scale than those at the top over the past decade. Therefore the Armed Forces are generally well placed to meet the challenges outlined in the Fair Pay report. Consideration of how to implement the specific recommendations will need to take the unique characteristics of the Armed Forces into account. MOD, like other Departments, has been asked to give detailed consideration to the final report proposal and bring forward implementation plans by July 2011.

Armed Forces Compensation Scheme (AFCS)

6.14 MOD has accepted all of the improvements recommended in Admiral the Lord Boyce's Review into the AFCS. Changes have now been made to the scheme, creating a more comprehensive compensation package for those injured as a result of service.

6.15 All those who have received an award under AFCS on or after 6 April 2005 will receive an increased payment to reflect the new levels of compensation. All uplifts are expected to be completed by June 2012. Those who have already received an award will be contacted automatically between now and next summer.

6.16 In addition to implementing Lord Boyce's recommendations, a group of senior medical professionals known as the 'Independent Medical Expert Group' provided expert advice on how the MOD can best compensate for certain injuries, including spinal cord injury and non-freezing cold injury. This work commenced in summer 2010 and the Group presented its first report in January 2011. The Report included initial findings in the areas of mental health and hearing loss and further work will continue on these issues in 2011.

Rest and Recuperation & Short Tours

6.17 The Defence Secretary announced on 22 July 2010 changes to the policy governing Rest and Recuperation. To ensure that those personnel who lose out as a result of operations or disruptions to the airbridge are not disadvantaged, additional Post Operational Tour Leave will be granted.

6.18 In addition, to increase the resilience of the airbridge, personnel deploying on short tours are

now posted for 119 days or less so they no longer require rest and recuperation. This policy has reduced passenger traffic over the airbridge by 11%, thereby improving operational efficiency.

Support to Service voters overseas

6.19 The Government is pursuing several parallel strands of work to improve the opportunities for Service personnel and their families overseas to register and to vote. We are finalising a process that aims to enable Electoral Registration Officers to utilise MOD data to authenticate individuals on the Electoral Register, identify where gaps exist and reduce the potential for electoral fraud.

6.20 For the UK Parliamentary and local elections in May 2010, a successful initiative was put in place to support the participation of Service personnel deployed in Afghanistan. In addition to our annual campaign to encourage all Service personnel to register to vote, a particular effort was made to encourage personnel who would be deployed at the time of the election to register. For those personnel in Afghanistan who wished to vote by post, arrangements for fast-tracking the handling of ballot papers within the UK and the use of supply flights to transport postal ballot packs to and from theatre (subject to operational priorities) saw over 200 postal ballots successfully returned in time for counting. This represented over 80% of those who wished to participate by post. Learning from last year's experience, we put in place similar arrangements to support the referendum on 5 May 2011.

Future Reserves 2020 Study

6.21 As part of the SDSR, the Prime Minister commissioned a review of the Reserve Forces to ensure that MOD makes the most efficient use of Reservist skills, experience and capabilities. General Sir Nicholas Houghton, the Vice Chief of Defence Staff, has been leading the review, supported by Julian Brazier TD MP and Lt Gen (Retd) Sir Graeme Lamb. The Future Reserves 2020 (FR20) study is due to report to Parliament shortly. FR20 has been exploring the role of the Reserves as part of the Whole Force Concept: a means to man a balanced force structure, comprised of Regular and Reserve personnel, contractors and civilians.

6.22 FR20 is looking closely at the future roles and structures of the Reserves out to the year 2020 and beyond. Reservists' skills and capabilities is at the forefront while moving towards a more efficient structure. A key aspect of the study is to examine how other countries use and structure their Reserve Forces and what lessons the UK might apply. FR20 is

also committed to ensuring the Reservist experience will remain valuable and high quality for Defence, individuals, and their employers.

Health and Social Care for Serving Personnel and Veterans

6.23 The MOD is working with the National Health Service, the Department of Health and Service charities to deliver in England the recommendations put forward by Dr Murrison in his report to the Prime Minister, 'Fighting Fit' *A Mental Health Plan for Servicemen and Veterans*, published in October 2010. The report focuses on improving the identification of mental health problems and better outreach, assessment and information services. The Government accepted all of the Report's recommendations and established a cross government committee to develop an implementation plan.

6.24 MOD will be working closely with King's College London on a two-year study, funded by the US military, starting in the Autumn 2011, on a potential screening tool for mental health disorders and Post Traumatic Stress Disorder using UK Armed Forces personnel. The cost of £1.6M will be met by funding obtained from a US military research facility.

6.25 In May 2011 the MOD launched a three month pilot in selected units across the RN, Army, and RAF to introduce enhanced mental health assessments into routine Service Medical Examinations. The pilot will inform the further rollout of the enhanced mental health assessments, which the MOD currently aims to integrate into discharge protocols – including those for seriously injured personnel – by late Summer 2011.

6.26 The Department of Health has commissioned 30 veterans mental health professionals to deliver improved NHS mental health services to veterans in England. They will forge links with health and other statutory agencies and with the voluntary sector and will also undertake outreach work to identify cases and refer individuals to veterans' organisations and other professionals. The service was commissioned in March 2011 and it will start to be rolled out later in 2011. In addition, a 24 hour mental health helpline¹, was introduced in March 2011. It is provided by Combat Stress with Department of Health funding and offers support to Service personnel, their families and veterans.

6.27 An online mental health wellbeing website will also be delivered by the Department of Health working in partnership with the MOD. The

¹ 0800 138 1619,

Department of Health has contracted with 'Big White Wall' to provide this online early intervention portal. The service will be targeted at three groups: veterans, serving personnel and families. This will be trialled during 2011 with a view to wider roll out in 2012.

6.28 MOD policy for management of Community Mental Health is currently being revised to allow Service personnel who have mental health issues whilst serving (or identified at the release medical), to continue to access the military mental health centres for up to six months after discharge. Arrangements to ensure follow-on treatment is provided are planned to be in place and operational by late Summer 2011.

University & Further Education Scholarships for Children of Service Personnel and Pupil Premium

6.29 The Coalition 'Programme for Government' contained two specific commitments for Service children: to provide university and further education scholarships for the children of Service men and women killed on active service since 1990, and to explore the potential for including Service children within their proposals for a pupil premium. The Armed Forces Bereavement Scholarship Scheme was launched on 8 April 2011 to provide scholarships of up to £8,240 per year for the children of personnel who died in service and whose deaths were deemed attributable to their service. MOD is administering the scheme, but the cost of the scholarships will be met by the Department for Education and the Department of Business, Innovation and Skills for those resident in England and by the Devolved Administrations for their residents. A Service pupil premium was included in the Government's revised school funding formula announced in December 2010. It is set at £200 per Service child in a maintained school in England in 2011.

Review of the exclusion of women from ground close-combat roles

6.30 In accordance with the requirements of the European Council Equal Treatment Directive, the MOD carried out a review of the policy of excluding women from ground close-combat roles. The review concluded that the policy should remain unchanged.

6.31 The outcome of the review was formally announced in a written Ministerial Statement by

Minister (DPWW) on 29 November 2010 [<http://www.publications.parliament.uk/pa/cm201011/cmhansrd/cm101129/wmstext/101129m0001.htm#1011294000011>] and, in parallel, a full report on the review, including the research that was carried out, was published on the Department's website. [<http://www.mod.uk/DefenceInternet/AboutDefence/CorporatePublications/PersonnelPublications/EqualityandDiversity/Gender/WomenInCombat.htm>]

Armed Forces Continuous Attitude Survey

6.32 The Armed Forces Continuous Attitude Survey (AFCAS) 2010 Report was published on 31 March 2011. The AFCAS collects information about Service personnel's attitudes regarding terms and conditions of service on an annual basis. The report draws out information on key aspects, such as satisfaction and morale, commitment, demands on the individual, remuneration, and Service living accommodation. The AFCAS is an important tool for informing our personnel policy staff and wider stakeholders about Service life. The Department will continue to use the information from the survey to focus attention where it is most needed to make further improvements in the future.

6.33 Some of the key findings of the survey were:

- Individual morale continued to increase and for the first time the majority (52%) rated their own morale as high. Up 3% from 2009.
- The vast majority (85%) were proud to be in the Service (unchanged from 2009).
- A lower proportion (38%) reported feeling valued, although this has improved year on year since 2007.
- Most (60%) were satisfied with their job in general (unchanged from 2009).
- Satisfaction levels with aspects of pay (Basic Pay 52%) have increased, by 3%. Satisfaction levels on specialist pay, pensions and allowances remain unchanged from 2009 (34%, 56% and 55% respectively). 26% agree the X-Factor is sufficient compensation.
- Satisfaction levels with the standard (40%) and amount (38%) of major equipment have steadily increased since 2008 and in each case report a 5% increase from 2009.
- A majority (68%) state: the frequency of my Operational deployments is about right, and 83%

state: the length of my Operational deployments is about right.

6.34 A copy of the full AFCAS 2010 report can be accessed at <http://www.mod.uk/DefenceInternet/FreedomOfInformation/PublicationScheme/SearchPublicationScheme/ResultsForArmedForcesContinuousAttitudeSurveyafcas.htm>

Manning Levels

6.35 Overall manning levels for the Armed Forces are published in the UK Defence Statistics, and can be found at <http://www.dasa.mod.uk>. The Defence Secretary has also committed to publishing data on Pinch Points, which are skills areas where there is insufficient trained personnel to meet the specified requirement. This can reflect a shortage of people against the peacetime requirement, a temporary operational requirement greater than the peacetime requirement, or a combination of the two. Pinch Points are managed by the individual Services, with a central working group maintaining an overview to identify trends and to ensure best practice. Each Service maintains a list reflecting operational commitments and manning levels within branches and trades, which varies over time. The position as of 31 March 2011 is set out at Table 3.1 opposite. This table excludes information on pinch-points that might jeopardise operational security.

Navy

6.36 Navy operational Pinch Point trades have during the year reduced from 16 to 11, which is an improvement. The most important trades to have left the list are: Lieutenant Submariner Warfare qualified and Rotary Wing Observers. There are shortages of 46% amongst Leading Aircraft Controllers and 50% amongst Strategic Weapon System Leading Hands in the Control and Monitoring Panel and Watch Keeper areas. Royal Marine Other Ranks shortfalls have been rebase-lined and the rank range reduced from OR2-9 to OR 4-8, where the 27% shortfall remains a concern.

Army

6.37 The Army currently has 22 Operational Pinch Points, a slight reduction during the year of two. Royal Logistic Corps Ammunition Technician has been removed from the operational list and transferred to the Manning Pinch Point list. The Royal Logistic Corps Improvised Explosive Devise Disposal Operators is the Army's critical concern followed closely by the shortage of interrogators (86%) and Electronic Warfare specialists. Infantry Private

to Corporal (Pte-Cpl) shortages remain a minor concern.

6.38 Army Manning Pinch Points have fallen from 20 to 17 mainly as a result of two trades moving off the list into the Operational list (Army Medical Services Intensive Therapy Nurse and Army Medical Services Emergency Medicine Nurse), two trades dropping off the list (Royal Signals Information System Engineer and Army Medical Services Operating Department Practitioner), one trade moving onto the list (Royal Logistic Corps Logistics Specialist, the Private to Lance Corporal grouping) and two trades moving from the operational list to the manning list (Royal Engineers Clerk of Works and Royal Engineer Mechanical Engineers Fitters).

RAF

6.39 In response to the previously (prior to Redundancy Programme announcement) suppressed outflow rates, RAF operational pinch points have reduced during the year from 12 to 7 with the Intelligence and Air Traffic Control branches, and the Logistic (Movements) and Intelligence Analyst trades leaving the list during the year. The RAF's main concern is the shortfall of Intelligence Analysts (Voice) and General Technician (Mechanical) and the potential shortage of pilots.

6.40 Manning pinch points have shown a similar degree of movement and now comprise only nine branches and trades, comprising those Operational Pinch Points listed above and also the Airspace Battle Manager and Chaplaincy branches.

Redundancy

6.41 In the SDSR, the Government announced reductions in the size of the Armed Forces, reducing the Army by 7,000, the Royal Air Force by 5,000 and the Royal Navy by 5,000. This will help to ensure that the UK has the required force structure, training and equipment to carry out operations, as part of the implementation of the SDSR. The Armed Forces redundancy programme is expected to deliver up to 11,000 redundancies across the three Services and should be completed by 31 March 2015.

6.42 The first redundancy criteria for the three Services were published on 1 March 2011 for the RAF and 4 April 2011 for the Army and RN. Those selected for redundancy will be notified on 1 September 2011 (Army and RAF) and 30 September 2011 (RN). Those leaving through redundancy are entitled to a comprehensive resettlement provision to help them transition back to civilian life. This is the first of up to four tranches of redundancy in each of the Services; the fields for the second tranche will be announced in Autumn 2011.

Table 3.1 – Operational Pinch Point Trades

Royal Navy		
Trades	Liability/Shortfall	% Shortfall
Lt Cdr XSM Command Qualified	46/4	9%
Leading Aircraft Controllers	67/31	46%
Rotary Wing Pilots	610/54	9%
Anti-submarine Warfare Aircrew men	89/21	24%
Strategic Weapons System Junior Rates	28/14	50%
Leading Seaman General Service	612/148	24%
Seaman Specialist	334/104	31%
Royal Marine Other Ranks	2,284/617	27%
Leading Air Engineering Technicians	828/244	29%
Cat A Nuclear Watch Keepers	147/26	18%
Cat B Nuclear Watch Keepers	373/91	24%
Army		
High Threat IED Operators	130/40	31%
Yeoman of Signals Electronic Warfare	35/16	46%
Systems Operator Electronic Warfare	170/61	36%
RAVC Dog Handler	201/58	29%
Military Intelligence Cpl-Sgt	640/232	36%
Interrogators	70/60	86%
Intelligence Corps Linguist	263/163	62%
RMP Special Investigation Branch Sgt-WO2	178/12	7%
Military Provost Staff	132/22	17%
Combat Medical Technician (CMT) Cpl-Sgt	720/250	35%
Royal Artillery Exactor DC	24/1	4%
Royal Engineer Clerk of Works SSgt – WO1	274/37	14%
Royal Artillery Weapons Locating Radar DC	156/0	0%
Royal Artillery UAV Operator Bdr-Sgt	225/86	38%
HUMINT Operator	232/78	34%
Geospatial Engineer Cpl	82/50	61%
REME Armourer Class 1	246/82	33%
Infantry Pte – Cpl	18,829/839	4%
Pharmacist Officer Capt and above	23/12	52%
Observation Post Assistant	395/75	19%
Royal Artillery Capts	260/18	7%
RMP GPD – LCpl – SSgt	1238/+32	+3%
Royal Air Force		
Intelligence Analyst (Voice) – SAC to Sgt	159/47	30%
Pilot – Junior Officer and Squadron Leader	1940/170	9%
Operations Support (Regiment) – Junior Officer	205/35	17%
Medical Officer – whole branch	280/30	12%
Emergency Nursing – whole cadre, all ranks	75/50	32%
Gunner – SAC to Cpl	1680/120	7%
General Technician (Mechanical) – SAC to Sgt	900/190	14%

A soldier returning from Afghanistan is reunited with his young son



7. Defence Reform Review

The third Coalition priority defined in the Structural Reform Plan is:

Deliver the Defence Reform Unit's review. Identify and deliver ways to create a simpler and more effective department, including significant reductions in running costs



Royal Air Force servicewoman, an Army soldier and a Royal Navy sailor salute

Defence Reform Review

7.1 On 13 August 2010, the Defence Secretary launched Defence Reform, to conduct a fundamental review of how the MOD is structured and managed and design a simpler and more cost-effective model for departmental management. It covered not only structures, processes and governance, but also clarity of purpose, behaviours, culture and incentives. He asked Lord Levene, Chair of Lloyds and a previous Chief of Defence Procurement, to lead a small steering group to oversee the work, provide external challenge and draw on wider private experience of managing change. On 27 June 2011 The Secretary of State published their Report, *Defence Reform: An independent report into the structure and management of the Ministry of Defence*. He has agreed its conclusions. The report can be found on www.mod.uk. Work is proceeding on its implementation as part of Defence Transformation. This will include statutory impact assessments on some of its proposals, and Trades Union consultation on those recommendations affecting civil servants.

7.2 In addition to Lord Levene the Steering Group comprised Conservative peer Baroness Noakes, George Iacobescu (Chief Executive of Canary Wharf), Dr David Allen (a Non-Executive member of the Defence Board), Raymond McKeeve (a partner at law firm Berwin Leighton Paisner), Björn Conway (a partner at Ernst and Young), and Gerry Grimstone (Chair of Standard Life and formerly a Non-Executive Director at Air Command). The 2nd Permanent Secretary and Vice Chief of the Defence Staff were also members to provide defence expertise and a departmental perspective. The Steering Group met monthly, and in between these meetings worked through three sub-groups looking at:

- policy, strategy, planning and financial management, including support to Ministers and accountability to Parliament;
- integration with the Armed Forces; and
- estates, corporate services and acquisition.

7.3 It was supported by a civilian-military team of about 20 people, drawing deeply on the skills and expertise of many people across the department.

7.4 Work was taken forward in three broad phases:

- diagnosing the core issues that had to be addressed, during which the Steering Group looked at how the organisation of the MOD has developed over the past century and why;

analysed the strengths and weaknesses of the current model, the problems it faces and their underlying causes, reviewed benchmarks within the Defence, wider public and private sectors, and looked at lessons from past efforts to reform the MOD to inform implementation;

- Following this investigative phase, they developed a range of options to address the problems and best deliver the Department's purpose and drew up a future operating model for Defence; and finally
- drew out the top level organisation and processes that flowed from that model to decide on the recommendations in their final report.

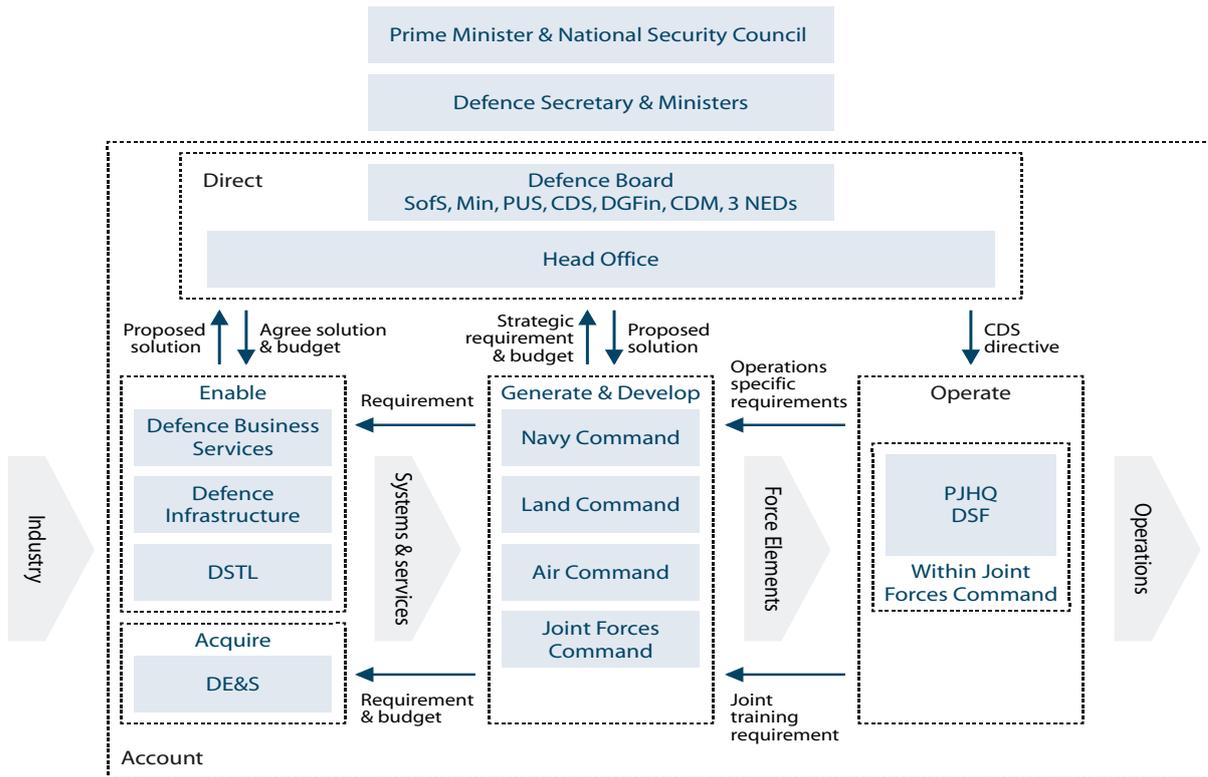
7.5 The Steering Group made 53 detailed recommendations, representing a coherent package of proposals that comprise a new high level operating model. It is based around a number of core themes:

- We must be clear who is responsible and accountable for taking decisions and delivering outputs within the budget they have been set;
- Financial management across Defence should be significantly tightened;
- Some military capabilities have to be integrated on a 'joint' basis;
- The success of the model depends on the people working within it and on the right leadership and behaviours;
- Some enabling functions are best performed consistently and on a collective basis to provide the efficient, effective and professional services that the Department and Defence users need. This underpins the creation of the Defence Infrastructure Organisation and Defence Business Services.

Armed Forces Day 1010



Defence operating model: future



7.6 In combination these represent a future Defence operating model which:

- increases real accountability for delivering Defence outputs within the agreed financial envelope;
- creates a stronger centre, better able to take difficult resource allocation decisions and monitor the delivery of outputs;
- provides a structured framework that sets out clearly which decisions are best taken in the centre and which are best taken in the business, but in all cases makes senior individuals responsible for them, gives them the means and incentives to deliver, and holds them robustly to account;
- establishes much tighter financial management processes to ensure that the need for affordability is recognised and owned at all levels across the Department and that the Board has the increased visibility and assurance necessary to ensure financial control, but ends micro-management;
- balances the strengths of the single Services with the need to build on the joint approach, and disentangles Head Office and joint activity

through establishment of a separate Joint Forces Command; and

- brings transparency, standardisation and best practice to enabling processes, both to ensure efficiency and to ensure that posts are filled with the right individuals, with the right skills, for the right length of time.

7.7 In close coordination with Defence Reform, Bernard Gray, the Chief of Defence Materiel, has taken forward work in parallel to reform the Defence Equipment and Support organisation (DE&S), including implementation of some measures outlined in the Strategy for Acquisition Reform. On 31 May 2011 the Department announced that it would produce a new Defence Materiel Strategy by the end of the year to consider how DE&S can operate differently to become more effective and more efficient. The initial phase will take several months to identify a high level operating model. A second phase will then develop a more detailed design for the future organisation and its implementation.

7.8 Defence Reform is only one component of the substantial transformation needed across defence to deliver an organisation that is affordable and effective. As set out in the SDSR implementation

chapter, the Department has established the Defence Transformation Portfolio (DTP). The 2nd Permanent Secretary and the Defence Operating Board (Transformation) are therefore overseeing not only the implementation of the SDSR, but also Defence Reform, decisions from the current planning round, and other pre-existing change programmes, to ensure that the changes required over the next few years are taken forward coherently and effectively.

7.9 Prior to the formation of the DTP, the MOD governed, supported and assured its most strategically important business change programmes through the Defence Change Portfolio (DCP). Although the DTP will cover a very large number of initiatives, we will continue to govern and assure the delivery of a small number of key transformation programmes following best practice established by the DCP. The performance of these key programmes will be measured by six-monthly Senior Responsible Owner self-assessments against a set of performance indicators (the same set used by the former Office of Government Commerce for management of the pan-government Major Projects and Programmes portfolio).

7.10 Significant progress was made during 2010-11 by the DCP programmes. Head Office Streamlining (which aimed to improve the way the MOD's Head Office worked and reduce it by 25%), Hyperion (which aimed to establish an integrated Headquarters Land Forces at Andover to command and direct the Army) and Defence Electronic Commerce Service (an outsourced service which sought to enable MOD and industry to achieve efficiency savings through electronic commerce services) graduated from the DCP on completion. Defence Training Review Package 2 left, following a decision to cancel the programme and replace it with Project ARTD² Kestrel.

7.11 Other notable events within DCP programmes during 2010-11 included:

- Transition to the new HQ Surgeon General and Joint Medical Command at Whittington completed by the Defence Health Change Programme.
- The move of the HQ Allied Rapid Reaction Corps from Rheindahlen to Innsworth by Project BORONA.
- The Defence Support Review programme joined the portfolio in April 2010.

² Army Recruiting and Training Division.

7.12 The MOD has also contributed to a number of cross-Government Information and Communications Technology (ICT) initiatives, including the Information Assurance (IA) Technical Programme, Public Services Network, National Information Assurance Strategy (now due to be merged with the new Cyber Security Strategy), IA Profession and Skills competence framework, Knowledge and Information Management, and the Sustainable Green ICT programme, where we lead on building sustainability into ICT Procurement. The release of the cross-Government ICT Strategy in March 2011 builds upon aspects of this work but with a focus the Government collectively providing infrastructure, services and applications that can be used by all. The strategy identifies several areas for action, of which MOD provides the lead for three:

- i. Public Services Network (PSN) – Deliver a secure network of networks, operating to common standards, to enable the public sector to develop innovative and more effective ways of doing business.
- ii. Security – In support of PSN, develop an appropriate and effective risk management regime for information and cyber-security risks for all major ICT projects and common infrastructure components and services.
- iii. Green – Publish a Greening Government ICT strategy in line with the Government ICT Strategy and wider carbon reduction policies, setting out how Government will achieve reductions in operational costs and carbon footprints, including the use of collaboration and mobile working technologies.

8. Delivering Defence

The fourth Coalition priority defined in the Structural Reform Plan is:

Meet benchmarking, efficiency and Government sustainable development targets, building on the Defence Reform Unit's review.

Delivering defence has three main components: military equipment, infrastructure (predominantly estates) and people.

Section 1 covers the overall resources available to the MOD.

Section 2 reports on acquisition and support of equipment, as well as logistic support to operations.

Section 3 looks at estates and the the recent establishment of the Defence Infrastructure Organisation.

Section 4 of this chapter covers the essential contribution made by civilians to the delivery of defence. Military Personnel issues are covered in Chapter 6 on the rebuilding the Armed Forces Covenant.

Section 5 sets out the Departmental overview on sustainability, together with an update on safety. Sustainability is firmly embedded in our estates and equipment procurement processes and is also covered in the relevant part of each section.

Section 6 reports on Defence in the public eye.

Section 7 accounts introduction

Section 8 remuneration report



Apache WAH64D helicopter

Section 1: Defence Budget and Spending

Departmental Outturn

8.1 Planned expenditure for 2010-11 was set out in the MOD 2010-11 Main Estimate, which was updated at the Winter and Spring Supplementary Estimates, as voted by Parliament. Provisional outturn for the year is set out in the Public Expenditure Outturn White Paper 2010-11, published this month by HM Treasury. Table 8.1 compares the final performance against the final Estimates approved by Parliament, as reported in the Statement of Parliamentary Supply in the Annual Accounts. It includes Resource Departmental Expenditure Limit (Resource DEL), Annually Managed Expenditure (AME) and non-budget expenditure, but it does not include the other accounting adjustments shown in Note 3.1 of the Annual Accounts.

8.2 Table 8.1 shows an underspend of sum £7.5Bn in Request for Resource 1. The main reason for this is the difficulty in fully identifying at the time of the Spring Supplementary Estimate the impact of decisions made in the SDSR on the value of equipment that was no longer needed. This led to a higher request for resources to cover impairments and write-off costs than was, in the event needed. The other accounting variances reflect the uncertainty and volatility in currency and asset values.

Costs of Operations

8.3 No formal budget is set for the cost of operations. The Department is voted additional resources (Request for Resources 2) to cover the net additional costs of Operations and Peacekeeping Programme Expenditure. Resource expenditure in this category was £2,890m against an estimate of £3,285m. This expenditure includes the costs of operations in Libya incurred to the end of March 2011. The main variance of Estimate against the eventual final outturn is accounted for by lower than expected consumption, equipment support and movement costs, all of which are difficult to forecast given the volatility and unpredictable nature of military operations. Table 8.2 provides a breakdown of Net Additional Costs of Operations.

Reconciliation Between DEL and Estimates

8.4 Table 8.3 provides reconciliation between the outturn shown in DEL and the Parliamentary Estimate. Non-Voted items in this table relate to the cash release of nuclear provisions which is not a Parliamentary control, but which makes up part of the Department's Net Cash Requirement and is contained within the DEL outturn figures.

Modernised Service Family Accommodation



Service accommodation at Woolwich, South East London



Table 8.1 – 2010-11 Parliamentary Controls (£M)

Request for Resources	Final Voted Provision	Net Resource Outturn	Variation
Request for Resources 1 (Provision of Defence Capability)	52,535	44,996	(7,539)
Request for Resources 2 (net additional cost of operations)	3,285	2,890	(394)
Request for Resources 3 (war pensions and allowances)	973	935	(38)
Net Resources	56,792	48,821	(7,971)
Net Cash Requirement	39,557	37,645	(1,912)

Table 8.2 – Net Additional Costs of Operations (£M)

	Iraq			Afghanistan			Libya			Conflict Pool		
	Allocation	Outturn	Outturn	Allocation	Outturn	Outturn	Allocation ¹	Outturn	Outturn	Allocation ²	Outturn	Outturn
	2010-11	2010-11	2009-10	2010-11	2010-11	2009-10	2010-11	2010-11	2009-10	2010-11	2010-11	2009-10
Personnel	8	8	42	224	220	200		0			18	20
Infrastructure	14	10	53	371	336	236		0			9	8
Inventory/Other Consumption	7	4	13	855	784	570		2			0	(1)
Equipment Support	28	21	101	640	605	551		1			1	1
Other Costs	18	10	53	598	503	437		1			32	26
Receipts and Other Income	(1)	(1)	(16)	(57)	(24)	(55)		0			(1)	(1)
Net Interest Payable	0	0	0	0	0	0		0			0	0
Legal Claims Liabilities	7	7	6	3	4	1		0			0	0
Non-Cash Costs (including depreciation)	5	5	47	469	292	390		17			0	0
Total Operating Costs	87	64	299	3101	2720	2230		22			60	53
Total Capital Costs	38	28	44	1390	1054	1491		0			1	1
Total Costs	125	95	343	4491	3774	3821	n/a	22	n/a	61	61	55

[1] There is no allocation for Libya as operations began after the Supply Estimates process had concluded.

[2] The allocation for the Conflict Pool is provided by DFID at a summary level and is not broken into categories.

Reconciliation between Estimates, Accounts and Budgets

8.5 The Department is required to use different frameworks to plan, control and account for income and expenditure. The planning framework uses resource and capital budgets broken down into Departmental Expenditure Limits and Annually Managed Expenditure. These budgets are referred to throughout the Spending Review, Budget Red Book, Pre-budget Report and individual Departmental Annual Reports. Control is exercised through the Parliamentary approval of Supply in the Main and Supplementary Estimates. Some elements of DEL and AME are outside the Supply process. Equally, some expenditure is voted but outside the scope of the budgets. Audited outturn figures are

reported within the Annual Accounts, prepared under the conventions of International Financial Reporting Standards (IFRS). The IFRS adopted for the government sector is 'adapted as necessary for the public sector' as stated in the Government Financial Reporting Manual. Table 8.4 provides a breakdown of reconciliation of resource expenditure between Estimates, Accounts and Budgets.

Table 8.3 – Reconciliation between Estimate and DEL (£M) for RFR1

	Provision	Outturn
Resource Estimate (RfR 1)	52,535	44,996
Annually Managed Expenditure	(2,530)	(779)
SDSR related Annually Managed Expenditure	(12,100)	(6,400)
Non Budget	(422)	(34)
Non Voted	456	243
Gain on derivatives	0	(128)
Less: Consolidated Fund Extra Receipts	0	(0)
Prior Period Adjustment IAS 17	(1,924)	(1,680)
Other Adjustments		4
Resource DEL	36,016	36,221
Capital Estimate (RfR 1)	8,259	8,360
AME	(68)	
Non Budget	(2)	(1)
Gain on Derivatives		(64)
Other Adjustments		
Capital DEL	8,189	8,295

Table 8.4 – Reconciliation of Resource Expenditure between Estimates, Accounts and Budgets (£M)

	Provision	Outturn
Net Resources Requirement (Estimates)	56,792	48,821
Adjustments to include:		
Consolidated Fund Extra Receipts in the OCS		(0)
Other adjustments		4
Prior Period Adjustment IAS 17	(1,923)	(1,680)
Net Operating Cost (Accounts)	54,869	47,145
Adjustments to remove:		
gain on derivative financial instruments		(128)
voted expenditure outside the budget	(252)	148
Adjustments to include:		
other Consolidated Fund Extra Receipts		0
Resource Consumption of NDPB's	(32)	(40)
Non-Voted		253
Other adjustments	202	
Resource Budget Outturn (Estimates Budget)	54,785	47,378
of which		
Departmental Expenditure Limits (DEL)	39,406	39,224
Less IFRS Element of Estimate	(101)	(240)
NDPB DEL	(142)	(142)
Departmental DEL	39,163	38,842
Annually Managed Expenditure (AME)	15,379	8,154

Notes:

1. All figures are rounded to the nearest £m
2. Resource Budget Outturn is subject to finalisation and is therefore subject to minor changes

Core Tables

8.6 Tables for Public Spending and Capital employed are below.

Table 8.5 – Total Departmental Spending

Total departmental spending	2005-06		2006-07		2007-08		2008-09		2009-10		2010-11		2011-12		2012-13		2013-14		2014-15		
	Outturn	Plans	Estimated outturn	Plans	Outturn	Plans	Outturn	Plans	Outturn	Plans	Outturn	Plans									
Resource DEL																					
Section A: Provision of Defence Capability Service Personnel Costs	10,989,775		8,484,781		8,787,857		8,818,819		9,270,207		9,498,313		9,610,297		9,511,540		9,439,080		9,439,080		9,439,080
Section B: Provision of Defence Capability Civilian Personnel Costs	-		2,476,966		2,565,443		2,574,482		2,706,255		2,741,739		2,668,018		2,565,519		2,469,002		2,469,002		2,469,002
Section C: Provision of Defence Capability Infrastructure costs	3,839,918		4,146,905		4,122,192		4,532,692		4,575,357		3,928,484		4,000,124		3,976,951		3,965,038		3,965,038		3,965,038
Section D: Provision of Defence Capability Inventory Consumption	1,957,374		2,020,993		1,851,609		1,922,549		1,851,181		1,418,871		1,444,746		1,436,376		1,432,074		1,432,074		1,432,074
Section E: Provision of Defence Capability Equipment Support Costs	4,979,058		5,140,885		5,195,819		5,428,001		6,080,820		5,520,854		5,621,535		5,588,969		5,572,227		5,572,227		5,572,227
Section F: Provision of Defence Capability Other Costs and Services (see details)	946,696		804,242		906,281		1,379,233		1,175,310		2,656,609		2,840,560		2,824,442		2,812,191		2,812,191		2,812,191
Section G: Provision of Defence Capability Receipts and other Income	-1,432,447		-1,479,442		-1,163,643		-1,423,486		-1,610,843		-1,208,000		-1,164,000		-1,190,000		-1,186,000		-1,186,000		-1,186,000
Section H: Provision of Defence Capability Depreciation and Impairment Costs	6,587,952		6,597,997		7,181,627		7,304,478		7,330,535		8,331,191		8,271,330		8,562,990		9,009,012		9,009,012		9,009,012
Section I: Provision of Defence Capability Cash Release of Provisions Costs	329,657		363,283		436,305		261,164		215,731		240,196		244,579		243,159		242,431		242,431		242,431
Section N: Operations and Peace-keeping Service Personnel Costs	90,672		142,377		162,053		174,953		187,477		183,416		-		-		-		-		-
Section O: Operations and Peace-keeping Personnel Staff Costs	29,439		46,227		52,615		56,804		60,870		35,280		-		-		-		-		-
Section P: Operations and Peace-keeping Infrastructure costs	169,507		233,372		343,360		367,614		366,443		304,043		-		-		-		-		-
Section Q: Operations and Peace-keeping Inventory Consumption	335,737		462,232		645,706		910,319		719,429		687,774		-		-		-		-		-
Section R: Operations and Peace-keeping Equipment Support Costs	277,608		382,203		599,008		847,896		806,205		623,052		-		-		-		-		-
Section S: Operations and Peace-keeping Other Costs and Services	95,714		131,776		134,065		136,399		155,714		621,435		-		-		-		-		-
Section T: Operations and Peace-keeping Receipts and other Income	-8,000		-15,557		-27,710		-28,090		-58,486		-22,697		-		-		-		-		-
Section U: Operations and Peace-keeping Depreciation and Impairment Costs	59,140		54,087		266,467		358,109		385,679		449,729		-		-		-		-		-
Section V: Operations and Peace-keeping Cash Release of Provisions Costs	-		-		-		-		7,379		6,390		-		-		-		-		-
Section Y: Global Pool Resource	-		-		-		-		-		52,253		-		-		-		-		-
Section Z: Non Departmental Public Bodies Costs	62,460		63,316		63,272		238,811		193,386		122,548		-		-		-		-		-
Total Resource DEL	29,310,260		30,056,643		32,122,326		33,860,747		34,301,289		36,191,480		33,537,189		33,519,946		33,755,055		33,755,055		33,755,055

* Figures are not comparable to previous years due to issues with transition to Clear Line of Sight and new Estimates Structure, which have particularly affected the lines relating to War Pensions and Armed Forces Pensions. These issues will be resolved for 2011-12

Table 8.5 – Total Departmental Spending

Total departmental spending										£'000		
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	Plans	Plans
	Outturn	Outturn	Outturn	Outturn	Outturn	Estimated outturn	Plans	Plans	Plans	Plans	Plans	Plans
<i>Of which:</i>												
Pay	11,211,679	11,263,549	11,708,002	11,772,534	12,305,054	-	12,458,748	12,278,315	12,077,059	11,908,082		
Net current procurement ¹	11,450,292	12,137,068	12,847,142	14,268,358	14,367,723	-	14,833,353	12,853,743	12,746,868	12,705,330		
Current grants and subsidies to the private sector and abroad	128,548	141,578	152,664	182,118	168,005	-	-	-	-	-		
Current grants to local government	-	-	-	-	-	-	-	-	-	-		
Depreciation ²	-	-	-	-	-	-	-	-	-	-		
Other	6,519,741	6,514,448	7,414,518	7,637,737	7,460,507	-	8,899,379	8,405,131	8,696,019	9,141,643		
Resource AME												
Section AA: Provision of Defence Capability/Depreciation and Impairment Costs	-	12,256	71,862	-673,425	1,044,065	-	2,566,013	2,843,308	2,994,949	3,126,734		
Section AB: Provision of Defence Capability Provisions Costs	1,477,610	-115,565	493,175	294,790	548,130	-	456,183	457,268	502,210	541,697		
Section AC: Provision of Defence Cash Release of Provisions Costs	-385,340	-413,347	-486,912	-316,031	-281,588	-	-246,586	-244,576	-243,159	-242,431		
Section AD: Movement on Fair Value of Financial Instruments	-	-	-	-1,177,064	202,354	-	218,879	252,627	277,456	299,271		
Section AE: Operations and Peace-keeping Provisions Costs	1,123	6,285	11,695	-324	7,168	-	15,056	-	-	-		
Section AF: Operations and Peace-keeping Cash Release of Provisions Costs	-	-	-	-	-7,379	-	-6,390	-	-	-		
Section AG: War Pensions Benefits Programme costs	4,390	-	-	-	-	-	966,000	960,000	952,000	943,000		
Total Resource AME	1,097,783	-510,371	89,820	-1,872,054	1,512,750		3,969,155	4,268,627	4,483,456	4,668,271		
<i>Of which:</i>												
Pay	-	-	-	-	-	-	-	-	-	-		
Net current procurement ¹	-	-	-	-	770	-	-	-	-	-		
Current grants and subsidies to the private sector and abroad	1,064,746	1,038,574	1,014,616	1,000,400	980,294	-	966,000	960,000	952,000	943,000		
Current grants to local government	-	-	-	-	-	-	-	-	-	-		
Net public service pensions ³	-	-	-	-	-	-	-	-	-	-		
Take up of provisions	1,464,122	-140,134	476,487	292,020	544,479	-	471,239	457,268	502,210	541,697		
Release of provisions	-	-	-	-	-	-	-	-	-	-		
Depreciation ²	-	-	-	-	-	-	-	-	-	-		
Other	-1,431,085	-1,408,811	-1,401,283	-3,164,474	-12,793	-	2,531,916	2,851,359	3,029,246	3,183,574		
Total Resource Budget	30,408,043	29,546,272	32,212,146	31,988,693	35,814,039		40,160,635	37,805,816	38,003,402	38,423,326		

Table 8.5 – Total Departmental Spending

Total departmental spending										£'000		
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15		
	Outturn	Outturn	Outturn	Outturn	Outturn	Estimated outturn	Plans	Plans	Plans	Plans		
<i>Of which:</i>												
Depreciation ²	-	-	-	-	-	-	-	-	-	-	-	-
Capital DEL												
Section J: Provision of Defence Capability Capital Single Use Military Equipment	5,795,417	6,158,123	4,567,698	4,517,457	4,488,004	-	5,718,500	5,784,000	5,719,000	5,156,000		
Section K: Provision of Defence Capability Other Capital (Fiscal)	1,111,440	1,036,456	3,211,714	3,360,643	2,970,173	-	3,211,254	3,419,000	3,658,000	3,935,000		
Section L: Provision of Defence Capability Asset / Estate Disposal Costs	-196,914	-346,839	-	-87,324	-16,386	-	-87,139	-67,000	-186,000	-342,000		
Section M: Provision of Defence Capability New Loans and Loan Repayment	-68,573	2,914	-845	-39,065	6,857	-	4,486	-	-	-		
Section W: Operations and Peace-keeping Capital Single Use Military Equipment	211,243	348,198	526,998	1,148,685	807,357	-	662,594	-	-	-		
Section X: Operations and Peace-keeping Other Capital (Fiscal)	-	-	308,878	77,057	728,431	-	519,652	-	-	-		
Section Z: Non Departmental Public Bodies Costs	-	-	-	-	-	-	2,139	-	-	-		
Total Capital DEL	6,852,613	7,198,852	8,614,443	8,977,453	8,984,436	-	10,031,486	9,136,000	9,191,000	8,749,000		
<i>Of which:</i>												
Net capital procurement ⁴	6,922,037	7,196,789	8,616,139	9,017,369	8,978,430	-	10,027,000	9,136,000	9,191,000	8,749,000		
Capital grants to the private sector and abroad	-	-	-	-	-	-	-	-	-	-		
Capital support for local government	-	-	-	-	-	-	-	-	-	-		
Capital support for public corporations	-75,567	-4,080	-9,949	-39,065	6,857	-	4,486	-	-	-		
Other	6,143	6,143	8,253	-851	-851	-	-	-	-	-		
Capital AME												
Section AB: Provision of Defence Capability Provisions Costs	-	-	-	-	5,083	-	-	-	-	-		
Total Capital AME	-	-	-	-	5,083	-	-	-	-	-		
<i>Of which:</i>												
Capital grants to the private sector and abroad	-	-	-	-	-	-	-	-	-	-		
Net lending to the private sector and abroad	-	-	-	-	-	-	-	-	-	-		
Capital support for public corporations	-	-	-	-	-	-	-	-	-	-		
Other	-	-	-	-	5,083	-	-	-	-	-		
Total Capital Budget	6,852,613	7,198,852	8,614,443	8,977,453	8,989,519	-	10,031,486	9,136,000	9,191,000	8,749,000		

Table 8.5 – Total Departmental Spending

Total departmental spending	2005-06		2006-07		2007-08		2008-09		2009-10		2010-11		2011-12		2012-13		2013-14		2014-15		
	Outturn	Plans	Outturn	Plans	Outturn	Plans	Outturn	Plans	Outturn	Plans	Estimated outturn	Plans									
Total departmental spending¹	37,260,656	36,745,124	40,826,589	40,966,146	44,803,558	50,192,121	46,941,816	47,194,402	47,172,326												
<i>of which:</i>																					
Total DEL	36,162,873	37,255,495	40,736,769	42,838,200	43,285,725	46,222,966	42,673,189	42,710,946	42,504,055												
Total AME	1,097,783	-510,371	89,820	-1,872,054	1,517,833	3,969,155	4,268,627	4,483,456	4,668,271												

¹ Net of income from sales of goods and services

² Includes impairments

³ Pension schemes report under FRS 17 accounting requirements. These figures therefore include cash payments made and contributions received, as well as certain non-cash items

⁴ Expenditure on tangible and intangible fixed assets net of sales

⁵ Total departmental spending is the sum of the resource budget and the capital budget less depreciation. Similarly, total DEL is the sum of the resource budget DEL and capital budget DEL less depreciation in DEL, and total AME is the sum of resource budget AME and capital budget AME less depreciation in AME.

Table 8.6 – Spending by local authorities on functions relevant to the Department

Spending by local authorities on functions relevant to the department	2005-06		2006-07		2007-08		2008-09		2009-10		2010-11	
	Outturn	Plans	Outturn	Plans	Outturn	Plans	Outturn	Plans	Outturn	Plans	Estimated outturn	Plans
Current spending	-	-	-	-	-	-	-	-	-	-	-	-
<i>of which:</i>												
financed by grants from budgets above	22,667,337	23,419,745	24,048,943	25,930,531	26,802,550							
Capital spending	-	-	-	-	-	-	-	-	-	-	-	-
<i>of which:</i>												
financed by grants from budgets above	6,922,037	7,196,789	8,616,139	9,018,972	8,978,430							

The 2010-11 Estimated Outturn is not available at this time for technical reasons. Actual Outturn for 2010-11 is reported in the relevant section of the Annual Accounts

Table 8.7 – Resource Departmental Expenditure Limits excluding depreciation 2010-11

Resource Departmental Expenditure Limits excluding depreciation 2010-11		Original provision †	Final provision	Provisional outturn	Under/Overspend
Ministry of Defence		27,148,451	28,307,847	27,965,854	-341,993

Table 8.8 – Assets and Liabilities in the Statement of Financial Position at year end

<i>Assets and liabilities in the Statement of Financial Position at year end:</i>	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
	outturn (UK GAAP) £m	outturn (UK GAAP) £m	outturn (UK GAAP) £m	outturn £m	outturn £m	Outturn £m	Projected Outturn £m	Plans £m	Plans £m	Plans £m	Plans £m
Assets											
Non-current assets	92,630	95,272	99,263	111,376	119,142	121,893	116,500	118,247	120,021	121,821	123,648
Property, plant and equipment	69,635	71,775	74,601	82,434	89,877	91,653	88,300	89,625	90,969	92,334	93,719
Intangible assets	22,648	22,983	24,163	26,718	27,959	29,134	27,106	27,513	27,926	28,345	28,770
Financial Assets	347	514	500	256	217	224	206	209	213	216	219
Receivables due after more than one year				1,968	1,088	883	887	900	914	927	941
Current assets*	9,405	9,991	9,032	8,581	11,027	11,165	11,377	11,547	11,720	11,896	12,075
Liabilities											
Current Liabilities	- 6,076	- 6,449	- 6,739	- 8,840	- 9,078	- 9,278	- 10,252	- 10,406	- 10,562	- 10,720	- 10,881
Non-current liabilities	- 10,313	- 7,333	- 6,747	- 10,252	- 11,045	- 11,103	- 11,025	- 11,190	- 11,358	- 11,528	- 11,701
Capital employed within main department	85,645	91,481	94,810	100,866	110,045	112,678	106,600	108,199	109,821	111,469	113,141
NDPB total assets less liabilities	339	336	343	613	608	608	608	608	608	608	608
Total capital employed in dept'l group	85,984	91,817	95,153	101,478	110,653	113,285	107,207	108,806	110,429	112,077	113,749

8.7 The MOD is in the process of revising its Administrative Costs regime, so this table is not included at this time. Details of Staff in Post can be found at <http://www.dasa.mod.uk/applications/newWeb/www/index.php?page=48&pubType=1&thiscontent=170&PublishTime=09:30:00&date=2011-05-12&disText=1>. As in previous years, data on regional spend has not been provided.

Section 2: Defence Equipment and Support (DE&S)

Value of New Equipment Delivered

8.8 The DE&S organisation delivered new equipment valued at £8.5Bn which includes £1.1Bn of Urgent Operational Requirements (UOR). Further details on UORs are provided in paragraph 8.14 below. There were 13³ major equipment procurement projects formally accepted into service.

8.9 Total programmed capital expenditure for DE&S in 2010-11 was £7.5Bn. Capital expenditure covers money spent on acquisition less any capital receipts. It is made up of two principal elements:

- Single Use Military Equipment such as warships, military aircraft and armoured fighting vehicles;
- Equipment that can be used for either military or civilian purposes such as transport equipment and infrastructure (docks and airfields), computers, IT and communications, and hospital equipment.

8.10 DE&S was responsible for £91.5Bn⁴ of capital assets, a decrease of £5Bn during 2010-11. Depreciation of assets on operations was £252.5M. Items of equipment procured through the UOR process were depreciated in the same way as other assets but the expected life was adjusted to reflect the harsh environment in which they were operated. DE&S also owns the majority of non-property assets and equipment under construction, which decreased by 16% from £18.6Bn to £15.6Bn during the year.

Wolfhound, part of the Tactical Support Vehicles Group



3 The 13 major equipment procurement projects are; Joint Command & Control Support Programme (JC2SP) – Application Migration Project, ASTUTE Boats 1 to 3, BOWMAN – Capability Release 1.5, T45 DESTROYER, General Service Respirator (GSR), Artillery Fuzing System (AFS), HILDING, C17 (7th Aircraft), Advanced Jet Trainer – Ground Based Training Environment, WATCHTOWER (Enhanced Computer Network Defence), STANO Systems Future Integrated Soldier Technology, Naval EHF/SHF SATCOM Terminals, and SKYSIREN.

4 Figure includes Intangible Non-Current Asset Manager, Single Use Military Equipment (SUME), Plant & Machinery, IT and Comms Equipment, Transport and Assets Under Construction

Key contracts and achievements

8.11 For the Royal Navy:

- The new Type 45 destroyers entered service with two of the six ships in the class, HMS DARING and HMS DAUNTLESS, accepted into service in July and November 2010 respectively. HMS DIAMOND and HMS DRAGON are undergoing sea trials and HMS DEFENDER is being fitted out. The last of the six Type 45 destroyers, HMS DUNCAN, was successfully launched on the Clyde;
- The first of seven Astute class submarines, has entered service. The second boat, HMS AMBUSH was launched in December 2010 and sea trials are expected to commence in the next 12 to 18 months;
- 'Goliath' – The largest Crane in the UK with a height of 68 metres, that will assemble the Royal Navy's Queen Elizabeth class aircraft carriers, arrived at Rosyth on the 3rd March from China. The last four modules to make up the first 6000 tonne lower block of HMS QUEEN ELIZABETH are underway, less than 12 months after the first two modules made the journey from Babcock's yard in Appledore.

8.12 For the Army:

- The Army's newest heavyweight protected vehicle, Wolfhound, is now operational in Afghanistan. The six-wheeled Wolfhound joins Coyote and Husky as the biggest of the Tactical Support Vehicle family, giving troops increased protection as they support missions in high-threat areas. In addition, a £180m contract was signed with Force Protection Europe to build 200 Foxhound vehicles with the first batch intended to be delivered for training later this year;
- The UK's newest protected all-terrain vehicle has been used on operations in Afghanistan. Around 30 of the powerful and versatile new Warthog vehicles have arrived on the front line and are being used on operations. The first of a contract for around 100 new, improved Mastiff 3 troop-carrying patrol vehicles have also been despatched to Afghanistan;
- Future Infantry Soldier Technology first tranche was delivered ahead of schedule. This £187m project has been delivered into training in preparation for deployment on operations;
- A six-year programme delivering thousands of night vision systems for UK troops has been accelerated to less than 12 months. The

Dismounted Soldier Systems team delivered the last 100 of 11,000 Head Mounted Night Vision Systems in December. They have been issued to deployable units and training establishments across all three Services.

8.13 For the RAF:

- Typhoon, the UK's largest procurement programme to date, has passed the significant milestone of 100,000 flying hours across the six Air Forces who operate the leading edge multi-role combat aircraft. The first operational release of enhanced Paveway II precision guided bomb from a Typhoon aircraft has been achieved. In March 2011, Typhoon aircraft were deployed overseas for the first time on contingent operations in support of the coalition plan to enforce United Nations Resolution 1973 on Libya.
- The required number of simulated flight-cycles on a full scale test airframe have been completed to achieve civil type certification of the A400M by the European Aviation Safety Agency. The test programme is required to simulate flights at least one year ahead of the actual operations performed by the aircraft. The aircraft's arrival into service alongside the C-17 and C-130J aircraft will provide the RAF with a four-aircraft transport fleet operating simultaneously from 2015 until 2022 when the C-130J is planned to leave service;
- The Prime Minister welcomed the seventh C-17 transport aircraft to the RAF which, entered service two months early on 14 January 2011. Arrival of this aircraft will bolster the airbridge between the UK and front line operations;
- The second of 14 aircraft in the Future Strategic Tanker Aircraft (FSTA) project for the RAF has made its debut flight in military configuration. The flight from Airbus Military's base near Madrid on 26 October lasted two hours and the aircraft now joins the first FSTA in a comprehensive flight testing programme. The FSTA programme continues to run on schedule, with the first aircraft ready for delivery to the RAF this Autumn;
- All eight Chinook Mk 3 aircraft were delivered by the end of 2010 . All Chinook supporting operations in Afghanistan have been fitted with more powerful Honeywell 714A engines two years earlier than planned. In addition, flight testing of the first Chinook Mk4 aircraft for the RAF has taken place. The aircraft is the first of 38 Boeing Mk2/2A helicopters to be modified into the new Mk4/4A configuration under Project Julius;

- The first UK KC135 tanker aircraft was inducted in December 2010 for conversion to UK Rivet-Joint-18 which will replace the Nimrod RI to sustain the UK's Airborne Signal Intelligence capability.

8.14 Pan Defence:

- General Service Respirator, which has replaced the in-service S10 respirator, providing enhanced levels of protection, equipment compatibility and reduced user burden, entered service in August 2010;
- SKYSIREN entered service in March 2011. This provides an enhanced capability for the dissemination of information to MOD tri-Service assets and platforms deployed across the world;
- An upgraded information management software system under the Joint Asset Management Engineering Solutions programme has been launched which will allow effective management of millions of assets, resulting in improved assessment of availability, location, and configuration;
- A £76m contract with Agusta Westland will see a new training centre for the Army and Navy Lynx Wildcat helicopter. The training centre, part of an integrated training package, will be at the Royal Naval Air Station Yeovilton and will train Army aircrew, maintainers and ground crew starting in early 2013, with training for Royal Navy aircrew and maintainers starting early in 2014;
- Boeing Defence UK has been awarded a contract as the partner for Future Logistic Information Services which will deliver operationally essential logistic information across defence. It means current logistic information services will be delivered in a more effective and efficient manner, while at the same time providing the transformational capability which defence needs. The new contract, which has an estimated value of £800m over eleven years, will realise financial efficiencies of more than £160m over the life of the contract;
- During the past three years, the Defence Information Infrastructure programme has been delivering a single IT information infrastructure across defence, replacing around 300 independent information systems. This has provided a standard, consistent platform for defence applications and delivered a more effective, modern environment for the sharing of information and the transmission of messages.

Urgent Operational Requirements (UORs)

8.15 UORs are pieces of equipment that are required urgently for a specific military operation. Where the requirement is new and unforeseen, and specific to a particular operational theatre, it will be funded from the Government Reserve rather than the Defence budget. Over £6.7Bn of expenditure has been approved through the UOR process since 2001. Of this, over £4.9Bn has been for emerging requirements for Afghanistan. In 2010-11, the MOD successfully delivered 79 UORs.

8.16 For 2010-11, the Department agreed an estimate with HM Treasury for Reserve expenditure on UORs of up to £850m. The final outturn against this estimate was £583m, with an additional £208m spent in-year on equipment previously authorised and equipment for the Counter IED campaign. For financial year 2010-11, the Treasury agreed to provide up to £150m of additional funding for Urgent Defence Requirements. This equipment is expected to have a longer term value for Defence and so any money spent will be paid back in full from the Defence budget in financial year 2012-13. The final outturn in Financial Year 10-11, based on the eventual operational demand, was £50m.

8.17 UOR performance has exceeded target with 95% of UORs meeting their Equipment Delivery Dates or being delivered early. In total, the 79 UORs were delivered some 179 months earlier than planned. This included a UOR for the modification of 12 Lynx Mk9a aircraft, which allowed deployment to Afghanistan 18 months from commencement of upgrade programme. Other UORs successfully delivered included improved base protection and Counter Improvised Explosive Device capability.

8.18 On top of this, we also signed a £180m contract for 200 new FOXHOUND protected patrol vehicles in 2010-11. These will be procured through the UOR process, funded in large part from the Treasury Reserve, with the MOD contributing to the overall buy, in recognition of the vehicle's wider utility. Based on current plans, we expect the first vehicles to be delivered to training in late 2011, with the first vehicles arriving on operations in 2012.

Sustainable Procurement

8.19 We have continued to make good progress on embedding sustainable development in our acquisition processes. 84% of our Key Suppliers disclosed their greenhouse gas emissions during 2010. We will continue to work with them during

2011 to establish a firm baseline for reducing future emissions, water consumption and waste in line with the new Greening Government Commitments. In addition, we have established a baseline for our operational energy consumption. This averages around 1.2Bn litres of fuel per year, which at current prices costs around £450m. We have identified this as a priority area for achieving savings.

Logistic Support to Operations

8.20 Rotary wing support to operations remains critical to success in Afghanistan and the increased numbers of helicopters and flying hours required have been delivered. The new Lynx Mk9a has been delivered and provides a significant performance increase over its predecessor enabling year-round operations in Afghanistan. The Department continued to take significant steps in many other areas. These have included further improvements to Counter IED capabilities (particularly intelligence and analytical capability), an improved Dismounted Close Combat equipment package that will enable troops to train with equipment prior to deployment, and increased funding for intelligence, surveillance, target acquisition and reconnaissance capabilities, including the doubling of Reaper unmanned aerial vehicles. The deployment and sustainment of UK forces and equipment to the Mediterranean region to support Op ELLAMY has required co-ordinated support from across the DE&S, including the movement of personnel, assets and supplies; establishment of postal, fuel, food and transport personnel and commercial contracts; and rapid work to provide additional munitions.

Movements

8.21 The standard pattern of troop movement to and from Afghanistan includes a deployment and periods of rest and recuperation; mid-tour and prior to return home. This amounts to approximately 130,000 individual movements per year. Passenger movements still rely heavily on Tristar aircraft with additional commercial charter and C-17 support to add resilience. Air freight is delivered through a combination of military and commercially chartered resources. Approximately 16,000 tonnes of air freight capacity was provided in support of Afghanistan, including air freight charter. In Financial Year 2010-11, the cost of air charter in support of Afghanistan was around £200m, approximately 90% of the total Defence requirement for commercial airlift. Surface routes also continued to play a significant role in the delivery of supplies to Afghanistan, with approximately 26,000 tonnes of routine sustainment traffic moving by the surface line of communication, delivered primarily by commercial means but

supplemented by the MOD Strategic Ro-Ro ferries, 'Sail-Fly' via Cyprus or UAE, and the successful trial of a rail route from the Baltic coast to Afghanistan via Russia and the Central Asian Republics. Recent work in support of Op ELLAMY has seen the rapid development of lines of communication for passengers and freight to Italy and Malta to support air and maritime operations.

Disposals

8.22 The Disposal Services Authority (DSA) achieved £84.3m in gross sales during 2010-11. Major activities included the completion of the refurbishment package for the two Hunt Class Mine Counter Measures vessels, former HM Ships COTTESMORE and DULVERTON. Since refurbishment both have been delivered to the Lithuanian Navy with a total in-year gross sale of £25m.

8.23 The DSA successfully negotiated the sale and handover of HM Ships LEEDS CASTLE and DUMBARTON CASTLE (Castle Class Offshore Patrol Vessels) for £2.45m and HMS ROEBUCK for £4.4m, to the Bangladesh Navy. All 3 vessels have since sailed to Bangladesh.

8.24 The DSA has sold RFA OAKLEAF for £1.3m and HMS INVINCIBLE for £2m to Leyal Ship Recycling in Turkey.

Section 3: Defence Infrastructure

8.25 The MOD is one of the largest landowners in the UK, with an estate of some 240,000 hectares, about 1% of the UK mainland. Some 80,000 hectares of this comprise a varied built estate including naval bases, airfields, living accommodation for military personnel, scientific facilities, storage and distribution centres, communications facilities and offices, making the MOD the UK's largest property manager. Reflecting the long history of the Armed Forces, the estate contains a substantial number of listed buildings. The rural estate (some 160,000 hectares) comprises mainly training areas and ranges, on undeveloped land which is in places of particular environmental or archaeological significance. The MOD has rights to use a further 125,000 hectares in the UK, mainly for training. In addition the MOD manages an overseas estate comprising the garrisons and training facilities in Germany, Cyprus, the Falkland Islands and Gibraltar, as well as facilities in Ascension Island, Belize, Brunei, Nepal, Singapore and the United States. The Armed Forces regularly use major training facilities in Canada, Cyprus, Germany, Norway, Poland and Kenya. As at 31 March 2011 estate related Defence assets were valued at some £24 Bn.

Table 8.9 – Project SLAM Delivery

	2003/4	2004/5	2005/6	2006/7	2007/8	2008/09	2009/10	2010/11
Target	1000	1640	2500	1500	2100	2300	1250	2100
Cumulative Target	1000	2640	5140	6640	8740	11040	12240	14340
Delivered	150	1862	3570	2207	2008	2719	1442	2542
Cumulative Delivery	150	2012	5582	7789	9797	12516	13958	16500

Table 8.10 – TLB Funded and PFI Delivery

	2003/4	2004/5	2005/6	2006/7	2007/8	2008/09	2009/10	2010/11
Target	1500	4300	5300	5800	5550	4150	3630	3018
Cumulative Target	1500	5800	11100	16900	22450	26600	30230	33248
Delivered	2765	3749	1969	3615	4897	5191	4367	3312
Cumulative Delivery	2765	6514	8483	12098	16995	22186	26553	29865

Move to the new Defence Infrastructure Organisation

8.26 The last six months has seen the transformation of Defence Estates into the new Defence Infrastructure Organisation (DIO) with effect from 1 April 2011. DIO will strategically manage the estate and centralise MOD management of infrastructure. This initiative is compatible with wider government initiatives and will achieve significant cost reductions, improve estate utilisation and drive forward further rationalisation.

Regional Prime Contracts

8.27 Maintenance of the majority of the MOD's built estate across England, Scotland and Wales has been provided through five Regional Prime Contracts (RPC). These have cost some £394m a year and have driven the introduction of collaborative working, supply chain management and incentivisation into the delivery of estate services. Financial reductions last year have required the MOD to renegotiate all 5 RPC contracts, resulting in a reduction of over £50m pa in programme costs. All contracts were aligned to a basic standard of delivery that provides a safe and legal estate.

Next Generation Estates Contract

8.28 The last 12 months have seen the first of the new Regional Prime contracts for Scotland, Northern Ireland and National Housing advertised to Industry with In Service Delivery (ISD) due by April 2013.

The remaining contracts are due to be advertised through 2011 with final ISD in April 2014.

Sustainability of the Estate

8.29 Defence Estates has continued to lead the way for MOD energy efficiency and Sustainable Practices and has exceeded the Government's 12.5% carbon reduction target on the defence estate relative to FY 99/00 levels by achieving a 19.4% reduction. Reductions in water consumption across the estate continue with a reduction of 28% achieved against a 25% target against the 04-05 baseline. MOD has met the Government target to achieve 95% of its Sites of Special Scientific Interest in favourable or recovering condition, and has reduced the number of listed buildings at risk on the estate from 28 to 23. The MOD exceeded the Government Flexible Framework targets for embedding sustainable development including halving waste to Landfill Charters that have been signed by all estate key suppliers. The MOD also continues to lead across Government on its approach to building an estate that is resilient to extreme weather events and future climate fluctuations. It focuses on creating a risk register to inform short to medium term estate maintenance, Business Continuity and long term strategic planning. Its Climate Impact Risk Assessment Method is currently being rolled out to the most critical sites to ensure defence outputs are not compromised.

8.30 The MOD remains fully committed to being a national leader in sustainable procurement for construction and estate management services. The MOD exceeded the Government Flexible Framework Level 3 target for embedding Sustainable Development (SD) principles into estate procurement, attaining levels 4 and 5 in most categories. The MOD is embedding SD into the next generation of estate contracts by including material in the requirement documents, advertisements and tendering stages.

Defence Training Estate

8.31 The Defence Training Estate (DTE) organisation supplies the majority of military training for the Armed Forces. The last year was demanding with a high operational tempo. Since the creation of DTE in April 2006 there has been a major reorganisation of the Departments' training estate under the Defence Estate Training Rationalisation Study. This resulted in the transfer to DTE of training estate in Germany and Northern Ireland as well as additional Army, Royal Navy and Royal Air Force estates in the UK. This expansion is now in its final phase with the adoption of training areas in other parts of the world, notably Canada, Belize and Kenya, as well as Adventurous Training facilities and the management of military training on private land in the UK. Placing all of the Department's training estate under a single command is to enable a more flexible, efficient and cost efficient use of this vital resource.

Overseas Estate

8.32 DIO continues to provide Commercial and Facilities Management staff in theatre, and rebased support from UK, to support operations in Afghanistan. In Germany, a new five year contract has been awarded to deliver hard Facility Management including reactive, statutory and grounds maintenance services; on Vesting Day (8 Aug 2011) some 600 MOD staff will transfer to the new contractor.

Estates Disposals

8.33 Total receipts of £44m were achieved during FY 2010-11.

Future Estate

8.34 The SDSR set out the Government's aim of returning UK forces from Germany by 2020. This will mean accommodating some 18,000 service personnel and their families in the UK. The Department subsequently set in hand a broad review of the Department's future basing and estate rationalisation plans in order to determine how the return from Germany could best be achieved, whilst also delivering significant receipts from the disposal of surplus estate holdings.

Single Living Accommodation

8.35 There has been significant investment in Single Living Accommodation modernisation through Private Finance Initiatives, Project SLAM, and other MOD funded projects. The modern standard for Single Living Accommodation for junior ranks provides single en-suite bed-sitting rooms configured in either six or eight person flats or hotel layout supported by additional communal space and utility rooms with laundry and kitchenette facilities. There are similar scales for more senior personnel. Over the last eight years the MOD has modernised some 46,000 bed-spaces of which 5,850 were delivered in 2010-11. A detailed break down of delivery in tables 8.8 and 8.9.

Service Family Accommodation

8.36 The MOD controls 67,000 properties worldwide. Of these some 49,000 properties are in the UK and some 18,000 properties are on the overseas estate with the majority being held in Germany. Service Family Accommodation is owned in a variety of ways. In Germany almost all is leased from either the Federal Government or private owners, as is the case in remote overseas locations. However, in the other overseas bases most is MOD owned. In England and Wales, most properties are leased from Annington Homes Ltd (AHL). AHL own 39,750 properties in England and Wales that were purchased from the MOD in 1996 and leased back for a period of 199 years. Most of the properties in Scotland and Northern Ireland are owned by the MOD.

8.37 Standard for Condition is used to determine the overall physical state of SFA, with Standard 1 being the highest and Standard 4 the lowest. Some 96% of the UK housing stock is in Good Condition (that is Standard 1 and 2 for Condition) and has been assessed by the NAO as meeting or exceeding the Government's Decent Homes standard. In the UK there are only some 1,260 properties at Standard

3 (which will not be allocated from January 2012 onwards) and only 222 properties at Standard 4 (which are no longer actively allocated).

8.38 A Management Margin is required to support the annual rotation of reassigned personnel, in particular peak demand in the late summer before the new school year, as well as periodic repair and upgrade of properties. The proportion of empty properties in the UK has been driven down from an historic high of 21% in May 2008 to 12.4% in Mar 2011. This helps the Department to target investment where it is needed most and will deliver the greatest long term benefit.

8.39 Over £62m was allocated for the upgrade and improvement of, UK property in Financial Year 2010-11. This enabled some 800 properties to be upgraded to Standard 1 for Condition, with a further 4,000 benefiting from other improvements such as new kitchens and bathrooms, double glazing and insulation.

8.40 The last FY has seen the MOD manage some 15,000 moves in and 14,000 moves out of SFA in the UK. This reflects increasing demand for publicly funded properties. Keen to provide greater transparency for families seeking accommodation, the MOD is considering the introduction of an on-line application process whereby personnel can view available properties and express their preference for one that they wish to occupy.

Section 4: Civilian Personnel

8.41 Civil Servants have a distinctive role in Defence. The challenge for Civil Servants today is to continue to help the Department deliver in support of operations in Afghanistan, Libya and elsewhere while ensuring proper control over the management of resources of all kinds, on behalf of Ministers and the Permanent Secretary as Accounting Officer.

8.42 Civilians also have an important role as the result of our Parliamentary democracy. Like all Departments of State, the MOD has a fundamental duty to support our Ministers not simply on questions of finance but on all issues for which they are responsible.

8.43 The final distinctive Civil Service role is maintaining civilian and democratic control of the Armed Forces. Civil and democratic control is not control by civil servants but by Ministers. It is the responsibility of civilian staff to ensure that Ministers have full visibility of issues and the opportunity to take decisions. Civil Servants have a duty to support

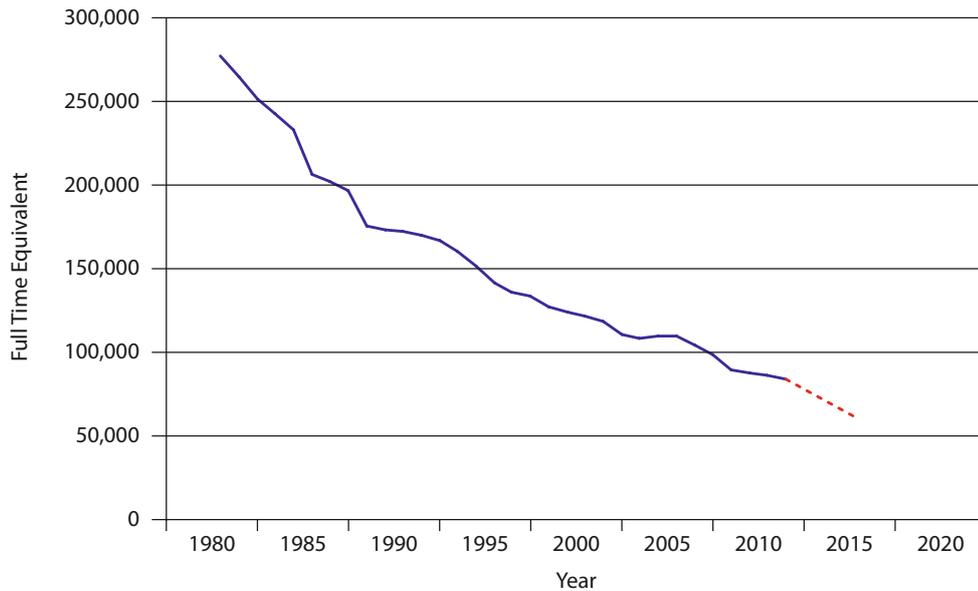
Ministers to ensure that the proper constitutional balance is maintained.

8.44 MOD civil servants play a vital role directly supporting the success of military operations. Civil servants deploy alongside the military to operational theatres, undertaking a range of important roles in support of the military mission; roles including policy advisers, finance officers, intelligence analysts, scientific advisers, engineers, and police officers training the Afghan Police forces. All of those civilians who deploy are volunteers and great care is taken to ensure that they are properly prepared and supported at each stage, before they go, while they are deployed, and after they return. This includes robust risk assessment and management processes, guidance and support for families, assistance re-integrating into the workplace, and championing their contribution amongst the rest of the Defence community.

8.45 Civilians also provide direct support in a range of UK-based roles, from advising Ministers to the procurement of urgent operational equipment needs. We take great care to ensure that highly skilled civil servants provide the fullest support to our armed forces in combat and peacekeeping operations overseas.

8.46 Across Defence MOD prioritises civilian support according to where the need is greatest. Provision of direct support to military operations rightly takes precedence over all other work. In 2010 we created a capability to focus and manage civilian support to the Main Effort. Civilian resources are diverted depending on the Government's emerging Defence priorities, encompassing not just Afghanistan, but emerging new crises or operations as well as important non-operational requirements such as the implementation of the SDSR. As the UK drew closer to involvement in the no-fly-zone in Libya in March 2011, for example, we were able to provide support to the teams handling this effort within four hours of the need being identified. We have continued to provide increased levels of highly-skilled support as the crisis continued. This ensured that military commanders and the Cabinet were fully supported with appropriate policy advice and briefing at all stages of the crisis.

Figure 8.2 – MOD Workforce – Full Time Equivalent Numbers – 1 April Date Point



Workforce Numbers

8.47 The MOD civilian workforce has significantly reduced in size over the past thirty years, and will continue on a downward trend post-SDSR. In 1980, the workforce consisted of 276,200 full time equivalents, reducing to figure 8.2 in 2011.

8.48 As a result of the SDSR, the current civilian workforce will reduce to around 60,000 by 2015.

8.49 Additional personnel related information can be found at: <http://www.mod.uk/DefenceInternet/AboutDefence/CorporatePublications>; and statistical information including staff numbers can be found at: <http://www.dasa.mod.uk/>. The MOD publishes details of its management of civilian sick absence on its website – details can be found at: <http://www.mod.uk/DefenceInternet/AboutDefence/CorporatePublications/PersonnelPublications/Welfare/SicknessAbsenceAnnouncement.htm>

Civilian Voluntary Early Release Scheme (Vers) 2011

8.50 A voluntary early release scheme (VERS) for MOD civil servants was launched at the end of February in response to the outcome of the SDSR announcement. The VERS is a first step towards the Department achieving the 25,000 civilian staff reductions required by 31 March 2015.

8.51 Voluntary early release for 2011 was open to all permanent UK-based civilians currently employed by the MOD, excluding staff employed in the Trading Fund (industrial) Agencies and by the United States Visiting Forces. By the closing date of 31 March; 13,439 applications were received. It must be stressed that this is not indicative of final releases, but applications.

8.52 A decision on what further action may be required to achieve the full 25,000 reduction will be taken later in the year in the light of the take-up of the initial scheme and the outcome from Defence Reform and other efficiency programmes that are ongoing.

Recruitment

8.53 As part of the Government’s announcement to make £6.2Bn of efficiency savings, Civil Service recruitment was frozen in June 2010. The freeze impacts civil service recruitment across Government departments and agencies, with only limited exceptions for frontline and business critical staff, requiring agreement from the Secretary of State or (where appropriate) an Agency Chief Executive. The tables below show civilian recruitment in 2010-11 and the exceptions.

Table 8.11 – Civilian Recruitment in 2010-11

	Non Industrial	Industrial
Total Number of Staff Recruited	960	270
Number and Percentage of Women Recruited	420 44.0%	60 21.5%
Number and Percentage of Ethnic Minorities Recruited ³	40 5.9%	10 3.5%
Number and Percentage of People with Disabilities Recruited ⁴	20 2.1%	~ ⁵ ~ ⁵

Source: DASA (SMG)

1. Data supplied by DASA, recruitment data based on personnel directly recruited by Department or through the CAPITA (RAS)
2. The recruitment statistics shown are for all permanent and casual civilian personnel including Trading Fund staff. No recruitment information is available for Royal Fleet Auxiliary or locally Engaged civilians.
3. Percentage of staff recruitment is based on known declarations of ethnicity and excludes staff with unknown or undeclared ethnicity.
4. Percentage of staff recruitment is based on known declarations of disability status and excludes staff with unknown or undeclared disability status.
5. ~ is equal to all strengths of less than ten or percentages based on strengths of less than ten.
6. All figures are on a Full Time Equivalent basis.
7. All figures have been rounded to meet the Freedom of Information requirements and protect confidentiality.

Table 8.12 – Permitted exceptions to the Civil Service Commissioners Recruitment Principles

	Non Industrial	Industrial
Total exceptions	309	31
Appointments of individuals with highly specialised skills up to 2 years	2	0
Secondments of up to 2 years	74	0
Transfer of staff with their work (TUPE and not TUPE)	122	0
Transfer of individuals into the Civil Service	25	0
Casual/temporary appointments	86	31
All other categories	0	0

Table includes 64 exceptions made by the Trading Funds.

8.54 In accordance with our obligations to the Civil Service Commission Principles on Recruitment Table 8.12 show the use of permitted exceptions in 2010-11 to the principles of fair and open competition and selection on merit.

Disabled Persons Employment Policy

8.55 It is MOD Policy that any form of unfair discrimination or harassment on the grounds of an individual's gender, race, disability, sexual orientation, religion or belief, marital status, age, non-standard working pattern or any other difference, is totally unacceptable and not to be tolerated in the workplace. Information on the MOD's disabled persons employment policy is published on the MOD website at: <http://www.pppaservices.qinetiq-tim.com/https@knowledge.chris.r.mil.uk/pppa/index@page=viewtask&id=ta112.htm>

Section 5: Safety and Sustainability

Safety

8.56 The safety of our military and civilian personnel is of paramount importance and can be seen across Defence. We cannot be complacent about safety and despite pressure on resources across the Department, we continually strive to improve and develop our health and safety processes, our organisational culture and our individual behaviours. Over the past year the Department has continued to further develop and demonstrate our commitment to safety including the establishment of the Military Aviation Authority (MAA) in response to the recommendations of the Nimrod Review undertaken by Charles Haddon-Cave QC. It is an independent and autonomous organisation responsible for regulating all aspects of Air Safety across Defence, ensuring the safe design and use of military air systems. More details on the MAA can be found at: <http://www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/AirSafetyandAviation/MAA/MilitaryAviationAuthoritymaa.htm>.

8.57 The Nimrod Review⁵ recommendations also have resonance for safety functions beyond the air domain and the MOD continues to assess the wider implications for the Department. This includes examining a range of issues such as interfaces with industry, safety culture, the state of non aviation internal safety regulation, and clarification of the delegation of responsibilities. This work will take time but the Department will continue to endeavour to make real and enduring improvements in safety management and behaviours.

Safety Strategy

8.58 The Safety Strategy has been developed to provide more focus on delivering improvements in safety management and performance in the longer term. It incorporates the following strategic goals: a learning organisation; demonstrable leadership and continuous improvement; clear competence and performance measurement requirements; understanding and managing hazards and risks; recognising, influencing and complying with legislation and policy; and involving people and effective communications. A delivery plan has been produced which, as a key part of the strategy, contains specific and measurable actions aimed at achieving sustainable reductions in fatalities and injuries to our military and civilian personnel.

Avoiding Fatalities

8.59 There were 12 deaths related to health and safety failures in 2010-11, some of which are still under investigation. This is in comparison to 11 in 2009-10. We continue to work hard to reduce and minimise the number of fatalities as a result of accidents.

Minimising Major Injuries

8.60 1,260 major injuries⁶ were reported in 2010-11 compared to 1,178 in 2009-10. We believe this increase in major injuries is in part due to the better understanding and reporting of incidents and further work is underway to analyse any potential trends or issues. We continually strive to reduce the number of major injuries and our aim, reflected in the Safety Strategy, is for a 10% reduction in major injuries by 2013-14.

5 The Nimrod Review. An independent review by Charles Haddon-Cave QC into the broader issues surrounding the loss of the Royal Air Force Nimrod MR2 aircraft XV230 in Afghanistan on 2 September 2006. Published 25 Oct 2009

6 The MoD uses the Health & Safety Executive's definition of major injury as defined under RIDDOR (The Reporting of Injuries, Diseases and Dangerous Occurrences Regulations). Which can be found at <http://www.hse.gov.uk/riddor/index.htm>

Assurance and Accountability

8.61 Safety in the MOD is monitored by the Defence Environment and Safety Board (DESB) whose role is to provide critical review and assurance upwards to the Defence Audit Committee and the Defence Board. The DESB annual assurance report provides a detailed summary of the Department's current position with regard to safety. In February 2011 the DESB noted that there has been little evidence of improvement over the past 12 months, but that current initiatives at corporate and TLB level have the potential to improve the assurance rating. It therefore agreed to provide the Defence Audit Committee with a "Limited Assurance" against the management of Safety, Environmental Protection and Sustainable Development in 2010.

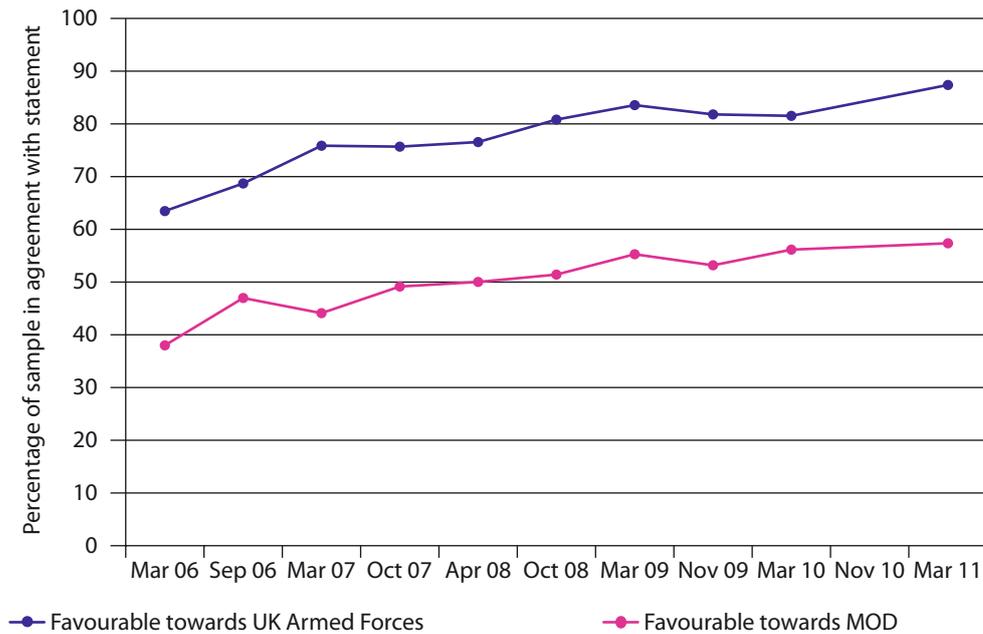
Sustainable Development

Sustainable Development and Defence

8.62 Global environmental, social and economic pressures pose real threats to Defence's ability to meet its strategic objectives. For example, climate change, natural resource depletion, water scarcity and energy and resource security are all potential catalysts for increased unrest or armed conflict. These challenges will also present fresh demands on our people, infrastructure and equipment.

8.63 Embracing Sustainable Development will help ensure that Defence is prepared for these challenges and that we play our part in reducing the severity of any environmental, social or economic threats to Defence capability in the first place. Other important benefits to Defence include reduced costs; saved lives; more resilient Defence capability and improved reputation.

Figure 8.2 – External opinion of the Armed Forces and MOD 2006-11⁴



8.64 The Sustainable Development Strategy is a sub-strategy of the Strategy for Defence. The 2008 Sustainable Development Strategy has recently been revised and has been replaced by a new 2011-2030 strategy.

8.65 The new Strategy will also ensure that Sustainable Development principles become an integral part of all other Defence strategies, policies, decision making processes, programmes, projects, activities and behaviours. This will drive further progress in:

- Reducing our reliance on fossil fuel;
- Reducing waste production and increase reuse and recycling.
- Reducing water consumption;
- Engaging suppliers in our sustainability agenda;
- Ensuring that defence decision making process fully consider and respond to environmental, social and economic impacts, threats and opportunities.

Sustainable Development Performance

8.66 In 2010 the MOD met or exceeded the majority of Government SD targets. We reduced carbon emissions from our estate by 19.4% (relative to 1999-2000 levels) against a target of 12.5%. We have also continued to make good progress against a Government-wide Sustainable Procurement Flexible Framework, produced a sustainable ICT policy and are leading on developing a Government wide greening ICT strategy. Further details of the MOD's performance can be found in the Procurement, Infrastructure, Safety, Civilian and Service Personnel sections of this report. MOD's SD Annual Report 2009-10 also contains details of performance against SD targets.

8.67 Our strong performance has been based on making SD a priority. SD is now one of seven Defence priorities in the MOD Business Plan 2011-15 and the SD Strategy is a sub-strategy of the Strategy for Defence. The 2008 SD Strategy has recently been revised and has been replaced by a new 2011-2030 strategy.

8.68 The new Strategy will also ensure that SD principles become an integral part of all other Defence strategies, policies, decision making processes, programmes, projects, activities and behaviours. This will drive further progress in:

- Reducing our reliance on fossil fuel;

- Reducing waste production and increase reuse and recycling;
- Reducing water consumption;
- Engaging suppliers in our sustainability agenda;
- Ensuring that defence decision making process fully consider and respond to environmental, social and economic impacts, threats and opportunities.

Section 6: Defence in the Public Eye

8.69 The work of the MOD and the Armed Forces is rarely out of the public eye. The MOD works hard to ensure that Parliament, the public, the media and other stakeholders understand our role, what we do, and why we do it. The results of independent public opinion polling conducted on our behalf show that the British population continues to be highly favourable towards the UK Armed Forces. The proportion of favourable ratings for the MOD and the Armed Forces has continued to improve steadily and is now at its highest level since polling began.

Table 8.13 – External opinion of the Armed Forces and MOD

Favourable ratings for Armed Forces			
March 2011	March 2010	March 2009	April 2008
88%	82%	84%	77%
Unfavourable ratings for the Armed Forces			
3%	4%	2%	4%
Favourable ratings for MOD			
March 2011	March 2010	March 2009	April 2008
57%	56%	55%	50%
Unfavourable ratings for MOD			
15%	11%	9%	12%

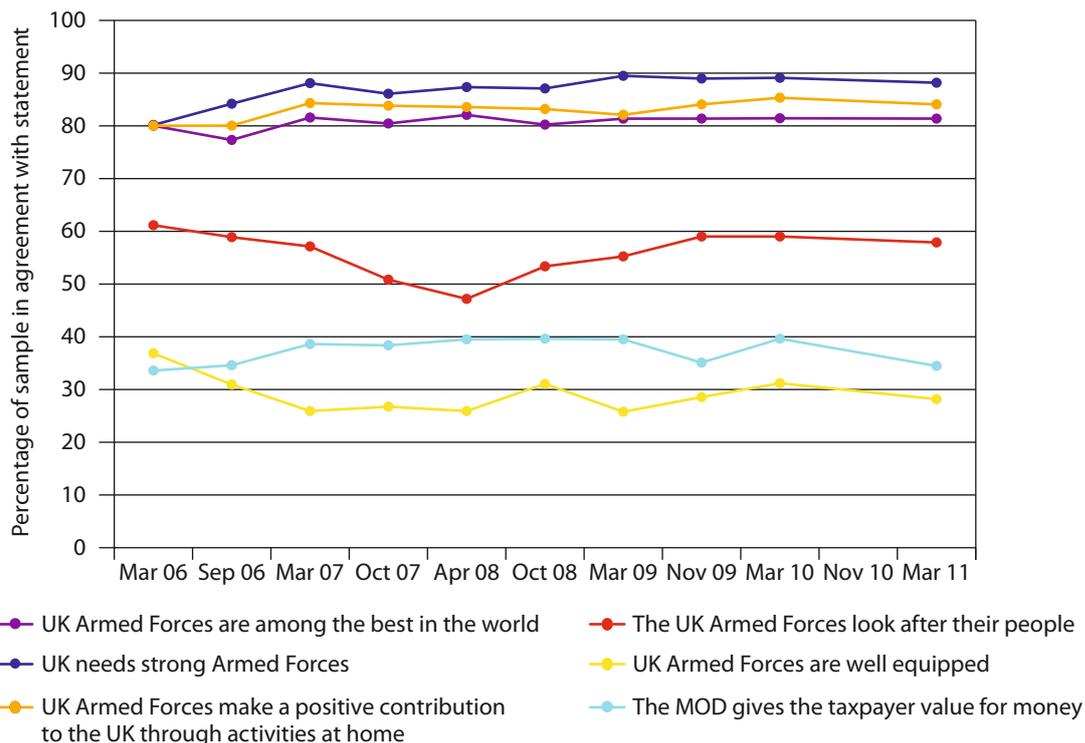
Table 8.14 – External Opinion Survey Headlines

Armed Forces	March 2011	March 2010
Favourable towards Armed Forces	88%	82%
UK Armed Forces are among the best in the world	82%	82%
UK needs strong Armed Forces	88%	89%
UK Armed Forces look after their people	58%	59%
UK Armed Forces make a positive contribution to the UK through their activities at home	84%	85%
Ministry of Defence	March 2011	March 2010
Favourable towards MOD	57%	56%
UK Armed Forces are well equipped	28%	31%
MOD gives the taxpayer value for money	35%	40%

BFPO Staff



Figure 8.3 – External Opinion Survey Polling Results, 2006-11



Reputation among Service and Civilian Personnel

8.70 We carry out an annual survey to determine the views of our own people – Service and civilian – on Defence issues and the Armed Forces. Our most recent poll conducted in Spring 2011 showed that the majority of our people agree that both the Armed Forces and the MOD are a force for good at 90% and 75% respectively. Internal views on equipment have increased again and 75% of our people believe Armed Forces equipment is good or satisfactory.

Table 8.15 – Internal opinion (Service and civilian personnel) of MOD and Armed Forces

% of Service and civilian personnel who thought that the Armed Forces were a Force for Good		
Spring 2011	Spring 2010	Spring 2009
90%	91%	89%
% of Service and civilian personnel thought that the MOD was a Force for Good		
Spring 2011	Spring 2010	Spring 2009
75%	79%	79%

Teaching Service Personnel

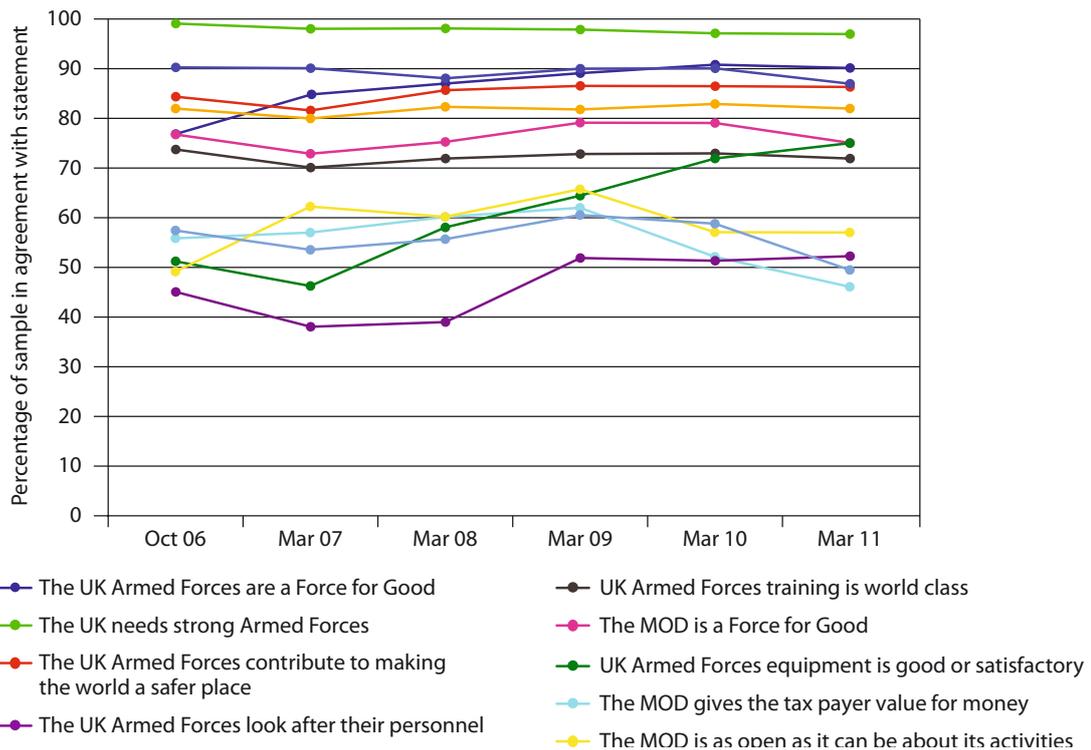


Table 8.16 – Internal Opinion Survey headlines

Armed Forces	March 2011	March 2010
UK Armed Forces are a Force for Good	90%	91%
UK Armed Forces are among the best in the world	88%	91%
UK needs strong Armed Forces	97%	97%
UK Armed Forces contribute to making the world a safer place	87%	87%
UK Armed Forces have the highest professional standards	82%	83%
UK Armed Forces look after their personnel	46%	51%
UK Armed Forces make a positive contribution to the UK through their activities at home	87%	93%
UK Armed Forces training is world class	72%	73%

Ministry of Defence	March 2011	March 2010
MOD is a Force for Good	75%	79%
UK Armed Forces equipment is good or satisfactory	75%	72%
MOD gives the taxpayer value for money	46%	52%
MOD is as open as it can be about its activities	57%	57%
MOD looks after its civilian employees	50%	59%

Figure 8.4 – Internal polling results, 2006-2011



Section 7: Accounts Introduction

Departmental Accounting Boundary

8.71 As at 31 March 2011, the Department consisted of 7 (2009-10: 8) Top Level Budget (TLB) Holders; the reduction is a result of a reorganisation of Science, Innovation, Technology TLB with some functions being transferred to the Defence Science and Technology Laboratory (Dstl) (a Defence Trading Fund outside the accounting boundary) and the remainder being included under the Central TLB. The TLBs are responsible for providing forces and support services required for a modern defence force and are detailed in Note 2 to the accounts – Analysis of Net Resource Outturn. Within the TLBs, there were 31 (2009-10: 32) reporting entities, known as management groupings, producing detailed management accounting information as part of in-year financial management, planning and budgeting processes. Accounting transactions are recorded at management group level for in-year management purposes but reporting for the annual financial accounts is based on TLB level returns.

8.72 Following removal of agency status from the Defence Storage and Distribution Agency on 31 July 2010 there are 5 (2009-10: 6) on-vote Defence Agencies (listed in Note 33 – Entities within the Departmental Boundary). Defence Agencies publish their own accounts. All on-vote Agencies are also management groupings. Further information on each agency can be found at the following websites:

Agency	Website
Defence Vetting Agency	http://www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/SecurityandIntelligence/DVA/
MOD Police and Guarding Agency	http://www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/SecurityandIntelligence/MDPGA/
People, Pay and Pensions Agency	http://www.mod.uk/DefenceInternet/MicroSite/PPPA/
Service Children's Education	http://www.sceschools.com/home-ie6.php
Service Personnel and Veterans Agency	http://www.veterans-uk.info/

8.73 Also included within the Departmental Boundary are Advisory Non-Departmental Public Bodies (NDPBs) sponsored by the Department; these are listed at Note 33.

8.74 There are 4 (2009-10: 4) Executive Defence Agencies established as Trading Funds, and owned by the Secretary of State for Defence, at 31 March 2011. The Trading Funds produce their own accounts and fall outside the Departmental Boundary. Further details are provided in: Note 16 – Financial Instruments, Note 30 – Related Party Transactions and on the Trading Funds' websites:

Trading Fund	Website
Defence Science and Technology Laboratory (Dstl)	http://www.dstl.gov.uk/
UK Hydrographic Office (UKHO)	http://www.ukho.gov.uk/Pages/Home.aspx
Met Office	http://www.metoffice.gov.uk/
Defence Support Group (DSG)	http://www.dsg.mod.uk/default.asp

8.75 The Department also sponsors 3 (2009-10: 3) Executive Non-Departmental Public Bodies (NDPBs): The National Museum of the Royal Navy, The National Army Museum and The RAF Museum. The 3 Executive NDPBs receive Grants-in-Aid from the MOD and fall outside the Departmental Boundary. Further details are at Note 30 – Related Party Transactions.

8.76 The Oil and Pipelines Agency, the NAAFI and the Fleet Air Arm Museum are Public Corporations; they also fall outside the Departmental Boundary.

Pension Liabilities

8.77 The transactions and balances of the Armed Forces Pension Scheme (AFPS) (including the Gurkha Pension Scheme, the Non-Regular Permanent Staff Pension Scheme and the Reserve Forces Pension Scheme) and the Armed Forces Compensation Scheme are not consolidated in the financial statements. The report and accounts of the AFPS are prepared separately; further information is available on the website:

<http://www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/Personnel/Pensions>

8.78 The Department's share of the transactions and balances of other pension schemes to which employees belong (e.g. under Civil Service Pension (CSP) arrangements, the NHS Superannuation Scheme and the Teachers' Pension Scheme) is also

not consolidated in the accounts; separate accounts are prepared for the schemes and details can be found on the following websites:

http://www.civilservice-pensions.gov.uk/facts_and_figures.aspx

<http://www.education.gov.uk/schools/careers/payandpensions>

<http://www.nhsbsa.nhs.uk/pensions>

8.79 Other employees are members of smaller pension schemes e.g. schemes for Locally Employed Civilians in Germany, Cyprus and Gibraltar and the Merchant Navy Ratings Pension Fund; estimates of the liabilities for these schemes are included in the figure for Provisions for Liabilities and Charges (see Note 23).

8.80 Employer's contributions payable to the Armed Forces, Civil Service, NHS, Teachers' and other pension schemes have been charged to the Statement of Comprehensive Net Expenditure. Further information on the various pension schemes can be found in the Remuneration Report and at Note 9 – Staff Numbers and Costs.

Research and Development

8.81 Research and Development expenditure is incurred mainly for the future benefit of the Department. Such expenditure is primarily incurred on the development of new single use military equipment and on the improvement of the effectiveness and capability of existing single use military equipment.

8.82 In accordance with IAS 38 – Intangible Assets (as adapted for the public sector by the FReM, chapter 7) amounts spent on research are not capitalised and certain development expenditure is expensed. The amounts are included at Note 10 – Other Administration Costs and Note 11 – Other Programme Costs.

8.83 Capitalised development expenditure is included in Note 14 – Intangible Assets.

Payments to Suppliers

8.84 The Department's invoices, with the exception of some payments to suppliers made by units locally, are paid through the Financial Management Shared Service Centre (FMSSC). In the period 1 April 2010 to 31 March 2011, the FMSSC paid 99.97% of all correctly submitted invoices within 11 calendar days. This contributed to the Department's overall performance of 99.46% over the 30 calendar day cycle ensuring a high level of compliance with its statutory obligation under the Late Payment of Commercial Debts (Interest) Act 1998. Commercial debt interest paid during this period amounted to £188 (2009-10: £20,300). From May 2010 all Government Departments were asked to pay 80% of invoices from suppliers within 5 working days. The Department, including its Trading Funds, has achieved a performance of 95.23% against this target up to 31 March 2011.

Financial Instruments

8.85 The MOD holds financial instruments to finance its operations, to manage related currency risks and as a hedge against future fuel price risk arising from those operations; in addition various trade and other receivables and payables arise directly from operations. The Department uses derivative financial instruments, in the form of forward currency contracts, to manage exposure to market risks from changes in foreign exchange rates and swap contracts as a hedge against future changes in fuel prices; it does not hold or issue derivative financial instruments for trading purposes. Transactions in derivative financial instruments are undertaken to manage the risks arising from underlying business activities.

8.86 The Department's funding, liquidity and cash flow risks are managed, based on consideration of the cash flows from operations (including non-operating Appropriations-in-Aid), by a central treasury function whose primary role is the forecasting of cash requirement, management of the Supply funding and supply of funds to business areas across the Department. The central treasury function is subject to controls set out in: Managing Public Money, which sets out HM Treasury's principles for dealing with resources used by public sector organisations, Departmental regulations (Joint Service Publications) and a biennial banking review, completed by Defence Internal Audit, as well as additional controls and monitoring by HM Treasury.

8.87 The Department has entered into forward currency contracts for the US Dollar and the Euro. These contracts are designed to mitigate 80% of the risk that Request for Resources 1 (RfR1) – Provision of Defence Capability cash flows will be affected by changes in exchange rates; thus providing greater certainty over transactions in these key foreign currencies. As a result MOD's exposure to foreign currency risk arises mainly on: residual exposure in RfR1; RfR2 – Operations and Peace-Keeping expenditure and exposure in other currencies. The value of the forward currency contracts is detailed at Note 16 – Financial Instruments.

8.88 During financial year 2010-11 the Department has, for the first time, entered into swap contracts for Aviation Turbine Fuel and Gasoil for delivery of these fuels starting in 2011-12. These contracts are designed to mitigate 80% of the risk that RfR1 cash flows will be affected by changes in the prices of the two fuel commodities from 2011-12. As a result MOD's exposure to the price risk for these fuel types arises from residual exposure in RfR1 and expenditure in RfR2. The value of the swap contracts is detailed at Note 16 – Financial Instruments.

8.89 The Department is subject to some credit risk or credit related losses. The maximum credit risk exposure is represented by the amounts reported under the relevant Statement of Financial Position headings; more detailed analysis is provided at Notes 20 (trade receivables and other current assets) and 16.3 (credit risk).

Provision of Information and Consultation with Employees

8.90 The MOD has a strong Whitley committee structure through which employees' representatives, in the form of recognised industrial and non industrial trades unions (TUs), are consulted on and informed of all matters likely to affect our civilian personnel. This structure is supported by formal policy and procedures for consulting and informing TUs. We also advocate the development of informal relationships with the TUs to discuss ideas together. Our policy makes clear that consulting the TUs is not a substitute for dealing with personnel direct, and vice versa. Managers and project leaders, for example, are encouraged to use all media available, including cascade briefings, newsletters and intranet websites/email. In respect of Service personnel, the process operates through the chain of command, with no formal representation through the TUs.

IFRIC 4 – Determining whether an Arrangement Contains a Lease

8.91 Contrary to the statement in the 2009-10 accounts the MOD has not applied IFRIC 4 to new contracts agreed on or after 1 April 2010. The Department commenced a review with its main suppliers and identified indicative costs that would be incurred in the short and longer term to ensure that these suppliers would continue to provide the necessary information to meet the accounting disclosures. However, the announcement of the SDSR and the potential impact on existing contracts and the supplier base has meant that further work to comply with IFRIC 4 has been put on hold until contract re-negotiations have been completed. Contract negotiations began in late 2010-11 and will continue during 2011-12 after which the Department will be able to resume its review of the application of IFRIC 4.

8.92 The non-application of IFRIC 4 will result in a qualification of the Comptroller and Auditor General's (C&AG) opinion on the financial statements for as long as non-compliance is considered to have a material impact on the accounts.

Performance

8.93 The MOD's internet site (www.mod.uk) provides access to detailed information set out, as best practice, in the Accounting Standards Board's (ASB's) Reporting Statement: Operating and Financial Review.

8.94 The *Strategic Defence and Security Review* available at: <http://www.mod.uk/DefenceInternet/DefenceNews/DefencePolicyAndBusiness/StrategicDefenceAndSecurityReviewPublished.htm>

- describes Defence strategies, priorities and activities, and how they are managed and delivered in the legislative, regulatory and external environments in which MOD operates;
- provides a forward looking view of performance and development; and
- sets out information on the availability and use of resources.

8.95 The plan describes some of the risks and uncertainties which might affect performance. The Statement on Internal Control also describes the Department's risk and control framework.

8.96 Additional detail is provided by the *Business Plan 2011-15* published by the Department at: <http://www.mod.uk/DefenceInternet/AboutDefence/CorporatePublications/BusinessPlans/ModBusinessPlans/BusinessPlan20112015.htm>

Environmental, Social, Community, Employee and Other Matters

8.97 The *Business Plan 2011-15* summarises senior managers' views of how the Department's work will realise the Defence Vision, highlighting relevant matters. Specific aspects mentioned in the ASB's Reporting Statement that are available elsewhere on MOD's website are:

- **Social and Community Issues** – including sections covering: current operations, cadet forces and support to veterans.
- **Environmental** – the MOD owns a large, varied and complex estate, with most of the UK's indigenous habitat types, exceptional biodiversity and some of the finest archaeological sites in the country. Further information on how the MOD is undertaking its responsibility for stewardship of the estate in the UK and overseas including links to *Sanctuary*, the annual MOD Conservation magazine, can be found at: <http://www.mod.uk/defenceinternet/microsite/dio>
- **Sustainability** – the MOD's work to build security overseas is a key contributor to Sustainable Development. Internationally, MOD works with other government departments to prevent or contain violence, protect people and institutions, build capacity and improve security in some of the most poorly developed regions and countries in the world. This work is essential for preventing further conflict, strengthening international peace and creating the conditions for sustainable development overseas. Further information can be found at: <http://www.mod.uk/DefenceInternet/AboutDefence/CorporatePublications/HealthandSafetyPublications/SSDCD/SustainableDevelopmentPolicy/>

- **Employees** – personnel related information can be found at: <http://www.mod.uk/DefenceInternet/AboutDefence/CorporatePublications>; and statistical information including staff numbers can be found at: <http://www.dasa.mod.uk/>. The MOD publishes details of its management of civilian sick absence on its website – details can be found at: <http://www.mod.uk/DefenceInternet/AboutDefence/CorporatePublications/PersonnelPublications/Welfare/SicknessAbsenceAnnouncement.htm>.
- **Performance Indicators** – Some details of MOD's performance are published as part of the Government's transparency initiative at: <http://transparency.number10.gov.uk/>
- **Contractual Arrangements** – the Department's contractual commitments under leases and service concession arrangements are detailed in Notes 26 and 27 to the accounts. In 2010-11 the Defence Science and Technology Laboratory, the UK Hydrographic Office, the Met Office, and Defence Support Group were Executive Defence Agencies financed by Trading Fund; they provided essential services to the Department. Details of the Defence Industrial Strategy are at: <http://www.mod.uk/DefenceInternet/DefenceFor/Business/DefenceIndustrialStrategy/>
- **Spending Review 2010** – implications of significant changes following the Department's Comprehensive Spending Review settlement are set out in the *Business Plan 2011-15*.
- **Contingent Liabilities** – Details of Contingent Liabilities disclosed under IAS 37 – Provisions, Contingent Liabilities and Contingent Assets, and additional liabilities included for Parliamentary Reporting and Accountability are at Note 28 to these accounts.

Personal Data Related Incidents

8.98 The following tables set out details of the Department's personal data related incidents during 2010-11. An incident is defined as a loss, unauthorised disclosure or insecure disposal of personal data. Protected personal data is information that links an identifiable living person with information about them which, if released, would put the individual at risk of harm or distress. The definition includes sources of information that, because of the nature of the individuals or the nature, source or extent of the information, is treated as protected personal data by the Department.

The Department's Chief Information Officer has responsibility for setting strategy, policy and standards relating to information and for ensuring appropriate governance and monitoring. A risk-based information assurance process is in place, taking account of an independent review by Sir Edmund Burton and Cabinet Office guidance

Month of Incident	Nature of Incident	Nature of Data Involved	Number of People Potentially Affected	Notification Steps
July 2010	Loss of CD from secured Government premises	Personal information including names, address, date of birth, National Insurance numbers and salary details	2,350	Individuals notified by letter
July 2010	Incorrect packaging of mailing to ex-service personnel in Northern Ireland	Names and addresses	3,800	Individuals notified by letter
Further action on information risk:		The Information Assurance Programme is focussed on working towards the target of compliance across the MOD with Level 3 of the Information Assurance Maturity Model by April 2012. It continues to implement those recommendations from the Burton Report and Data Handling Review which required longer timescales to implement.		

Incidents deemed by the Data Controller not to fall within the criteria for report to the Information Commissioner's Office but recorded centrally within the Department are set out in the table below. Small, localised incidents are not recorded centrally and are not cited in these figures

Category	Nature of Incident	Total
I	Loss of inadequately protected electronic equipment, devices or paper documents from secured Government premises.	6
II	Loss of inadequately protected electronic equipment, devices or paper documents from outside secured Government premises.	14
III	Insecure disposal of inadequately protected paper documents.	-
IV	Unauthorised disclosure.	-
V	Other.	-

Financial Position

8.99 The Statement of Parliamentary Supply – Summary of Resource Outturn compares Estimates and Outturn (Net Total Resources) and is analysed by Request for Resource.

8.100 Request for Resources (RfR) 1, Provision of Defence Capability, provides for expenditure primarily to meet the MOD's operational support and logistics services costs and the costs of providing the equipment capability required by Defence policy. Within RfR1, Appropriations-in-Aid are shown as the lower of actual Outturn or the Estimate. Appropriations-in-Aid in excess of the Estimate are shown at Note 5, and these will be surrendered to the Consolidated Fund. RfR1 is made up of three different controls:

- Resource Departmental Expenditure Limit (DEL), which consists of items such as pay, equipment support costs, fuel and administrative expenses, as well as non-cash items such as depreciation and movements in the level of provisions;

- Annually Managed Expenditure (AME), which covers programmes that are demand-led, or exceptionally volatile in a way that could not be controlled by the Department, and where the programmes are so large that the Department could not be expected to absorb the effects of volatility in its programme, for example movements in nuclear provisions and derivatives; and
- Non-Budget costs, items of expenditure which are subject to Parliamentary but not Treasury control, and therefore outside DEL and AME. The majority of these costs relate to changes in the discount rates for pensions and to Service Concession Arrangements added to the Statement of Financial Position under IFRIC 12 but 'Off-Balance Sheet' for National Accounts.

8.101 The net outturn for Total Resources is £48,821,266,000 against an Estimate of £56,792,036,000, an under spend of £7,970,770,000.

8.102 The net outturn for RfR1, Provision of Defence Capability is £44,995,706,000 against an Estimate of £52,534,636,000, an under spend of £7,538,930,000.

8.103 RfR2, Operations and Peace-Keeping, shows a net outturn of £2,890,494,000 against an Estimate of £3,284,709,000, an under spend of £394,215,000.

8.104 RfR3, War Pensions Benefits shows a net outturn of £935,066,000 against an Estimate of £972,691,000, an under spend of £37,625,000. This RfR provides for the payment of war disablement and war widows' pensions in accordance with relevant legislation; this is all AME. The costs of administering war pensions are borne by RfR1.

8.105 The non-operating Appropriations-in-Aid were £103,235,000, £193,891,000 lower than the Estimate of £297,126,000.

8.106 The Net Administration Costs were £2,026,012,000, £156,574,000 lower than the Estimate of £2,182,586,000.

8.107 The Net Cash Requirement shows an outturn of £37,644,715,000 against an Estimate of £39,556,772,000.

8.108 Additional information on the Department's budget and expenditure including a reconciliation of resource expenditure between Estimates, Accounts and Budgets and information on expenditure on military operations is included in the section on Delivering Defence.

Other Areas

8.109 The Department's Accounts include a note (Note 29) on Losses and Special Payments. The nature of the losses and special payments, as defined in Managing Public Money, varies from year to year depending on the circumstances arising and decisions made by the Department during the year. Cases brought forward from prior years are shown separately in order to identify the cases arising during the year.

8.110 The Department undertakes a professional revaluation of its land and building non-current assets every five years. The process is managed as a five year rolling programme; further details of the revaluation programme are at Note 15.1 – Quinquennial Revaluation to the accounts.

Directorships and Significant Interests

8.111 Details of directorships and other significant interests held by Ministers are set out in The Register of Lords' Interests and The Register of Members' Financial Interests which are available on the UK Parliament website at: <http://www.publications.parliament.uk/pa/ld/ldreg.htm> for Ministers in the Lords and at: <http://www.publications.parliament>.

[uk/pa/cm/cmregmem/memi02.htm](http://www.publications.parliament.uk/pa/cm/cmregmem/memi02.htm) for Ministers in the Commons.

8.112 In accordance with Cabinet Office guidance MOD maintains a register of interest which records details of directorships and other significant interests held by senior managers (but excluding Non-Executive Directors) in the Department. The Ministry of Defence Register of Interest is updated quarterly and a copy can be requested from DFM-RegisterofInterest-mailbox@mod.uk.

8.113 Details of Related Party Transactions, including those arising as a result of the interests of Ministers or Defence Board members, are listed at Note 30 – Related Party Transactions. During 2010-11, Ministers and Defence Board members had no personal transactions requiring disclosure. The MOD works closely with many organisations, especially in the charitable sector, and this can include representation on governing bodies, for example: The Secretary of State for Defence is trustee of Greenwich Hospital. The Department provides information, which reflects the Charity Commission's guidance on conflicts of interest for charity trustees, to individuals who hold appointments in outside organisations where a conflict of interest might arise, or be perceived to arise.

Auditor

8.114 The financial statements for the Department are audited by the Comptroller and Auditor General under the Government Resources and Accounts Act 2000. The Certificate and Report of the Comptroller and Auditor General on the financial statements form part of this Annual Report and Accounts. The audit fee is disclosed in Note 10 – Other Administration Costs. The Department did not contract with its external auditor for any non-audit services.

Statement as to Disclosure of Information to Auditors

8.115 So far as I, the Accounting Officer, am aware, there is no relevant audit information of which the Department's auditors are unaware, and I have taken all the steps that I ought to have taken to make myself aware of any relevant audit information and to establish that the Department's auditors are aware of that information.

Section 8: Remuneration Report

Remuneration Policy

8.116 The Review Body on Senior Salaries (SSRB) provides independent advice to the Prime Minister and the Secretary of State for Defence on the remuneration of senior civil servants and senior officers of the Armed Forces.

8.117 The Review Body also advises the Prime Minister from time to time on the pay, pensions and allowances of Members of Parliament; on Peers' allowances; and on the pay, pensions and allowances of Ministers and others, whose pay is determined by the Ministerial and Other Salaries Act 1975 (as amended).

8.118 In reaching its recommendations, the Review Body has regard to the following considerations:

- the need to recruit, retain and motivate suitably able and qualified people to exercise their different responsibilities;
- regional/local variations in labour markets and their effects on the recruitment and retention of staff;
- Government policies for improving the public services including the requirement on departments to meet the output targets for the delivery of departmental services;
- the funds available to departments as set out in the Government's departmental expenditure limits; and
- the Government's inflation target.

8.119 The Review Body takes account of the evidence it receives about wider economic considerations and the affordability of its recommendations. Further information about the work of the Review Body can be found at www.ome.uk.com.

8.120 There is an established departmental procedure for the appointment of all Non-Executive Directors (NEDs). This requires a visibly fair and open recruitment and selection process, with appointment on merit, thus mirroring the Civil Service Commissioners' Recruitment Principles for permanent employees to the Civil Service. NEDs appointed to the Defence Board receive a Letter of

Appointment setting out, amongst other things, details of the agreed remuneration.

8.121 Performance and Reward

8.122 Salary and reward for Permanent Secretaries is considered annually by the Permanent Secretaries' Remuneration Committee and, in common with that for other members of the Senior Civil Service (SCS), is subject to the rules and regulations imposed by the SSRB and the Cabinet Office. For the SCS below Permanent Secretary level, MOD implements its own pay and non-consolidated award arrangements within the Cabinet Office framework through an agreed pay strategy. Any non-consolidated award is based on a judgement of how well an individual has performed against their peers and awarded to individuals judged to have made the highest in-year contribution to MOD's business objectives. There is no restriction on the nature of the contribution; the only requirement is that it benefits the Department or Defence more widely. Recommendations for awards – which are considered by moderation committees – must be linked to demonstrable evidence of delivery.

8.123 SCS pay increases are normally calculated using the relationship between their percentage progression across the pay scale and their performance group assessment at the end of the moderation committee process. Minima and maxima of SCS pay bands are set by the Cabinet Office. There were no base increases for any members of the SCS on 1 April 2010 and no increase to pay band minimums. Furthermore, it was announced in June 2010 that the public sector would have a freeze on pay increases for two years from 2011-12. Additionally a new government-wide SCS Reward Strategy is currently being developed. Non-consolidated awards for performance year 2010-11 will be limited to 25% (2009-10: 65%) of the SCS.

8.124 The Department also employs a number of members of the SCS on Fixed Term Appointments. These individuals are externally recruited to fill specific roles where the Department does not already have the necessary skills in-house. They are employed on individual contracts which allow them a base salary and the opportunity to earn performance related awards, specifically linked to business and corporate objectives. They are expected to deliver substantial benefits to the Department both in terms of outputs, delivering change programmes and skills transfer. As with the rest of the SCS the awards paid to those on Fixed Term Appointments are non-consolidated and non-pensionable and are subject to rigorous scrutiny.

8.125 All senior (2-star and above) military officers (except for the Chief of the Defence Staff (CDS), Legal Branch 2-star officers, medical and dental officers and those in the Chaplaincy branches) are paid under the Performance Management and Pay System (PMPS). Depending on their performance and position on the pay scale, individuals can be awarded a double increment (although for 2 years with effect from 1 April 2011, the award of double increments has been suspended), a single increment or no increment, and progress accordingly up the incremental pay range for their rank. The average value of one incremental rise under the PMPS is 2.6% of salary (2009-10: 2.6%). The award of increments is recommended by the Senior Officers' Remuneration Committee, chaired by the Department's Permanent Under Secretary.

8.126 Whilst Non-Executive remuneration is not directly linked to performance, in part to avoid any suggestion that an employee/employer relationship exists, NED performance is reviewed annually. The aim of the reviews is to consider the impact of the NED on the performance of the board, recognise the contribution of the NED and identify ways this could be improved, and provide feedback.

Senior Managers' Contracts

8.127 Recruitment into the Civil Service is regulated by The Constitutional Reform and Governance Act 2010 which established the Civil Service Commission and requires selection in accordance with Recruitment Principles, which require appointments to be on merit on the basis of fair and open competition, but also include the circumstances when appointments may otherwise be made. Further information about the work of the Civil Service Commissioners can be found at www.civilservicecommissioners.org.

8.128 Unless otherwise stated below, the officials covered by this report hold appointments which are open-ended, and to which a notice period of 3 months would usually apply. Early termination, other than for misconduct, would result in the individual receiving compensation as set out in the Civil Service Compensation Scheme.

8.129 For the NEDs appointed to the Defence Board, the Department has employed recruitment consultants to search for suitable candidates based upon a specification drawn up by senior officials. Short-listed candidates are then interviewed by a selection panel (Permanent Under Secretary and Chief of the Defence Staff) with the successful candidate chosen on merit and appointed to the

Board for a period of 3 years with the possibility of an extension.

8.130 NEDs are not employees and, therefore, do not have a contractual relationship with the Department; they are appointees who receive a Letter of Appointment setting out: their role, period of appointment, standards and details of remuneration.

8.131 The Chief Scientific Adviser was recruited on a three year fixed term appointment which has been extended by four months to August 2011. The Chief of Defence Materiel was recruited on a four year fixed term appointment. Conditions covering termination of employment are set out in their respective contract documents.

8.132 The Chief of the Defence Staff, Vice Chief of the Defence Staff and Single-Service Chiefs of Staff are appointed on the recommendation of the Secretary of State for Defence to the Prime Minister. The final approval of the appointee lies with Her Majesty The Queen.

8.133 Senior military members of the Defence Board hold appointments which are subject to competition. Once selected for the appointment, they will usually hold the post for between 3 and 4 years.

Management

8.134 Ministers who had responsibility for the Department during the year were:

Secretary of State for Defence

The Right Honourable Dr Liam Fox MP
(appointed 12 May 2010, replacing The Right Honourable Bob Ainsworth).

Minister of State for the Armed Forces

Mr Nick Harvey MP
(appointed 13 May 2010 replacing Mr Bill Rammell).

Minister of State for Strategic Defence Acquisition Reform

The Right Honourable The Lord Drayson
(to 11 May 2010).

Parliamentary Under-Secretary of State for Defence (Minister for International Security Strategy)

Mr Gerald Howarth MP
(appointed 14 May 2010).

Parliamentary Under-Secretary of State for Defence (Minister for International Defence and Security)

The Right Honourable The Baroness Ann Taylor of Bolton PC
(to 11 May 2010).

Parliamentary Under-Secretary of State for Defence (Minister for Defence Personnel, Welfare and Veterans)
The Right Honourable Andrew Robathan MP
(appointed 14 May 2010).

Parliamentary Under-Secretary of State for Defence (Minister for Veterans)
Mr Kevan Jones MP
(to 11 May 2010).

Parliamentary Under-Secretary of State for Defence (Minister for Defence Equipment, Support and Technology)
Mr Peter Luff MP
(appointed 26 May 2010).

Parliamentary Under-Secretary of State for Defence (Minister for Defence Equipment and Support)
Mr Quentin Davies MP
(to 11 May 2010).

Parliamentary Under-Secretary of State and Spokesperson on Defence in the House of Lords
The Lord Astor of Hever DL
(appointed 26 May 2010).

During the year the following served as members of the Defence Board:

Permanent Under-Secretary of State
Mrs Ursula Brennan
(appointed 29 October 2010 replacing Sir Bill Jeffrey KCB).

Chief of the Defence Staff
General Sir David Richards GCB CBE DSO ADC Gen
(appointed 29 October 2010 replacing Air Chief Marshal Sir Jock Stirrup GCB AFC ADC DSc FRAeS FCMI RAF).

First Sea Lord and Chief of the Naval Staff
Admiral Sir Mark Stanhope GCB OBE ADC
(appointed 21 July 2009).

Chief of the General Staff
General Sir Peter Wall KCB CBE ADC Gen
(appointed 15 September 2010 replacing General Sir David Richards GCB CBE DSO ADC Gen).

Chief of the Air Staff
Air Chief Marshal Sir Stephen Dalton KCB ADC BSc FRAeS CCMI RAF
(appointed 31 July 2009).

Vice Chief of the Defence Staff
General Sir Nicholas Houghton GCB CBE ADC Gen
(appointed 5 May 2009).

Second Permanent Under-Secretary of State
Mr Jon Day CBE
(appointed 10 January 2011 replacing Mrs Ursula Brennan).

Chief of Defence Materiel
Mr Bernard Gray
(appointed 4 January 2011 replacing General Sir Kevin O'Donoghue KCB CBE).

Chief Scientific Adviser
Professor Sir Mark Welland FRS FREng
(appointed 7 April 2008).

Director General Finance
Mr Jonathan Thompson IPFA
(appointed 5 January 2009).

Non-Executive Directors

Dr David Allen
(appointed 11 January 2010).

Mr Ian Rushby, Chair of the Defence Audit Committee
(appointed 29 January 2007).

Mrs Priscilla Vacassin, Group Human Resources Director, Prudential plc
(appointed 1 September 2007).

Ministerial Salaries, Allowances and Taxable Benefits

(This section has been subject to audit)

	2010-11 Salary* (£)	2010-11 Benefits-in-kind (to the nearest £100)*	2009-10 Salary* (£)	2009-10 Benefits-in-kind (to the nearest £100)*
Secretary of State for Defence				
The Rt Hon Dr Liam Fox MP (from 12 May 2010)	61,056	Nil	Nil	Nil
Full year equivalent salary	68,827			
The Rt Hon Bob Ainsworth MP (to 11 May 2010)	8,847	Nil	64,208	Nil
Full year equivalent salary	78,356		78,356	
Minister of State for the Armed Forces				
Mr Nick Harvey MP (from 13 May 2010)	29,187	Nil	Nil	Nil
Full year equivalent salary	33,002			
Mr Bill Rammell MP (to 11 May 2010)	4,589	Nil	32,934	Nil
Full year equivalent salary	40,646		40,646	
Minister of State for Strategic Defence Acquisition Reform				
The Rt Hon The Lord Drayson † (to 11 May 2010)	Nil	Nil	Nil	Nil
Parliamentary Under-Secretary of State for Defence (Minister for International Security Strategy)				
Mr Gerald Howarth MP (from 14 May 2010)	20,894	Nil	Nil	Nil
Full year equivalent salary	23,697			
Parliamentary Under-Secretary of State for Defence (Minister for International Defence and Security)				
The Rt Hon The Baroness Ann Taylor of Bolton PC (to 11 May 2010)	12,488	Nil	110,606	Nil
Full year equivalent salary	110,606			
Parliamentary Under-Secretary of State for Defence (Minister for Defence Personnel, Welfare and Veterans)				
The Rt Hon Andrew Robathan MP (from 14 May 2010)	20,894	Nil	Nil	Nil
Full year equivalent salary	23,697			
Parliamentary Under-Secretary of State for Defence (Minister for Veterans)				
Mr Kevan Jones MP (to 11 May 2010)**	3,483	Nil	25,024	Nil
Full year equivalent salary	30,851		30,851	
Parliamentary Under-Secretary of State for Defence (Minister for Defence Equipment, Support and Technology)				
Mr Peter Luff MP (from 26 May 2010)	20,130	Nil	Nil	Nil
Full year equivalent salary	23,697			
Parliamentary Under-Secretary of State for Defence (Minister for Defence Equipment and Support)				
Mr Quentin Davies MP ††	Nil	Nil	Nil	Nil

	2010-11 Salary* (£)	2010-11 Benefits- in-kind (to the nearest £100)*	2009-10 Salary* (£)	2009-10 Benefits-in- kind (to the nearest £100)*
(now The Lord Davies of Stamford) (to 11 May 2010)				
Parliamentary Under Secretary of State and The Lords Spokesperson on Defence The Lord Astor of Hever DL† (from 26 May 2010)	Nil	Nil	Nil	Nil

*Disclosures cover the period during which individuals served as Ministers in the MOD.

**Mr Kevan Jones MP was appointed Under-Secretary of State on 5 October 2008 and served, unpaid, until 9 June 2009.

† The Rt Hon The Lord Drayson and The Rt Hon The Lord Astor of Hever did not draw the £84,524 Ministerial salary to which they were entitled.

†† Mr Quentin Davies MP did not draw the £31,401 Ministerial salary to which he was entitled.

8.135 Ministers who, on leaving office, have not attained the age of 65 and are not appointed to a relevant Ministerial or other paid office within three weeks, are eligible for a tax free severance payment of one quarter of the annual salary being paid. Four payments were made in 2010-11, (2009-10—one).

Ministerial Salary

8.136 'Salary' includes: gross salary; performance pay or bonuses; overtime; London weighting or London allowances; recruitment and retention allowances; private office allowances; ex-gratia payments and any other allowance to the extent that it is subject to UK taxation.

8.137 The figures above are based on payments made by the Department and thus recorded in the accounts. In respect of Ministers in the House of Commons, the Department bears only the cost of the additional Ministerial remuneration; the salary for their services as an MP – £65,738 pa with effect from 1 April 2010 (£64,766 pa with effect from 1 April 2009) and various allowances to which they are entitled, are borne centrally. The arrangements for Ministers in the House of Lords are different in that they do not receive a salary but rather an additional remuneration, which cannot be quantified separately from their Ministerial salaries. This total remuneration, as well as the allowances to which they are entitled, is paid by the Department and shown in full above.

Benefits-in-Kind for Ministers

8.138 The monetary value of benefits-in-kind covers any benefits provided by the Department and treated by HM Revenue and Customs as a taxable emolument.

Ministerial Pensions

(This section has been subject to audit)

8.139 The real increase in the value of the accrued pension compared to the 2009-10 value, is shown *in italics* (in bands of £2,500).

	Total Accrued Pension at Retirement as at 31 Mar 11 £000	CETV* at 31 Mar 10 or date of Appointment if Later £000	CETV at 31 Mar 11 or on Cessation of Appointment if Earlier £000	Real Increase in CETV £000
Secretary of State for Defence				
The Rt Hon Dr Liam Fox MP (from 12 May 2010)	0 – 5 <i>0 – 2.5</i>	16	31	8
The Rt Hon Bob Ainsworth MP (to 11 May 2010)	10 – 15 <i>0 – 2.5</i>	203	207	4
Minister of State for the Armed Forces				
Mr Nick Harvey MP (from 13 May 2010)	0 – 5 <i>0 – 2.5</i>	Nil	10	5
Mr Bill Rammell MP (to 11 May 2010)	5 – 10 <i>0 – 2.5</i>	81	82	1
Minister of State for Strategic Defence Acquisition Reform				
The Rt Hon The Lord Drayson (to 11 May 2010)	Nil	Nil	Nil	Nil
Parliamentary Under-Secretary of State for Defence (Minister for International Security Strategy)				
Mr Gerald Howarth MP (from 14 May 2010)	0 – 5 <i>0 – 2.5</i>	Nil	13	9
Parliamentary Under-Secretary of State for Defence (Minister for International Defence and Security)				
The Rt Hon The Baroness Ann Taylor of Bolton PC (to 11 May 2010)	0 – 5 <i>0 – 2.5</i>	59	63	2
Parliamentary Under-Secretary of State for Defence (Minister for Defence Personnel, Welfare and Veterans)				
The Rt Hon Andrew Robathan MP (from 14 May 2010)	0 – 5 <i>0 – 2.5</i>	48	62	7
Parliamentary Under-Secretary of State for Defence (Minister for Veterans)				
Mr Kevan Jones MP (to 11 May 2010)	0 – 5 <i>0 – 2.5</i>	6	7	Nil
Parliamentary Under-Secretary of State for Defence (Minister for Defence Equipment, Support and Technology)				
Mr Peter Luff MP (from 26 May 2010)	0 – 5 <i>0 – 2.5</i>	63	78	7
Parliamentary Under-Secretary of State for Defence (Minister for Defence Equipment and Support)				
Mr Quentin Davies MP (now The Lord Davies of Stamford) (to 11 May 2010)	Nil	Nil	Nil	Nil
Parliamentary Under-Secretary of State and The Lords Spokesperson on Defence				
The Lord Astor of Hever DL (from 26 May 2010)	Nil	Nil	Nil	Nil

*CETV – Cash Equivalent Transfer Value. For consistency CETVs as at 31 March 2010 and 31 March 2011 have been calculated using actuarial factors which changed during 2010. CETVs as at 31 March 2010 therefore differ from those published last year.

8.140 Pension benefits for Ministers are provided by the Parliamentary Contributory Pension Fund (PCPF). The scheme is made under statute (the regulations are set out in Statutory Instrument SI 1993 No 3253, as amended). Ministers who are Members of Parliament may also accrue an MP's pension under the PCPF; this pension is not included in the table above. The accrued pension quoted is the pension the Minister is entitled to receive when they reach the age of 65, or immediately on ceasing to be an active member of the scheme if they are already 65.

8.141 The arrangements for Ministers provide benefits on an 'average salary' basis, taking account of all service as a Minister. The accrual rate has been 1/40th since 15 July 2002 (or 5 July 2001 for those that chose to backdate the change). Ministers, in common with all other members of the PCPF, can opt for a 1/50th accrual rate and a lower rate of employee contribution. An additional 1/60th accrual rate option (backdated to 1 April 2008) was introduced from 1 January 2010.

8.142 Benefits for Ministers are payable at the same time as MPs' benefits become payable under the PCPF or, for those who are not MPs, on retirement from Ministerial office from age 65. Pensions are increased annually in line with changes in Pensions Increase legislation. From 1 April 2009 members pay contributions of 5.9% of their Ministerial salary if they have opted for the 1/60th accrual rate, 7.9% of salary if they have opted for the 1/50th accrual rate or 11.9% of salary if they have opted for the 1/40th accrual rate. There is also an employer contribution paid by the Exchequer representing the balance of cost as advised by the Government Actuary. This is currently 28.7% of the Ministerial salary.

The Cash Equivalent Transfer Value (CETV)

8.143 This is the actuarially-assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. It is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the pension benefits they have accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total Ministerial service, not just their current appointment as a Minister. CETVs are calculated in accordance with the guidelines and framework prescribed by the Institute and Faculty of Actuaries and do not take account of any actual or potential reduction to benefits resulting from Lifetime Allowance Tax which may be due when pension benefits are taken.

The Real Increase in the Value of the CETV

8.144 This is the element of the increase in accrued pension funded by the Exchequer. It excludes increases due to inflation and contributions paid by the Minister and is calculated using common market valuation factors for the start and end of the period.

Defence Board – Salaries, Allowances and Taxable Benefits-in-Kind

(This section has been subject to audit)

	2010-11 Salary* £000	2010-11 Annual Performance Award*	2010-11 Benefits- in-kind (to the nearest £100)**	2009-10 Salary* £000	2009-10 Annual Performance Award*	2009-10 Benefits- in-kind (to the nearest £100)**
Permanent Under-Secretary of State						
Mrs Ursula Brennan (from 29 October 2010)	75 – 80	Nil	Not*** Available	Nil	Nil	Nil
<i>Full year equivalent salary</i>	175 – 180					
Sir Bill Jeffrey KCB (to 28 October 2010)	105 – 110	Nil	Not*** Available	175 – 180	Nil	21,900
<i>Full year equivalent salary</i>	175 – 180					
Chief of the Defence Staff						
General Sir David Richards GCB CBE DSO ADC Gen (from 29 October 2010)	100 – 105	Nil	28,200	Nil	Nil	Nil
<i>Full year equivalent salary</i>	235 – 240					
Air Chief Marshal Sir Jock Stirrup GCB AFC ADC DSc FRAeS FCMI RAF (now The Lord Stirrup of Marylebone in the City of Westminster) (to 28 October 2010)	145 – 150	Nil	39,600	245 – 250	Nil	56,200
<i>Full year equivalent salary</i>	250 – 255					
First Sea Lord and Chief of the Naval Staff						
Admiral Sir Mark Stanhope GCB OBE ADC (from 21 July 2009)	185 – 190	Nil	59,500	120 – 125 175 – 180	Nil	34,200
<i>Full year equivalent salary</i>						
Chief of the General Staff						
General Sir Peter Wall KCB CBE ADC Gen (from 15 September 2010)	110 – 115	Nil	49,200	Nil	Nil	Nil
<i>Full year equivalent salary</i>	205 – 210					
General Sir David Richards GCB CBE DSO ADC Gen (until 14 September 2010)	80 – 85	Nil	40,400	100 – 105 165 – 170	Nil	26,100
<i>Full year equivalent salary</i>	175 – 180					
Chief of the Air Staff						
Air Chief Marshal Sir Stephen Dalton KCB ADC BSc FRAeS CCMI RAF (from 31 July 2009)	185 – 190	Nil	57,800	135 – 140 195 – 200	Nil	30,100****
<i>Full year equivalent salary</i>						
Vice Chief of the Defence Staff						
General Sir Nicholas Houghton GCB CBE ADC Gen (from 5 May 2009)	175 – 180	Nil	54,000	150 – 155 165 – 170	Nil	37,900
<i>Full year equivalent salary</i>						
Second Permanent Under-Secretary of State						
Mr Jon Day CBE (from 10 January 2011)	30 – 35	Nil	Not*** Available	Nil	Nil	Nil
<i>Full year equivalent salary</i>	140 – 145					
Mrs Ursula Brennan (to 28 October 2010)	90 – 95	Nil	Not*** Available	155 – 160	Nil	11,000
<i>Full year equivalent salary</i>	155 – 160					

	2010-11 Salary* £000	2010-11 Annual Performance Award*	2010-11 Benefits- in-kind (to the nearest £100)**	2009-10 Salary* £000	2009-10 Annual Performance Award*	2009-10 Benefits- in-kind (to the nearest £100)**
Chief of Defence Materiel						
Mr Bernard Gray (from 4 January 2011) <i>Full year equivalent salary</i>	50 – 55 215 – 220	Nil	Not*** Available	Nil	Nil	Nil
General Sir Kevin O'Donoghue KCB CBE (to 22 December 2010) <i>Full year equivalent salary</i>	130 – 135 185 – 190	Nil	30,800	175 – 180	Nil	31,000
Chief Scientific Adviser			Not***			
Professor Sir Mark Welland FRS FREng	140 – 145	Nil	Available	140 – 145	Nil	26,200
Director General Finance						
Mr Jonathan Thompson IPFA	175 – 180	5 – 10	Nil	175 – 180	10 – 15	Nil
Non-Executive Directors						
Dr David Allen (from 11 January 2010) <i>Full year equivalent salary</i>	25 – 30	Nil	Nil	5 – 10 25 – 30	Nil	Nil
Mr Ian Rushby	35 – 40	Nil	Nil	30 – 35****	Nil	Nil
Mrs Priscilla Vacassin	20 – 25	Nil	Nil	20 – 25	Nil	Nil

*Salary includes gross salary, taxable allowances and payments in lieu of untaken leave (if applicable). Any annual performance award paid is shown separately and is in respect of amounts paid in 2010-11 but based on performance in an assessment period ended prior to the start of the financial year. Permanent Secretaries decided not to accept individual non-consolidated performance related pay awards (bonuses) in relation to the 2008-09 and 2009-10 performance years. The payment of business expenses e.g. travel costs incurred on duty, is not part of salary and is not disclosed above.

**For civilian members of the Board the figures for benefits-in-kind represent the taxable benefit attributed to individuals where an official car is available for private use (the benefit accrues even if the individual chooses not to make use of the car). For military Board members the figures disclosed as benefits-in-kind combine the taxable value in respect of their occupation of Official Service Residences and the value attributed to individuals for their private use of official cars; the benefit arising from use of cars is disclosed for the first time and is the cause of the restated figures for 2009-10. For the disclosed benefits-in-kind the Department has arrangements under which MOD pays the tax liability that would normally be paid by the individual; this liability is included in the figures quoted.

*** For 2010-11 the taxable benefit applicable to civilian Board members has not yet been agreed with HMRC; the figures for 2010-11 will be published in the 2011-12 Annual Report and Accounts.

**** Restated.

Defence Board – Pension Benefits

(This section has been subject to audit)

8.145 The real increase in the pension, from 2009-10, and where applicable the real increase in the lump sum payment, are shown in *italics*.

	Total Accrued Pension at Retirement as at 31 Mar 11 £000	CETV at 31 Mar 10 or date of Appointment if Later* £000	CETV at 31 Mar 11 or on Cessation of Appointment if Earlier* £000	Real Increase in CETV £000
Permanent Under-Secretary of State Mrs Ursula Brennan	Pension 75 – 80 <i>2.5 – 5</i> Lump Sum 235 – 240 <i>12.5 – 15</i>	1,533	1,830	98
Sir Bill Jeffrey KCB (to 28 October 2010)	Pension 85 – 90 <i>0 – -2.5</i> Lump Sum 255 – 260 <i>0 – -2.5</i>	1,901	1,943	-7
Chief of the Defence Staff General Sir David Richards GCB CBE DSO ADC Gen	Pension 105 – 110 <i>10 – 12.5</i> Lump Sum 320 – 325 <i>30 – 32.5</i>	1,980	2,235	198
Air Chief Marshal Sir Jock Stirrup GCB AFC ADC DSc FRAeS FCMI RAF (now The Lord Stirrup of Marylebone in the City of Westminster) (to 28 October 2010)	Pension 140 – 145 <i>2.5 – 5</i> Lump Sum 430 – 435 <i>12.5 – 15</i>	2,740	2,912	77
First Sea Lord and Chief of the Naval Staff Admiral Sir Mark Stanhope GCB OBE ADC	Pension 105 – 110 <i>2.5 – 5</i> Lump Sum 315 – 320 <i>12.5 – 15</i>	2,086	2,216	89
Chief of the General Staff General Sir Peter Wall KCB CBE ADC Gen (from 15 September 2010)	Pension 90 – 95 <i>2.5 – 5</i> Lump Sum 270 – 275 <i>7.5 – 10</i>	1,972	2,068	69
Chief of the Air Staff Air Chief Marshal Sir Stephen Dalton KCB ADC BSc FRAeS FCMI RAF	Pension 95 – 100 <i>5 – 7.5</i> Lump Sum			

	Total Accrued Pension at Retirement as at 31 Mar 11 £000	CETV at 31 Mar 10 or date of Appointment if Later* £000	CETV at 31 Mar 11 or on Cessation of Appointment if Earlier* £000	Real Increase in CETV £000
	285 – 290 15 – 17.5	1,756	2,134	127
Vice Chief of the Defence Staff General Sir Nicholas Houghton GCB CBE ADC Gen	Pension 90 – 95 5 – 7.5 Lump Sum 280 – 285 15 – 17.5	1,799	2,107	124
Second Permanent Under-Secretary of State Mr Jon Day CBE (from 10 January 2011)	Pension 35 – 40 2.5 – 5 Lump Sum 100 – 115 7.5 – 10	716	813	61
Chief of Defence Materiel Mr Bernard Gray (from 4 January 2011)	Pension 0 – 5 0 – 2.5 Lump Sum Nil	Nil	14	12
General Sir Kevin O'Donoghue KCB CBE (to 22 December 2010)	Pension 100 – 105 0 – 2.5 Lump Sum 310 – 315 5 – 7.5	1,902	1,952	28
Chief Scientific Adviser Professor Sir Mark Welland FRS FREng	Pension 10 – 15 2.5 – 5 Lump Sum Nil	79	136	40
Director General Finance Mr Jonathan Thompson IPFA	Pension 30 – 35 0 – 2.5 Lump Sum Nil	339	402	10
Non-Executive Directors				
Dr David Allen	Nil	Nil	Nil	Nil
Mr Ian Rushby	Nil	Nil	Nil	Nil
Mrs Priscilla Vacassin	Nil	Nil	Nil	Nil

* For consistency CETVs for members of the PCSPS as at 31 March 2010 and 31 March 2011 have been calculated using actuarial factors which changed during 2010. CETVs as at 31 March 2010 therefore differ from those published last year. Calculations of CETVs for members of the AFPS have not used revised actuarial factors as these were not available.

Civil Service Pensions

8.146 Pension benefits are provided through the Civil Service pension arrangements. From 30 July 2007, civil servants may be in one of four defined benefit schemes; either a 'final salary' scheme (classic, premium, or classic plus) or a 'whole career' scheme (nuvos). Classic, premium and classic plus are now closed to new members. These statutory arrangements are unfunded with the cost of benefits met by monies voted by Parliament each year. Pensions payable under nuvos, classic, premium, and classic plus are increased annually in line with Pensions Increase legislation. Members joining from October 2002 may opt for either the appropriate defined benefit arrangement or a 'money purchase' stakeholder pension with an employer contribution (partnership pension account). The accrued pensions quoted above are the pensions the members are entitled to receive when they reach 60 (nuvos 65), or immediately on ceasing to be an active member of the scheme if they are already 60 (nuvos 65).

8.147 Employee contributions are set at the rate of 1.5% of pensionable earnings for classic and 3.5% for premium, classic plus and nuvos. Employer contributions are calculated using four percentage rates (16.7%, 18.8%, 21.8% and 24.3%) of pensionable pay, based on four salary bands. Benefits in classic accrue at the rate of 1/80th of final pensionable earnings for each year of service; in addition, a lump sum equivalent to three years' pension is payable on retirement. For premium, benefits accrue at the rate of 1/60th of final pensionable earnings for each year of service; unlike classic, there is no automatic lump sum. Classic plus is essentially a hybrid with benefits in respect of service before 1 October 2002 calculated broadly as per classic and benefits for service from October 2002 calculated as in premium. In nuvos a member builds up a pension based on pensionable earnings during their period of scheme membership. At the end of the scheme year (31 March) the member's earned pension account is credited with 2.3% of their pensionable earnings in that scheme year and the accrued pension is increased in line with Pensions Increase legislation. In all cases members may opt to give up (commute) pension for a lump sum up to the limits set by the Finance Act 2004.

8.148 The partnership pension account is a stakeholder pension arrangement. The employer makes a basic contribution of between 3% and 12.5% (depending on the age of the member) into a stakeholder pension product chosen by the employee. The employee does not have to contribute but, where they do make contributions, the employer will match these up to a limit of 3% of pensionable salary (in addition to the employer's basic contribution). Employers also contribute a

further 0.8% of pensionable salary to cover the cost of centrally-provided risk benefit cover (death in service and ill health retirement).

8.149 Further details about the Civil Service pension arrangements can be found at the website www.civilservice-pensions.gov.uk.

Armed Forces Pension Scheme (AFPS)

8.150 From 6 April 2005, a new Armed Forces Pension Scheme (known as AFPS 05) was introduced for all new members of the Armed Forces; those in service before this date have been given the opportunity to transfer, from AFPS 75, to the new scheme. Both schemes are defined benefit, salary-related, contracted out, occupational pension schemes. The AFPS is non-contributory for members; the cost of accruing benefits are met by the employer at rates approximately equivalent to 40.1% (42.8% from 2011-12) for Officers and 25.6% (30.8% from 2011-12) for Other Ranks of pensionable pay for regular personnel. Members are entitled to a taxable pension for life and a tax-free pension lump sum if they leave the Armed Forces at or beyond either the Early Departure Point or the Immediate Pension Point. If a scheme member leaves before these points, they will be entitled to a preserved pension and related lump sum.

8.151 Further details about Armed Forces Pensions can be found at the website www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/Personnel/SPVA/Pensions.htm

Cash Equivalent Transfer Value

8.152 A Cash Equivalent Transfer Value (CETV) is the actuarially-assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the pension scheme, not just their service in a senior capacity to which disclosure applies. The figures include the value of any pension benefit in another scheme or arrangement which the individual has transferred to the AFPS or Civil Service pension arrangements. They also include any additional pension benefit accrued to the member as a result of their purchasing additional pension

benefits at their own cost. CETVs are calculated in accordance with the guidelines and framework prescribed by the Institute and Faculty of Actuaries and do not take account of any actual or potential reduction to benefits resulting from Lifetime Allowance Tax which may be due when pension benefits are taken.

Real Increase in CETV

8.153 This reflects the increase in CETV that is funded by the employer. It does not include the increase in accrued pension due to inflation or contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market valuation factors for the start and end of the period.

Civil Service and Other Compensation Schemes – Exit Packages

(This section has been subject to audit)

8.154 The figures in the following table are in respect of redundancy and other departure costs paid in accordance with the provisions of the Civil Service Compensation Scheme (CSCS). Where the

Department has agreed early retirements the costs are met by the MOD and not by the Civil Service Pension Scheme. The table includes 166 individuals who retired early on ill-health grounds during 2010-11 (2009-10: 159); their total accrued pension liabilities for the year amounted to £984,000 (2009-10: £1,004,000).

8.155 The value of exit packages for staff who left under the former compulsory, flexible or approved early retirement terms, is the capitalised cost of the whole package (including annual compensation payments or early enhanced pensions). For staff who left under the new voluntary exit or voluntary redundancy terms, the cost used includes any top-up to compensation provided by the Department to buy out the actuarial reduction on an individual's pension.

8.156 In addition to the exit packages detailed above the Department may occasionally make use of early release schemes to reduce the number of civilian staff who are not members of the CSCS, for example locally employed staff in Germany and Cyprus, teachers and nursing staff.

8.157 Members of the Armed Forces Pension Scheme who leave before the age of 55 may be entitled to an Early Departure Payment (EDP); these payments are not included above. Details of the EDP scheme are set out at Note 9.4 to the accounts.

Exit Package Cost Band	Number of Compulsory Redundancies		Number of Other Departures Agreed		Total Number of Exit Packages by Cost Band	
	2010-11	2009-10	2010-11	2009-10*	2010-11	2009-10
<£10,000	-	-	89	79	89	79
£10,000 – £25,000	-	-	164	138	164	138
£25,000 – £50,000	-	-	145	140	145	140
£50,000 – £100,000	-	-	135	211	135	211
£100,000 – £150,000	-	-	51	73	51	73
£150,000 – £200,000	-	-	8	61	8	61
£200,000 – £250,000	-	-	-	33	-	33
£250,000 – £300,000	-	-	1	10	1	10
£300,000 – £350,000	-	-	1	2	1	2
£350,000 – £400,000	-	-	-	1	-	1
Total Number of Exit Packages	-	-	594	748	594	748
	£000	£000	£000	£000	£000	£000
Total Resource Cost	-	-	26,331	53,423	26,331	53,423

* The figures for Number of Other Departures Agreed in 2009-10 is subject to review – any changes to the figures above will be published in the 2011-12 accounts.

Ursula Brennan
Accounting Officer

11 July 2011

Part Two – Annual Accounts

Statement of Accounting Officer's Responsibilities

Under the Government Resources and Accounts Act 2000, HM Treasury has directed the Ministry of Defence to prepare for each financial year resource accounts detailing the resources acquired, held or disposed of during the year and the use of resources by the Department during the year.

The accounts are prepared on an accruals basis and must give a true and fair view of the state of affairs of the Department and of its net resource outturn, changes in taxpayers' equity, and cash flows for the financial year.

In preparing the accounts, the Accounting Officer is required to comply with the requirements of the *Government Financial Reporting Manual* and in particular to:

- observe the Accounts Direction issued by HM Treasury, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards, as set out in the *Government Financial Reporting Manual*, have been followed, and disclose and explain any material departures in the accounts; and
- prepare the accounts on a going-concern basis.

HM Treasury has appointed the Permanent Head of Department as Accounting Officer of the Department. The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which the Accounting Officer is answerable, for keeping proper records and for safeguarding the Department's assets, are set out in the Accounting Officers' Memorandum issued by HM Treasury and published in *Managing Public Money*.

Statement on Internal Control

1. Scope of responsibility

As Accounting Officer I have responsibility for maintaining a sound system of internal control that supports the achievement of Defence policies, aims and objectives, whilst safeguarding the public funds and Departmental assets for which I am personally responsible, in accordance with the responsibilities assigned to me in Managing Public Money.

During the 2010-11 financial year the Department's outputs were delivered through four Trading Fund Agencies, three Executive Non-Departmental Public Bodies (NDPBs), one Public Corporation and seven Top Level Budgets (TLBs).

- The four MOD Trading Funds (The Defence Support Group (DSG), the Defence Science and Technology Laboratory (Dstl), the UK Hydrographic Office, and the Met Office) fall outside the Departmental Accounting Boundary and their Chief Executives are Accounting Officers in their own right. Given their close integration into the MOD's business, potential impact on MOD outputs and their extensive use of Departmental personnel and assets, their Chief Executives provide to me their Statement on Internal Control prepared for their Annual Accounts. In addition, a departmental representative sits on their Management Boards, whilst Ministers, supported by an Owners Board, are responsible for setting the Trading Funds top level objectives, approving major business decisions including their Corporate Plans and setting annual key targets.
- The three Executive NDPBs (National Museum of the Royal Navy, National Army Museum, and Royal Air Force Museum) and one Public Corporation, although sponsored by the Department, also fall outside the Departmental Boundary and their accounts are published separately. The NDPBs operate within a financial memorandum agreed between their respective Boards of Trustees and the MOD. The Public Corporation (Oil and Pipelines Agency) has a Board of Directors on which the MOD is represented.
- The Armed Forces Pension Scheme (AFPS) and the Armed Forces Compensation Scheme (AFCS) are administered by the Service Personnel and Veterans Agency (SPVA). Payments to eligible individuals under AFPS and AFCS fall outside the Departmental Accounting Boundary and have separate, published accounts for which I am also the Accounting Officer. The administration costs of both schemes and employer's contributions are within the scope of the Departmental boundary and fall within the Central Top Level Budget.

Top Level Budget Holders operate within a framework of responsibilities delegated by me. To assist me in assessing the adequacy of control arrangements across the Department, they submit to me an annual statement of assurance, endorsed by their Audit Committee and Management Board. Included within the Top Level Budgets are five on-vote Defence Agencies, whose Chief Executives are responsible for producing annual accounts which are laid before Parliament, but which also form part of the Departmental Resource Accounts. The Top Level Budget Holders are responsible for setting the operating framework of the Agencies in their area through a Framework Document, for agreeing performance targets and for monitoring progress.

- Central TLB
 - Defence Vetting Agency
 - MOD Police and Guarding Agency
 - People, Pay and Pensions Agency
 - Service Personnel and Veterans Agency
- Land Command TLB
 - Service Children's Education

Command and administration of the Armed Forces is vested by Letters Patent in the Defence Council, chaired by the Secretary of State for Defence, and beneath that in the three Service Boards, each chaired by a Minister. Membership of the Defence Council comprises all Defence Ministers and the executive members of the Defence Board. The Chief of the Defence Staff is the Government's and the Secretary of State's principal advisor on military operations and is responsible for the maintenance of military operational capability and

for the preparation and conduct of military operations, including managing the risks to successful outcomes. The Chiefs of Staff Committee is chaired by the Chief of the Defence Staff and is the main forum in which the collective military advice of the Chiefs is obtained on operational issues. The individual Service Chiefs also advise the Chief of the Defence Staff, the Secretary of State and, when required, the Prime Minister on the operational employment of their Service.

A Defence Ministerial Committee was established in April 2008, which brings together Ministers with the Department's most senior officials, to ensure that Ministers collectively are engaged more regularly on decisions affecting Defence.

The Defence Board, which I chair, ensures that the Strategy for Defence and the Defence Plan are carried out by using a corporate governance system that has two inter-related processes: performance management and assurance. The Board comprises senior executive members of the Department and at least two external independent members. Beneath the Defence Board sits a number of sub-committees and boards, including:

- the Defence Operating Board, which is responsible for executing and ensuring delivery of the decisions and direction issued from the Defence Board
- the Defence Audit Committee, which has a remit to review and challenge constructively the adequacy of internal controls and risk management and assurance processes within the Department;
- the Investment Approvals Board, which takes the lead in examining investment proposals and providing advice on them to Ministers, and;
- the Defence Board Sub-Committee on Equipment, with responsibility for determining an equipment plan and equipment support plan.

2. The purpose of the system of internal control

Defence is a complicated business, which is supported and run by a large complex organisation. It is important, therefore, to have the appropriate governance systems in place.

The system of internal control is designed to manage risk to a reasonable level. Internal control is based on processes designed to identify and prioritise the risks to the achievement of Departmental policies, aims and objectives, to evaluate the likelihood of those risks being realised and the impact this would have, and to manage them efficiently, effectively and economically. The system of internal control has been in place in the MOD for the year ended 31 March 2011 and up to the date of approval of the Annual Report and Accounts, and accords with HM Treasury guidance.

3. Capacity to handle risk

Active management of risk is fundamental to the effective achievement of Defence objectives, and is central to the way business is conducted within the Department. It informs operational decision making, contingency planning, investment decisions and the financial planning process. Guidance on the Department's approach to risk is detailed in a Joint Service Publication (JSP). This guidance is cascaded down through Top Level Budget Holders and is available to all staff on the MOD's intranet. Individual training is available to all staff via the Department's in-house training provider.

4. The risk and control framework

The new Defence Performance Framework (brought into effect on 01 April 2010) provides the focus for the Department's processes to identify, report and manage strategic performance and risk. It provides a tool for top down ownership and direct leadership by the Defence Board. It requires lower level management boards to embed performance and risk management processes in their businesses that enable them to manage performance and risk and to provide accurate and timely management information to the Board's quarterly and annual performance and risk reviews.

The Defence Board Strategic Objectives identified by the Defence Board and embedded in the Defence Plan provide the short-term focus. These support the long-term focus articulated in the Strategy for Defence and Defence Strategic Direction. The Defence Performance Framework polices and assesses strategic performance and risk providing the information and insight necessary for the Defence Board to provide timely direction and guidance. These business requirements cascade from the Defence Strategic Direction, Defence Plan and subordinate sub-Strategies. The cross-cutting sub-Strategies (owned by Process Owners) ensure compliance with legal and regulatory requirements, and other binding policies, standards and rules on behalf of the Defence Board.

In addition, the Defence Board has identified 8 Risks to Strategic Aims and 6 Major Failure Risks. These are monitored and reviewed by the Board during the quarterly and annual performance and risk reviews. A Better Risk Management review concluded in April 2011. The main workstreams included: establishing a Risk Group, chaired by the Director General Finance, to identify the Department's key risks and drive a risk focussed culture back into the business; a review of the Defence Board's set of Strategic Risks, to drive top down risk management, and; defining the department's tolerance of risk. These workstreams will be implemented over the next year.

The Department's tolerance of risk varies between the different areas of Defence business. Military operations are inherently risky. The level of risk that Ministers agree to accept is based on advice from senior military and civilian officials. Every effort is made to provide personnel and assets with proper protection through planning, equipment and training, but we ultimately rely on the judgment of Force Commanders to manage the risks on a day to day basis. On the non-operational side the Defence Board now receives regular Security, Business Continuity and Health & Safety reports. This year has seen a rise in the number of non-operational fatalities from eight to sixteen. There is no common factor that explains the rise, and the Defence Analytical Services and Advice have advised that, because the absolute number of fatalities is small, the rise may not be statistically significant.

The Defence Audit Committee, chaired by an external independent member of the Defence Board, reviews the Department's approach to internal control and provides independent advice to the Defence Board and me as Accounting Officer. The Committee adopts a strategic approach, challenging the overall risk identification and assessment processes and pulling together all the strands of independent assurance. It co-ordinates the activities of internal audit, and draws on annual reports from pan-Departmental Process Owners and specialist assurance sources.

Each Top Level Budget Holder is supported by an Audit Committee, chaired by a non-executive member and at which representatives from the internal and external auditors are present. Like the Defence Audit Committee, these committees focus their activities to provide advice on wider-business risk and assurance processes.

An annual risk-based programme of internal audit is provided by Defence Internal Audit, who are the primary source of independent assurance. The Directorate of Operational Capability provide independent military operational audit and assurance to the Secretary of State and the Chief of the Defence Staff on specific issues.

The Department's external audit function is provided on behalf of Parliament by the Comptroller and Auditor General, supported by staff from the National Audit Office (NAO). NAO see all Defence Audit Committee and TLB Audit Committee papers and attend their meetings.

5. Review of effectiveness

As Accounting Officer, I have responsibility for reviewing the effectiveness of the system of internal control. My review is informed by a report from Defence Internal Auditors, by assurance reviews by Top Level Budget Holders and by Process Owners who have responsibility for the development and maintenance of the internal control framework. I have also taken account of comments made by the external auditors in their management letter and other reports and have been advised by the Defence Board and the Defence Audit Committee.

A number of steps have been taken during 2010-11 to maintain and improve the effectiveness of the system of internal control. These include:

- The implementation of the Defence Performance Framework. As set out above, this is the Department's top-level strategic performance and risk management system. It is designed to support the Defence Board in the continuous evaluation, development, communication and implementation of strategy, through monitoring and analysis of strategic performance information. It has replaced the Defence Balanced Scorecard. It consists of three main elements: an annual Strategic Performance and Risk Report based on seven Key Performance Question and the analysis of Defence Board Strategic Risks; a Quarterly Performance and Risk Report showing progress against Defence Board Strategic Objectives and analysis of levels of risk in the Department; and the annual holding to account of the owners of the sub-strategies that underpin the overarching Strategy for Defence.
- Following work undertaken previously to improve and streamline the Department's assurance process, the revised arrangements governing Process Owners continue to bed-in. This has led to significant improvements in the reports submitted for consideration by the Defence Audit Committee. Most of the Process Owners also own the Sub-Strategy for their area of business. In total, Process Owners are responsible for 13 of the 24 Department's sub-strategies.
- Further improvements have been made to the governance and control of the Joint Personnel Administration system. All of the qualifications of the Accounts relating to JPA have now been lifted. The Assurance and Compliance Working Group was formed in 2009 to address the JPA issues and its successor, the Assurance Steering Group has continued to do good work addressing the issues raised. Some issues remain, particularly on charging for food and accommodation, but I am satisfied that the new mechanisms provide effective control. This will be particularly important in managing the risks that arise from the imminent technical refresh of the system.

Two further pieces of work were started in 2010-11 that will result in significant changes in the way the Department is controlled:

- The Defence Reform Review, led by Lord Levene This is a fundamental examination of how the Ministry of Defence is structured and managed. Its purpose is to develop a new model for Departmental management, with a leaner and less centralised organisation that works and is affordable within the budget set by the Spending Review and has clear allocation of responsibility, authority and accountability. It covers not only structures, processes and governance, but also clarity of purpose, behaviours, culture and incentives. The Review Report was published on 27th June 2011. The findings of the report are summarised in Chapter 6 of the Annual Report.
- New Cabinet Office guidance on Departmental boards, including having a main board chaired by the Secretary of State and with a substantially different balance between executive and non-executive members. The new board met for the first time on the 20th June 2011. The Department was governed through the old structure of the Defence Ministerial Committee and a Defence Board chaired by me throughout 2010-11.

The DIA overall opinion is that of Limited Assurance, based upon the audit and consultancy tasks undertaken throughout 2010-11. The DIA found that existing risk management processes remain overly complex, bureaucratic and did not consistently reflect good practice. They recommended a fresh direction from the top, which would build upon the significant engagement, interest and enthusiasm they found across the Department for better risk management. The DIA also echoed NAO concerns regarding financial management, inventory and asset management.

The majority of Process Owners in their 2010-11 reports to the Defence Audit committees assessed the level of assurance as being limited. There was a slight improvement on last year, with two process owners (the Surgeon General and the Security process owner) moving from 'limited' to 'substantial' assurance, and one (the Logistics process owner) moving from 'substantial' to 'limited'.

6. Significant Internal Control Issues

Affordability of the Defence Programme

In financial year 2010-11, the Department again had to take significant in-year management action to ensure it remained within the amounts voted to Defence by Parliament. Much of this budgetary pressure was due to the wider fiscal environment, and the fact that longer term decisions depended on the outcome of the SDSR, which did not report until half way through the financial year. My predecessor reported last year that for a variety of reasons, including the deterioration in the general economic context, the Defence programme was unaffordable against the likely available financial provision. The need to cut the deficit resulted in a Comprehensive Spending Review Settlement in October 2010 that reduced the Defence Budget by 7.5% over the next four years, which substantially increased this challenge. The changes announced in the SDSR rectified some of the imbalance, but a significant gap remains. A range of exercises are in hand to reduce the gap further, and inform the Department's next planning round, including an assessment of the costs and affordability of the equipment element of the forward programme accompanied by an independent audit from the NAO.

Managing the risk has been made more difficult by acknowledged weaknesses in the Department's capacity to plan and budget effectively. The Department has made significant changes designed to improve planning and financial accountability, including giving the Director General Finance responsibility for the annual planning round. Further major changes will be made through the implementation of the Defence Reform Review referred to above.

Manpower Reductions

The savings required to live with the Department's reduced budget cannot be achieved without substantial reductions in both Service and Civilian Manpower. The Department has had restrictions in place on the recruitment of civilians for some time, and announced earlier this year an early release scheme for civilians and redundancies for Service Personnel. The Department will need to decide whether to release a significant number of people before key pieces of work have concluded, including detailed implementation of the Defence Reform Review. This leads to a risk that we allow the wrong people to leave. This risk is being managed by assessing which skills will be important, and ensuring that this is taken into account in decisions about which people should leave. For civilians, this is made more difficult by weaknesses in the information that the Department holds on skills. The reductions, coupled with changes to terms and conditions and the financial position, also pose a risk to the morale of both the Armed Forces and civil servants.

Manpower reductions are also having a direct effect on the control environment, as posts supporting assurance are gapped or cut, particularly in support of Business Continuity. There also remains a shortage of Suitably Qualified and Experienced personnel in several key areas, including Safety and Security. Posts critical to meeting the Department's Health and Safety obligations are explicitly excluded from restrictions on recruitment.

Inventory and Stock Control

Weaknesses regarding Bowman and Stock Control that were previously identified by the NAO remain, but improvements are being made. For Bowman, an Asset Management Plan has been developed to address governance and accounting issues. We are working with the contractor, General Dynamics, to ensure we receive good quality management information and improve internal processes for reporting damaged/destroyed assets, particularly those arising in operational theatre. The Chief of Defence Materiel, as logistics process owner, is leading a review of the stock control issues. A Programme Board has been established to direct the development of essential improvements to current processes, information management systems, policy and practice. This will ensure implementation of effective solutions to material and financial accounting problems within the End to End Supply Chain. These initiatives will take time to resolve the problem. I therefore expect that control issues will remain in these areas for the next two to three years.

Unauthorised Disclosures

Leaks from within the Department remain damaging and resource intensive to manage; they reached new levels during the SDSR and have continued at a high level ever since. Leaking damages trust between Ministers, civil servants and the Military and they undermine the Chain of Command. They have also made internal communications more difficult, which further raises the risk to morale. We are taking vigorous step to ensure that the rules are rigorously enforced.

Condition of the estate

Resource constraints have led to a lack of investment in both the fuels and explosives estates, posing a risk to both the environment and safety. For the fuels environment, the single greatest challenge remains the aging infrastructure, and now continues to operate through a mix of stop-gap maintenance, careful risk management and reactive funding. This risk has been mitigated to an extent by an improved reporting and assurance regime. The condition of the Explosive Estate remains a concern, which is being closely managed. The Department's requirements for ammunition storage are currently being reviewed in the light of the SDSR. The results of this review and the subsequent action plan will influence the level of risk.

Ursula Brennan
Accounting Officer

11 July 2011

The Certificate of the Comptroller And Auditor General To The House Of Commons

I certify that I have audited the financial statements of the Ministry of Defence for the year ended 31 March 2011 under the Government Resources and Accounts Act 2000. These comprise the Statement of Parliamentary Supply, Statement of Comprehensive Net Expenditure and the Statement of Financial Position, the Statement of Cash Flows, the Statement of Changes in Taxpayers' Equity and the related notes. These financial statements have been prepared under the accounting policies set out within them. I have also audited the information in the Remuneration Report that is described in that report as having been audited.

Respective responsibilities of the Accounting Officer and auditor

As explained more fully in the Statement of Accounting Officer's Responsibilities, the Accounting Officer is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit, certify and report on the financial statements in accordance with the Government Resources and Accounts Act 2000. I conducted my audit in accordance with International Standards on Auditing (UK and Ireland). Those standards require me and my staff to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Department's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Department; and the overall presentation of the financial statements. In addition I read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my certificate.

In addition, I am required to obtain evidence sufficient to give reasonable assurance that the expenditure and income reported in the financial statements have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

Opinion on Regularity

In my opinion, in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

Basis for Qualified Opinion on Financial Statements

The Ministry of Defence has not complied with the Financial Reporting Framework as it has not accounted for the expenditure, assets and liabilities arising from certain contracts in accordance with IAS 17 *Leases* as interpreted by IFRIC 4 *Determining whether an Arrangement Contains a Lease*. Consequently, the Ministry of Defence has omitted a material value of assets and liabilities from its Statement of Financial Position as at 1 April 2009, 31 March 2010 and 31 March 2011. This has also led to a consequential material misstatement of the Statement of Comprehensive Net Expenditure for 2009-10 and 2010-11 and Statement of Parliamentary Supply for 2010-11. I am unable to quantify the impact on the financial statements because the Ministry of Defence has not maintained the records or obtained the information required to comply with International Financial Reporting Standards in this respect.

In addition, the evidence available to me was limited due to a failure to maintain adequate accounting records, operate adequate stocktaking and asset verification procedures, and perform sufficient impairment review. Consequently I was unable to obtain sufficient, appropriate audit evidence to support the accounting for certain inventory and non-current assets (5.3bn); and the valuation of a further unquantifiable value of inventory and non-current assets which may require impairment because the associated asset platforms have been taken out of service. I have also been unable to assess the accuracy, occurrence and completeness of the associated transactions in the Statement of Comprehensive Net Expenditure.

In addition, I have been unable to obtain sufficient, appropriate audit evidence to support the corresponding 2009-10 figures.

Qualified Opinion on Financial Statements

In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraph:

- the financial statements give a true and fair view of the state of the Department's affairs as at 31 March 2011 and of its net cash requirement, net resource outturn and net operating cost, for the year then ended; and
- the financial statements have been properly prepared in accordance with the Government Resources and Accounts Act 2000 and HM Treasury directions issued thereunder.

Opinion on other matters

In my opinion:

- the part of the Remuneration Report to be audited has been properly prepared in accordance with HM Treasury directions made under the Government Resources and Accounts Act 2000; and
- the information given in Part One; Section B: *Delivering Defence* for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception

In respect of the lack of accounting records held by the Department to support the proper application of IAS 17 and the limitations on my work relating to certain inventory and non-current assets, described above:

- I have not obtained all the information and explanations that I considered necessary for the purposes of my audit; and
- Proper accounting records have not been maintained.

I have nothing to report in respect of the following matters which I report to you if, in my opinion:

- the financial statements and the part of the Remuneration Report to be audited are not in agreement with the accounting records or returns; or
- the Statement on Internal Control does not reflect compliance with HM Treasury's guidance.

Opinion on Votes A

The Ministry of Defence's Votes A is presented annually to Parliament to seek statutory authority for the maximum numbers of personnel to be maintained for service with the armed forces. Note 35 to the Accounts shows that the maximum numbers maintained during 2010-11 for the Naval, Army and Air Force Services in all active and reserve categories were within the numbers voted by Parliament. My role is to inform Parliament whether or not the approved Estimates (Vote A) have been exceeded.

In my opinion, the numbers provided for in the Estimate have not been exceeded.

Report

My report, which follows, provides further detail of my audit opinions on the financial statements.

Amyas CE Morse

Comptroller and Auditor General

National Audit Office

157 – 197 Buckingham Palace Road

Victoria, London SW1W 9SP

15 July 2011

Report of the Comptroller and Auditor General on the 2010-11 Accounts of the Ministry of Defence

Introduction

1. The Ministry of Defence (the Department) Annual Accounts for 2010-11 report a net operating cost of some £47.1 billion and assets of some £127.9 billion mainly consisting of land, buildings, fighting equipment and stores together with gross liabilities of some £21.3 billion.
2. Since my last report the Department has announced the results of the Strategic Defence and Security Review (SDSR) and its Comprehensive Spending Review (CSR) settlement. These announcements have led to decisions about the future of major defence platforms, including the cessation of the Nimrod project and the retirement of the Harrier fleet. As presented in the financial statements, these decisions have had a significant impact on the Department's financial performance and position. The Department has recognised in the Statement on Internal Control that a significant gap remains between the anticipated cost of the Defence Programme, and the likely available funding; prior to the SDSR the funding gap through to 2020 was quantified as £38bn. The Department is undertaking exercises to significantly reduce the scale of the deficit, but recognises the uncertainty and challenge of addressing this gap.
3. In this context, decisions may be required which give rise to further significant cancellations of capital projects or withdrawal from service of existing asset platforms. The financial statements have been prepared using the historic cost convention modified for the revaluation of non-current assets, this presumes that the value of assets will be realised through continuing use. While I consider this to remain an appropriate basis for the Statement of Financial Position at 31 March 2011, the valuation of these assets could be significantly lower if the Department was unable to fund its continued use of assets or the existing equipment programmes to completion.
4. While the Department has made some progress in addressing the issues raised in my previous reports on the accounts much of this progress has been the result of labour intensive manual processes. Following the SDSR, the Department has commenced a programme of redundancies for both civilian and military personnel, without substantial improvement in existing systems progress might not be sustainable.

The purpose of my report

5. This Report explains the basis for the qualification of my audit opinion on the 2010-11 Annual Accounts and provides an update on the actions taken by the Department to address the issues identified in my Report on the 2009-10 Annual Accounts⁷.

My obligations as Auditor

6. Under the Government, Resources and Accounts Act 2000 (the Act) I am required to examine and certify the financial statements of all central government Departments. International Standards on Auditing (UK and Ireland) require me to obtain evidence to give reasonable assurance that the Department's financial statements are free from material misstatement. In forming my opinion I examine, on a test basis, evidence supporting the disclosures in the financial statements and assess the significant estimates and judgements made in preparing them. I also consider whether the accounting policies are appropriate, consistently applied and adequately disclosed. I am also required to satisfy myself that, in all material respects, the expenditure and income shown in the Annual Accounts have been applied to the purposes intended by Parliament and conform to the authorities that govern them.
7. Votes A for the Ministry of Defence is presented annually to Parliament to seek statutory authority for the maximum numbers of personnel to be maintained by the Armed Forces. Note 35 to the accounts discloses the number voted by Parliament and the maximum numbers maintained during 2010-11 for the Royal Navy, Army and Royal Air Force in all active and reserve categories. My role is to inform Parliament whether or not the approved Estimates (Votes A) have been exceeded.

⁷ HC 258 2009-10 Ministry of Defence Annual Report and Accounts 2009-10

Qualified opinion due to material error arising from adopting accounting policies which do not fully comply with International Financial Reporting Standards as adapted or interpreted for the public sector context by the Government Financial Reporting Manual (FRoM), and a limitation of scope due to the inadequacy of evidence to support certain expenditure and balances in the financial statements.

Accounting for lease-type arrangements

Qualified audit opinion

8. I have qualified my opinion for a second year because the Department has not complied with the accounting requirements for determining whether a contract contains a lease and has therefore omitted a material value of assets and liabilities from its Statement of Financial Position. I cannot quantify the impact of this on the accounts with certainty because, as a result of its accounting policies, the Department has not maintained the records, or obtained the information required to do so.

Accounting requirements

9. In preparing its accounts, the Department must comply with the requirements of the Government Financial Reporting Manual (FRoM). Since 2009-10 the FRoM has required the adoption of International Financial Reporting Standards (IFRS) by UK central government bodies. IFRS⁸ requires preparers of accounts to establish whether lease-type contracts are in substance a lease, and then to consider whether these contracts have the characteristics of either a finance or operating lease. These decisions have a significant impact on the financial statements because if the contract is classified as a finance lease then, rather than simply recording contract expenditure as it is incurred in year in the Statement of Comprehensive Net Expenditure (SoCNE), the valuation of assets used to deliver the service would be recognised in the Statement of Financial Position (SoFP) alongside a liability for the minimum lease payments due under the contract.

10. While these considerations have not had a material impact in many other areas of the public sector they are of particular relevance to the Ministry of Defence. It necessarily enters into strategic arrangements with key contractors to procure specialist defence platforms on a non-competitive basis, for example in relation to surface ships, submarines and aircraft. These arrangements may provide for the exclusive, or near exclusive use of industrial assets and capability which have only limited utility to other customers. Consequently, the contractual terms, which are covered by the Government Profit Formula and its Associated Arrangements (GPFAA)⁹, may give rise to the Department controlling the significant majority of the outputs of the supplier's assets involved in the arrangement. For example, where shipyards are used exclusively on defence contracts and the pricing of the contract recognises this by allowing recovery of fixed costs other than through market rate or unit cost pricing. As such, these arrangements may be considered to contain a lease under IFRS, and may have the characteristics of a finance lease.

Action by the Department

11. As part of the work undertaken in 2009-10 when it first adopted IFRS, the Department assessed its Private Finance Initiatives and Public Private Partnership contracts against the revised accounting requirements but it did not carry out this assessment for other contractual arrangements. Based on the results of its work, the Department believes that there may be a number of its contracts which would require disclosure as leases, including as finance leases (notes 1.49-1.50). Given the potential number and size of the contracts involved, there is likely to be material understatement of the assets and liabilities recognised in its financial statements.

12. Last year the Department undertook to account for new contracts, entered into from 2010-11, with a view to achieving full compliance with accounting requirements over time. Following the announcements in the SDSR and the potential impact on existing contracts and the supplier base, the Department has now put on hold further work to achieve compliance until contract re-negotiations have been completed.

13. The Department does not currently have the information to measure the value of the assets and liabilities associated with these arrangements in order to comply with reporting requirements. In my opinion if this information were available and presented in the financial statements the consequences of a potential decision to exit or scale back a finance lease type arrangement would be more transparent to the reader of

8 The key relevant accounting standards and interpretations are: International Financial Reporting Issues Committee Interpretation 4: Determining whether an arrangement contains a lease (IFRIC 4) and International Accounting Standard 17 Leases (IAS 17)

9 The GPFAA, also commonly referred to as the Yellow Book, is agreed by Government and industry, as represented by the CBI, and is subject to periodic review by an independent review board.

the accounts, for example the loss of asset utility would be disclosed as an impairment cost.

Recommendations for further action

14. I continue to recommend that the Department carries out further work to identify contracts where the risk of inappropriate accounting treatment is highest and targets further efforts on higher value, higher risk contracts. This work should be undertaken as contract renegotiations complete.

Non-current assets and inventory

Limitation on the scope of my opinion

15. I have limited the scope of my opinion in relation to certain non-current and inventory assets recorded within the Statement of Financial Position. The limitation arises due to the Department being unable to provide me with sufficient evidence to support:

- the accounting for military equipment in the form of BOWMAN radios (£0.1bn);
- the accounting for certain inventory and capital spares¹⁰ (£5.2bn); and
- the valuation of a further unquantifiable amount of inventory and capital spares, where the associated asset platforms have been taken out of service, and for which inadequate assessment of impairment has been made.

16. The scope of my opinion on the 2009-10 and 2008-09 accounts was also limited in relation to weaknesses in the controls over inventory and the evidence to support the valuation and existence of assets. However, due to improvements in the Department's asset verification exercises, I am no longer limiting the scope of my opinion in respect of certain grouped military equipment assets (£0.6bn).

Bowman radios

17. Bowman is a tactical communications system, with an overall net book value of £1.52bn. Locating Bowman communication equipment represents a challenge for the Department. This is due to the different tracking systems used at different locations where radios are used, and as a consequence of the underlying tracking data relying on manual processes and inputs. Furthermore, the individual assets move around more rapidly, for example between military units, the repair loop and operations.

18. My audit found that of the 50,893 radio sets recorded on the system (an increase of 5,961 on 2009-10), the Department could only provide supporting evidence in the form of serial numbers and location data for 37,645. The Department uses estimates based on other alternative forms of evidence to support the existence of the remaining radios, and due to improvements in the quality of some of these estimates I have been able to review evidence to support a further 9,155 radios. However, the department was unable to provide any suitable evidence to support the existence of 4,093 radios. Currently only 74 per cent of radios are recorded by serial number, the Department does not therefore have sufficient processes in place to monitor and control these assets.

19. In forming my opinion I have excluded the value of those radios where there was either insufficient evidence to support existence, or where I considered the estimates used to support the probable existence to be inadequate for the purposes of my opinion. I estimate that there is inadequate evidence to support around £125 million (2009-10 £184m) of Bowman radios held on the SoFP, and I have therefore excluded these from the scope of my audit opinion.

Recommendations for further action

20. In order to address the weaknesses highlighted by my audit the Department should ensure that sufficient focused effort is given to addressing the underlying problems, in particular the Department should:

- improve the robustness of the quarterly Bowman reconciliations, focusing on the quality of data input to inventory management systems by users; and

¹⁰ Capital spares are major spares for military equipment which are capitalised in the accounts. They are managed through the same processes and systems as inventory.

- ensure that any future IT solutions are matched with appropriate processes to accurately record all radios by serial number.

Inventory and Capital Spares

21. I reported last year that certain key controls over inventory were ineffective and that discrepancies between inventory counts and warehouse management records at the main Joint Supply Chain Services (JSCS) non explosives depots did not form a reliable basis for quantifying the value of inventory held on the SoFP.

22. Following my reports, the Department's Materiel and Financial Accounting Project Board and JSCS agreed a strategy to address inventory control weaknesses; the Department is only two years into the implementation of this strategy which has included:

- focusing effort towards higher value warehouses and inventory items;
- initiating an additional programme of location checks, with the aim of significantly reducing the levels of inventory omitted from warehouse system records; and
- approved new IT solutions which will aim to reduce the risk of error and improve the efficiency of stock management.

The Department considers that from 2014 these new systems will begin to impact on the underlying inventory system weaknesses.

23. While some progress has been made a number of significant issues will remain until the strategy is fully implemented. Consequently the Department remains unable to provide sufficient evidence to adequately support inventory and capital spares balances within the financial statements, giving rise to my scope limitation. The main areas of weaknesses relate to:

- discrepancies between inventory counts and warehouse management records;
- inadequate impairment of inventory and capital spares; and
- unreconciled differences between the warehouse system records and the accounting system.

Discrepancies between inventory counts and warehouse management records

Completeness of inventory

24. The sample testing carried out by my staff to verify warehouse records against inventory on the shelf identified significant levels of inventory that were not recorded on the warehouse system. Due to the level and nature of these errors it is not possible to estimate, with sufficient accuracy, the change in value which would result if all such discrepancies had been identified and corrected, or to assess the consequent impact on the SoFP and the SoCNE.

25. Following my previous recommendation that the Department should improve its completeness checks an enhanced process of location checks was undertaken during the year, covering the three main non-explosives depots. Following this exercise error levels of this type have reduced slightly when compared with 2009-10. However my audit testing identified an average of 7 per cent of items tested which were not recorded in warehouse systems. Where items are not recorded on warehouse systems their value cannot be captured in the financial records, and this error rate continues to lead me to limit the scope of my audit opinion.

Existence of inventory

26. The testing carried out by my staff to verify warehouse records to physical inventory holdings has identified a reduction in existence error rates when compared to last year. Higher value inventory items were significantly more accurate, reflecting the focus of JSCS's efforts. Although the level of inaccuracy remains high by location (16%) the results of my testing indicate that the level of inaccuracy by value is in the region of £17 million, and I consider that this level of net error is sufficient to support evidence of existence.

Inadequate assessment of impairment of inventory and capital spares

27. My audit considered how the Department assesses its inventory and capital spares holdings to ensure that the appropriate value is reflected in its accounts and that adequate assessment of impairment has been made. Assets can become impaired, most usually due to deterioration of their physical condition or because of obsolescence. Being able to identify and record the condition of inventory is critical for operational reasons in enabling the repair, replenishment and disposal of inventory, as well as ensuring that only functional inventory is distributed for use. Identifying obsolete inventory is also important in reducing storage costs.

28. I have previously reported limitations in management information and a lack of clarity in Departmental guidance for assessing impairment. Following my recommendations the Department has undertaken a number of initiatives to improve the processes it operates to assess impairment. The Department conducted a centralised sample review of slow-moving inventory lines, representing some 25 per cent of total non-explosive inventory, resulting in a net write down of £325m. The Department plans to undertake further work in future years, recognising that impairment assessment is not systematically or routinely undertaken.

29. Information held in the warehouse data systems indicates that there are significant levels of inventory held at JSCS depots that are unlikely to be used. For example, the warehouse management systems showed that, at the year end, some 44 per cent by value of non-explosive inventory at depots was recorded in a condition which prevented immediate issue. This has led me to limit the scope of my opinion over the valuation of the £5.2bn of inventory and capital spares held in these depots (2009-10: £5.4bn).

30. Following decisions in the SDSR to take certain asset platforms out of service, the Department has not fully assessed the impact, through impairment review, on the utility of the associated inventory and capital spares. A review of these assets may have given rise to the impairment of assets currently valued in the SoFP. This has led me to further limit the scope of my opinion, but due to the lack of information I am unable to quantify the value of inventory and capital spares that might be affected.

Inability to fully reconcile warehouse system records with accounting systems

31. The Department remains unable to perform a full reconciliation between the financial accounting and warehouse systems, although some progress has been made. The Department continues to run a large number of legacy warehousing systems which are difficult to integrate due to age and incompatibility. The Department plans a long-term solution of fewer host systems, coupled with improved processes. The investment in the new Base Inventory Management Systems (BIMS) is underway and the Department expects it to be delivered in 2014, and that this will rationalise the reconciliation process.

32. Despite progress there remains a high level of unexplained discrepancy, particularly in respect of two key system interfaces where I am unable to obtain assurance that information passes with sufficient accuracy from warehouse to accounting systems. Had I not already limited the scope of my opinion these reconciliation deficiencies would represent a significant limitation in the evidence available to me. It should remain a key focus for the Department to reconcile the financial systems to the underlying accounting records held on inventory systems.

Recommendations for further action

33. I welcome the way in which the Department has responded to my previous recommendations and acknowledge that it has adopted a strategy to address these issues over a number of years. However, further improvements are required:

- JSCS should revisit and improve its procedures for shelf to system checks to drive down the level of stocks not recorded;
- further develop and escalate the initiatives to ensure inventory is assessed for impairment, particularly in light of the SDSR impacts;
- continue to develop the present initiatives to improve the reconciliation process between the various inventory systems to support the financial statements; and
- as the current process weaknesses are addressed in the short-term it is important that the Department designs more efficient and effective processes to operate with the planned new IT systems.

Progress on previous areas of qualification

Grouped military equipment assets

34. Last year I reported on the challenges facing the Department in maintaining adequate records for grouped military equipment assets, MAESTRO, with a value of £0.6bn. For the last two years I have reported weaknesses in the MAESTRO census, which verifies existence and condition of these assets. Last year this exercise delivered low return rates of around 83 per cent and identified high levels of discrepancies, resulting in limitation in the scope of my opinion. Following my previous report the Department has sought to improve the MAESTRO census results by raising the profile of the census exercise; completing it earlier; and putting a greater premium in resolving discrepancies identified through the census.

35. The census return levels for 2010-11 have improved to over 92 per cent and the Department identified fewer discrepancies; resulting in only £55m of assets having insufficient evidence to support existence. The results of this exercise are now sufficient to provide me with evidence for the purposes of providing an opinion on these balances.

Single living accommodation and food charges income from service personnel

36. In 2009-10, I limited the scope of my opinion due to the inadequacy of evidence to support the completeness of income recorded in the accounts at £87 million, relating to charges made to personnel.

37. During 2010-11 more detailed analysis has been carried out by the Department which provides sufficient assurance that the income from charges made to personnel is complete in all material respects. I have, therefore, not limited the scope of my opinion in this regard this year. The Department plans to introduce monthly checks at unit level, this will enhance the assurance which the Department has to ensure the completeness of charges made to personnel. However, the Department will need to ensure that it establishes mechanisms to collate the results of these reviews.

Votes A – approved maximum numbers of personnel

38. In 2008-09 and 2009-10, I was unable to obtain sufficient evidence to support the accuracy of certain categories of service personnel numbers reported to Parliament; I was therefore unable to report whether or not the approved estimates (Votes A) had been exceeded in respect of the Reserve Land Forces and the Royal Naval Reserve List 7.

39. During 2010-11 the Department has undertaken a data cleansing exercise on the Joint Personnel Administration system used to collate this information. My audit procedures have confirmed that this now provides a reliable basis to support service personnel numbers reported to Parliament in respect of all categories. I have, therefore, not qualified my audit opinion in this regard this year.

Amyas CE Morse

Comptroller and Auditor General
National Audit Office
157 – 197 Buckingham Palace Road
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15 July 2011

Statement of Parliamentary Supply

Summary of Resource Outturn 2010-11

Request for Resources	Note	Estimate			Outturn			2010-11 Net Total Outturn Compared to Estimate Saving / (Excess) £000	2009-10 Total Net Outturn*** £000
		Gross Expenditure £000	A in A* £000	Net Total £000	Gross Expenditure £000	A in A* £000	Net Total £000		
1	2	54,006,180	1,471,544	52,534,636	46,414,424	1,418,718	44,995,706	7,538,930	37,389,091
2	2	3,343,077	58,368	3,284,709	2,924,496	34,002	2,890,494	394,215	2,681,835
3	2	972,691	-	972,691	935,066	-	935,066	37,625	979,641
Total Resources**	3.1	58,321,948	1,529,912	56,792,036	50,273,986	1,452,720	48,821,266	7,970,770	41,050,567
Non-Operating Cost A in A*	7			297,126			103,235	193,891	119,071

* Appropriation-in-Aid

** The total net resource outturn for 2010-11 of £48,821,266,000 includes the net effect of £1,680,211,000 resulting from a change in accounting policy in respect of leased land. Further details of the changes are at Note 3.1.

*** Following a change in accounting policy by HM Treasury the notional Cost of Capital Charge is no longer included in the accounts. Prior Period Adjustments (PPAs) arising from the removal were not included in Spring Supplementary Estimates for 2010-11, other than as a note, on the basis that the PPA numbers could have been misleading. The impact of this accounting policy change on the Supply outturn in respect of 2009-10 would have been a reduction in the outturn of £3,827,560,000 from £41,050,567,000 to £37,223,007,000.

Net Cash Requirement 2010-11

	Note	Estimate £000	Outturn £000	2010-11 Net Total Outturn compared to Estimate Savings/ (Excess) £000	2009-10 Outturn £000

Summary of Income Payable to the Consolidated Fund

(In addition to appropriations-in-aid, the following income relates to the Department and is payable to the Consolidated Fund (cash receipts being shown in *italics*)).

	Note	Forecast 2010-11		Outturn 2010-11	
		Income £000	Receipts £000	Income £000	Receipts £000
Total	5	-	-	43	43

Notes 1 to 34 which follow the Statement of Changes in Taxpayers' Equity form part of these accounts.

Statement of Parliamentary Supply

Approval of the Spring Supplementary Estimate (SSE) increased the Department's Resources Estimate by £18Bn. The figure was unusually high because the SSE included an initial estimate of the non-cash resource implications of the SDSR. These initial estimations had to be made in time for the publication of the SSE in February 2011 and were included, to avoid exceeding the limits of Parliamentary expenditure, despite the high degree of uncertainty over the final costs and the timing of SDSR decisions. Consequently, the Estimates Memorandum stated that the final outcome would be subject to adjustment.

Planning and implementation of the SDSR involves wide ranging impacts on people, equipment, inventory and the estate (including relocations, closures and disposals); these impacts will continue throughout 2011-12 and beyond. Production of the 2010-11 accounts has highlighted that the prudent provision of funding via the SSE, in attempting to provide for all possible impacts of the SDSR, has not been matched by actual costs in 2010-11. Many of the SDSR decisions have taken time to refine with actual costs now falling into later years or not materialising at all.

Some of the difficulties in refining and identifying costs for the 2010-11 accounts included: uncertainty over extensions to equipment on operations; the timing of work to examine detailed changes in capability and the resulting withdrawal of equipment and supporting spares and inventory; the time taken to identify and negotiate the potential sale of equipment as operational and/or spares or scrap; and the identification of inventory relating to specific equipment and decisions on sale or re-use by other equipment programmes.

The Net Resource Outturn is £48,821M. This means there is a surplus of £7,971M against the Net Resource Estimate of £56,792M. £394M of the underspend is in respect of the additional costs of military operations (RfR2) an area of the Department's activity that can vary significantly depending on conditions on the ground. A further £38M underspend is in respect of war pensions (RfR3) and is consistent with the reducing number of pensioners.

The balance of the underspend, £7,539M, consists of:

- £3,200M included in the Estimate for inventory writes off following withdrawal of equipment. Detailed work is ongoing to identify the total inventory writes off – only £800M in respect of Nimrod, Harrier and Tornado, was included in the 2010-11 accounts;
- a surplus of £840M relating to movements in indexation factors and movements in foreign exchange derivatives both of which did not materialise;
- a surplus of £400M relating to the write off of vehicles. Funding was included for the write off of tanks and artillery (AS90) but the identification of specific vehicles has not progressed sufficiently for inclusion of actual costs in the 2010-11 accounts.
- £1,200M included in the Estimate for additional writes off of assets and assets under construction; the Estimate assumed sufficient progress would have been made to enable accounting action to be taken in the 2010-11 accounts – this was not the case;
- a £265M surplus after the write off of ships (4 Type 22 frigates, HMS Ark Royal, RFAs Fort George and Largs Bay) and aircraft (Harrier and Nimrod MRA4) being the difference between the estimate and the actual costs incurred in 2010-11;
- a £243M surplus on the £1,923M estimate included in the SSE for the effect of a change in accounting policy for leased land;
- A further surplus of £1,391M arose against the Estimate for write off of other assets and provision for the future costs of staff reductions (£857M). These costs were included in the Estimate on the assumption that sufficient progress would have been made to enable accounting provisions (estimates of costs with uncertain timing) to be included in the 2010-11 accounts – this was not the case.

In 2011-12 the Department will continue its planning and implementation of the SDSR and when required the costs will be reflected in the Estimates process and subsequently in the annual accounts.

Statement of Comprehensive Net Expenditure (SoCNE)

for the year ended 31 March 2011

	Note	2010-11 £000	2009-10 £000
Administration Costs			
Staff costs	9.2	1,669,656	1,653,573
Other administration costs	10	357,195	485,085
Gross administration costs		2,026,851	2,138,658
Operating income		-	-
Net administration costs before interest		2,026,851	2,138,658
Net interest payable / (receivable)	13	(839)	2,183
Net administration costs		2,026,012	2,140,841
Programme Costs			
Staff costs	9.2	11,095,970	10,577,316
Other programme costs*	11	34,875,994	26,296,606
Gross programme costs		45,971,964	36,873,922
Operating income	12	(1,316,348)	(1,408,555)
Net programme cost before interest		44,655,616	35,465,367
Net interest payable*	13	463,252	436,537
Net programme cost**		45,118,868	35,901,904
Net operating cost**	3.1	47,144,880	38,042,745

Other Comprehensive Expenditure

for the year ended 31 March 2011

	Note	2010-11 £000	2009-10 £000
Receipt of donated assets	SoCITE	(71,436)	(32,032)
Net gain on revaluation of property, plant and equipment	SoCITE	(1,856,591)	(1,763,312)
Net gain on revaluation of intangible assets	SoCITE	(898,878)	(1,279,016)
Net (gain) / loss on revaluation of assets held for sale	SoCITE	(3,524)	17,758
Net gain on revaluation of inventories	SoCITE	(629,247)	(547,151)
Net (gain) / loss on pensions	SoCITE	(60,367)	90,206
Impairments / (Impairment Reversals) not included in operating costs	3.1	(3,868)	27,993
Additional depreciation and asset writes-on	SoCITE	(19,779)	(102,299)
Depreciation and impairment on donated assets	SoCITE	124,626	101,913
Total Other Comprehensive Expenditure		(3,419,064)	(3,485,940)
Total Net Comprehensive Expenditure		43,725,816	34,556,805

* As a result of the reclassification of a lease for land from an operating to a finance lease the 2009-10 other programme costs have increased by £614,471,000 and programme – net interest payable has increased by £48,041,000. Further details are at Notes 11 – Other Programme Costs, 13 – Net Interest Payable and 34 – Prior Period Adjustments.

** Following HM Treasury direction the cost of capital charge, a non-cash notional charge is no longer included in the accounts. The charge for 2009-10 (£3,827,560,000) has been removed from the comparator figures – reducing the net programme cost and the net operating cost.

Notes 1 to 34 which follow the Statement of Changes in Taxpayers' Equity form part of these accounts.

Statement of Financial Position (SoFP)

as at 31 March 2011

	Note	31 March 2011		31 March 2010		1 April 2009	
		£000	£000	£000	£000	£000	£000
Non-current assets							
Intangible assets	14	27,106,428		29,133,566		27,959,218	
Property plant and equipment*	15	88,300,099		91,652,802		89,877,182	
Financial assets		206,362		224,057		217,200	
Receivables due after more than one year	20.1	886,718		882,592		1,088,330	
Total non-current assets			116,499,607		121,893,017		119,141,930
Current assets							
Financial assets held for sale	16.6	1		1		1	
Non-current assets held for sale	18	122,899		83,062		124,820	
Inventories	19	7,719,673		7,183,855		6,647,386	
Trade and other receivables	20.1	2,500,610		2,707,343		2,230,178	
Financial assets	16.6	349,512		513,611		1,110,800	
Cash at bank and in hand	21	683,901		677,357		913,570	
Total current assets			11,376,596		11,165,229		11,026,755
Total assets***			127,876,203		133,058,246		130,168,685
Current liabilities							
Trade and other payables due within one year*	22.1	(10,149,137)		(9,246,607)		(9,078,494)	
Financial liabilities	16.6	(102,976)		(30,984)		-	
Total current liabilities			(10,252,113)		(9,277,591)		(9,078,494)
Non-current assets plus net current assets			117,624,090		123,780,655		121,090,191
Non-current liabilities							
Provisions	23	(5,485,042)		(5,706,669)		(5,734,204)	
Other payables*	22.1	(5,539,526)		(5,396,420)		(5,310,580)	
Total non-current liabilities***			(11,024,568)		(11,103,089)		(11,044,784)
Assets less liabilities**			106,599,522		112,677,566		110,045,407
Taxpayers' equity							
General fund*	SoCITE		82,105,470		87,141,370		85,164,114
Revaluation reserve	SoCITE		22,140,112		23,023,741		22,401,843
Donated assets reserve	SoCITE		2,353,940		2,512,455		2,479,450
			106,599,522		112,677,566		110,045,407

* Prior period figures have been restated following changes in accounting policy which resulted in the removal of the Cost of Capital Charge and the recognition of leasehold land and its related current and non-current liabilities for lease payments. Further details of the changes are at Note 34 – Prior Period Adjustments.

** The value of assets and liabilities accounted for under leases is understated because contracts, particularly strategic procurement arrangements with key contractors, have not been assessed under IFRIC 4; further details are at Notes 1.47 to 1.50 to the accounts

*** Changes in the value of total assets and total non-current liabilities include movements in respect of early decisions arising from the Strategic Defence and Security Review (SDSR). The figure for total assets includes a reduction of £6,189,000,000 as a result of the effect of: writes off of equipment and associated inventory, cancellation or early withdrawal of equipment e.g. Nimrod MR44 and Harrier and reductions in value due to accelerated depreciation and impairment. Liabilities include provisions (£130,000,000) for the first stages of staff early release schemes and accruals (£465,000,000) for the impact of initial contract re-negotiations. Additional impacts will occur during 2011-12 as a result of further decisions, to be taken following the SDSR.

Ursula Brennan
Accounting Officer

11 July 2011

Notes 1 to 34 which follow the Statement of Changes in Taxpayers' Equity form part of these accounts.

Statement of Cash Flows

for the year ended 31 March 2011

	Note	2010-11 £000	2009-10 £000
Cash flows from operating activities			
Net operating cost	SoCNE	47,144,880	38,042,745*
Adjustments for non-cash transactions		(18,410,126)	(10,497,312)*
Increase / (Decrease) in trade and other receivables		(191,760)	281,789
Less movements in receivables relating to items not passing through operating costs		112,244	(239,885)*
Increase / (Decrease) in inventories		599,289	497,525
Increase / (Decrease) in assets held for sale		137,602	9,696
(Increase) / Decrease in trade payables		(1,045,636)	(253,953)*
Less movements in payables relating to items not passing through operating costs		(229,017)	(303,376)*
Movement in derivatives not passing through operating costs		(192,182)	(357,567)
Use of provisions including movement due to change in discount rate		236,224	749,544
Net cash outflow from operating activities		28,161,518	27,929,206
Cash flows from investing activities			
Purchase of property, plant and equipment	15	8,068,447	7,746,377
Purchase of intangible assets	14	1,364,660	1,270,879
Less movements in payables relating to purchases of PPE and intangibles		(211,510)	(2,208)
Proceeds of disposal of property, plant and equipment		(64,267)	(79,042)
Loans to other bodies	16.18	-	15,079
(Repayments) from other bodies	16.18	(11,121)	(8,222)
Net cash outflow from investing activities		9,146,209	8,942,863
Cash flows from financing			
From the consolidated fund (Supply) – current year		(37,517,074)	(37,064,006)*
From the consolidated fund (Supply) – prior year		-	(120,807)
From the consolidated fund – settlement of prior year receivable		(239,885)	-
Repayment of loans from the National Loans Fund	22	2,270	2,141
Capital element of payments in respect of finance leases and Service Concession Arrangements		197,834	178,974
Net financing		(37,556,855)	(37,003,698)
Net increase / (decrease) in cash and cash equivalents in the period before adjustment for receipts and payments to the Consolidated Fund		249,128	131,629
From the consolidated fund (Supply) – prior year		-	(120,807)
Consolidated Fund Extra Receipts (prior year) paid over		(242,541)	(242,795)
Consolidated Fund Extra Receipts (current year) paid over		(43)	(4,240)
Net increase / (decrease) in cash and cash equivalents in the period after adjustment for receipts and payments to the Consolidated Fund		6,544	(236,213)
Cash and cash equivalents at the beginning of the period	21	677,357	913,570
Cash and cash equivalents at the end of the period	21	683,901	677,357

* Restated to reflect the removal of the notional Cost of Capital Charge, the adjustments in respect of the change in accounting treatment of leased land from an operating lease to a finance lease (further details of these changes are at Note 34 – Prior Year Adjustments) and the separate disclosure of the movement in receivables not passing through operating costs.

Notes 1 to 34 which follow the Statement of Changes in Taxpayers' Equity form part of these accounts.

Statement of Changes in Taxpayers Equity

for the period ended 31 March 2011

	Note	General Fund £000	Revaluation Reserve £000	Donated Asset Reserve £000	Total Reserves £000
Balance at 31 March 2009*		83,431,462	22,401,843	2,479,450	108,312,755
Prior period adjustment – leased land treated as a finance lease	34	1,732,652	-	-	1,732,652
Balance at 1 April 2009		85,164,114	22,401,843	2,479,450	110,045,407
Parliamentary Funding – drawn down in-year		37,064,006	-	-	37,064,006
Parliamentary Funding (prior year) – deemed funding		120,807	-	-	120,807
Parliamentary Funding – Supply receivable	20	239,885	-	-	239,885
Income not classified as A-in-A – paid to the Consolidated Fund		(4,240)	-	-	(4,240)
CFER** – Excess A-in-A in RfR1 payable to the Consolidated Fund	22	(242,541)	-	-	(242,541)
Adjustments to Service Concession Arrangements		-	-	7,447	7,447
Non-cash charge – auditors remuneration	10	3,600	-	-	3,600
Net operating costs	SoCNE	(38,042,745)	-	-	(38,042,745)
Other net comprehensive expenditure:					
Receipt of donated assets	SoCNE	-	-	32,032	32,032
Net gain on revaluation of property, plant and equipment	SoCNE	-	1,668,094	95,218	1,763,312
Net gain on revaluation of intangible assets	SoCNE	-	1,279,016	-	1,279,016
Net loss on revaluation of assets held for sale	SoCNE	-	(17,758)	-	(17,758)
Net gain on revaluation of inventories	SoCNE	-	547,151	-	547,151
Net (loss) / gain on pensions	SoCNE	(90,206)	-	-	(90,206)
Impairments / (Impairment Reversals) not included in operating costs	SoCNE	-	(27,993)	-	(27,993)
Transfer between reserves and additional depreciation	SoCNE	2,928,690	(2,826,612)	221	102,299
Release of reserves to operating cost to offset donated asset depreciation	SoCNE	-	-	(101,913)	(101,913)
Balance at 31 March 2010*		87,141,370	23,023,741	2,512,455	112,677,566
Parliamentary Funding – drawn down in-year		37,517,074	-	-	37,517,074
Parliamentary Funding – Supply receivable	20	127,641	-	-	127,641
Income not classified as A-in-A – paid to the Consolidated Fund	5	(43)	-	-	(43)
CFER** – Excess A-in-A in RfR2 payable to the Consolidated Fund	22, 5	-	-	-	-
Non-cash charge – auditors remuneration	10	3,100	-	-	3,100
Net operating costs	SoCNE	(47,144,880)	-	-	(47,144,880)
Other net comprehensive expenditure:					
Receipt of donated assets	SoCNE	-	-	71,436	71,436
Net gain on revaluation of property, plant and equipment	SoCNE	-	1,962,438	(105,847)	1,856,591
Net gain on revaluation of intangible assets	SoCNE	-	898,878	-	898,878
Net loss on revaluation of assets held for sale	SoCNE	-	3,524	-	3,524
Net gain on revaluation of inventories	SoCNE	-	629,247	-	629,247
Net (loss) / gain on pensions	SoCNE	60,367	-	-	60,367
Impairments / (Impairment Reversals) not included in operating costs	SoCNE	-	3,868	-	3,868
Transfer between reserves and asset writes-on	SoCNE	4,400,841	(4,381,584)	522	19,779
Impairment and release of reserves to operating cost to offset depreciation and impairment on donated assets	SoCNE	-	-	(124,626)	(124,626)
Balance at 31 March 2011		82,105,470	22,140,112	2,353,940	106,599,522

* Following HM Treasury direction, the non-cash notional Cost of Capital Charge (CoCC) is no longer included in the accounts. The total charge included in the accounts in the period since the introduction of Resource Accounting in 2001-02, to 31 March 2009 was £29,504,852,000. The CoCC in 2009-10 was £3,827,560,000. HM Treasury directed that removal of the CoCC should not be included as a Prior Period Adjustment in the 2010-11 Resource Outturn. The net impact of the notional CoCC on the General Fund is nil and its removal therefore also has no impact on the General Fund balances.

** Consolidated Fund Extra Receipt

Notes 1 to 34 which follow the Statement of Changes in Taxpayers' Equity form part of these accounts.

Notes to the Accounts

1. Statement of Accounting Policies

Introduction

1.1 These financial statements have been prepared in accordance with the 2010-11 International Financial Reporting Standards (IFRS) Government Financial Reporting Manual (FReM) issued by HM Treasury except that IFRIC 4 – Determining whether an Arrangement Contains a Lease, has not been applied. Further information on the reasons for this non-application and its impact on the financial statements are given in Notes 1.49 to 1.50 below. The accounting policies contained in the FReM apply IFRS as adapted or interpreted for the public sector context. Where the FReM permits a choice of accounting policy, the accounting policy which is judged to be the most appropriate to the particular circumstances of the Department for the purpose of giving a true and fair view has been selected. The particular policies adopted by the Department are described below. They have been applied consistently in dealing with items that are considered material to the accounts and comply with the requirements of the FReM except where HM Treasury has approved the following departures to enable the Department to reflect its own particular circumstances:

- The FReM's requirement for Departments to prepare accounts that present the transactions and flows for the financial year and the balances at the year end between "core" Department and the consolidated group in respect of the Statement of Comprehensive Net Expenditure (and supporting notes) and Statement of Financial Position (and supporting notes) has not been applied. Since agencies falling within the Departmental Boundary are on-vote and embedded within the Departmental chain of command, HM Treasury permits them to be treated as an integral part of the "core" Department. Throughout these accounts, the consolidated figures for the Ministry of Defence (including its on-vote agencies) are deemed to represent those of the "core" Department.
- The Department has not fully complied with the FReM emissions cap and trade scheme accounting requirements on the grounds of materiality. Rather than registering an asset and a liability to reflect its holding of allowances and its obligation to pay for emissions, the Department has reflected the purchase and sale of allowances as expenditure and income within the Statement of Comprehensive Net Expenditure. All other costs associated with the scheme, such as compliance checking, are also charged to the Statement of Comprehensive Net Expenditure.
- On the grounds of materiality, the Department, in applying IFRIC 1 – Changes in Existing Decommissioning, Restoration and Similar Liabilities – uses the cost model rather than the revaluation model to measure changes in its capitalised asset provisions.
- On the grounds of materiality, HM Treasury has also agreed that the information normally required by the FReM on Fees and Charges disclosures (paragraph 5.4.30) is not required and the disclosure provided at Note 12.1 is sufficient.

1.2 The Statement of Comprehensive Net Expenditure is analysed between administration and programme costs. Administration costs reflect the costs of running the Department. Programme costs reflect non-administration costs, including payments of grants and certain staff costs where they relate directly to service delivery. The classification of expenditure as administration or as programme follows the definition of administration costs set by HM Treasury except in the following instances which have been approved by HM Treasury:

- All Defence Equipment & Support and Defence Estates staff costs are classified as administration costs.
- All depreciation is classified as a programme cost.

Segmental Reporting

1.3 The Defence Board reviews performance and allocates resources at an aggregated level, varying their mix to meet prioritised changes in activities which, in combination, deliver defence capability. Although the Department is organised into separate budgetary areas for financial management purposes (see Note 2 – Analysis of Net Resource Outturn), it is only by combining the activities undertaken by each of these budgetary areas that the Department is able to deliver its principal output of meeting UK defence commitments. Therefore, on the basis that the Department's business output is not organised on any specific geographic, economic, regulatory, product or service basis, it is deemed appropriate to treat it as a single operating segment.

Accounting Convention

1.4 These financial statements have been prepared under the historical cost convention, modified to include the revaluation of intangible assets, property, plant and equipment assets and inventories.

Basis of Preparation of Department's Annual Accounts

1.5 These financial statements comprise the consolidation of the Department, its Supply financed Agencies and those Advisory Non-Departmental Public Bodies (NDPBs) sponsored by the Department, which are not self-accounting. The Defence Agencies and the Advisory NDPBs sponsored by the Department are listed in Note 33.

1.6 Four of the Department's agencies are established as Trading Funds and produce their own accounts. As they fall outside Voted Supply, the Department's interests are included in the financial statements as non-current financial assets. Executive NDPBs operate on a self-accounting basis and are not included within the consolidated accounts. They receive grant-in-aid funding from the Department, which is treated as an expense in the Statement of Comprehensive Net Expenditure.

1.7 The Armed Forces Pension Scheme (AFPS) is not consolidated within these financial statements. Separate accounts are prepared for the AFPS. Further details are available at: <http://www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/Personnel/Pensions/ArmedForcesPensionsAndRedundancy.htm>

Critical Accounting Judgements and Key Sources of Estimation Uncertainty

1.8 Preparation of the Department's Annual Accounts requires significant judgements and estimates to be applied in order to arrive at the value of Departmental assets and liabilities and likewise the amount of revenue and expenses to be reported during the accounting period. The key areas in which judgements and estimates have been used are described below.

Non-Current Assets

1.9 Intangible non-current assets and plant and equipment assets are expressed at their fair value through the application of indices produced by Defence Analytical Services and Advice (DASA). DASA supplied indices are also applied to property assets during periods between the quinquennial revaluations undertaken by external professional valuers. Details are provided in paragraphs 1.29 and 1.30.

1.10 The useful economic life of an equipment asset is assessed by reference to its estimated out of service date and for other assets on the basis of their estimated period of utility to the Department. There is an inherent uncertainty in estimating the annual depreciation charge and the carrying amount of a tangible non-current asset, for example an increase in the useful economic life will decrease the depreciation charged to the Statement of Comprehensive Net Expenditure during the year and increase the asset's carrying amount at financial year end.

1.11 The out of service date for tangible non-current assets is subject to change depending on factors such as strategic defence policy and predicted obsolescence. The economic lives of non-current assets are regularly reviewed and, where appropriate, revised to reflect changing circumstances such as decisions reflected in the latest finalised Planning Round. During the next financial year the useful economic life of some assets will change as a result of the Strategic Defence and Security Review (SDSR) as explained in

paragraph 1.16. Further details are also provided in paragraph 1.38.

Inventories

1.12 Where inventories are not expected to be used, an estimated financial provision is applied to their carrying value to reduce it to net realisable value. Details are given in Note 19.

Accruals

1.13 Where expenditure has been incurred but not invoiced an estimate is made of the amount to be accrued. Accruals are listed in Note 22.

Nuclear Decommissioning

1.14 Provisions have been made for the cost of decommissioning facilities and for the treatment, storage, and disposal of nuclear waste arising from operations at MOD sites. Provisions are also included for the future cost of decommissioning operational nuclear submarines and likewise for the cost of decommissioning those which have reached their out of service date.

1.15 In calculating the provisions, an estimate has been made of the cash flows required to settle the obligations. Key assumptions in this estimate are the time period over which the provisions are estimated, the costs for the future storage and decommissioning of waste, the VAT rate and the discount rate used. While the discount rate applied to the future cash flows is subject to assumptions, the Department has used the discount rate mandated by HM Treasury. Full details on how nuclear decommissioning provisions have been calculated are included in Note 23.2.

Strategic Defence and Security Review

1.16 Formal decisions over the future of Nimrod MRA4, the Harrier fleet and a number of Royal Navy and Royal Fleet Auxiliary vessels have already been announced. As a result assets will be withdrawn from service early or subject to a reduction in capability and a number of equipment programmes will be cancelled.

1.17 Contracts affected by SDSR decisions are being renegotiated on a sector by sector basis, starting with aviation. Where settlements have already been reached with industry the financial impact has been accrued in the 2010-11 accounts.

1.18 It is estimated that the Department will have to assess and potentially re-negotiate as many as 500 contracts. Settlements reached to date represent only a small proportion of this total. Until the Department commences negotiations on the balance of the contracts we cannot estimate the potential scale of future cancellation and restructuring claims and, therefore, there is insufficient evidence to justify the creation of a provision. However, a contingent liability is disclosed in Note 28.1.

1.19 To supplement existing internal policy guidance, finance guidelines were issued to commercial staff involved in negotiating settlements with industry. Furthermore specific guidance on how to report and account for assets withdrawn from service early as a result of SDSR decisions was also issued to finance staff.

1.20 Accounting for SDSR changes is described below.

1.21 Where a project is cancelled prior to completion, the Assets under Construction balance and any associated capitalised development costs are written off to the Statement of Comprehensive Net Expenditure.

1.22 Where an asset is withdrawn from service during the current financial year and this is earlier than its planned out of service date:

- The asset is classified as an asset held for sale if it is estimated that the sale is highly probably within 12 months. The asset is valued at the lower of its carrying amount and its fair value less costs to sell and any reduction in value is recognised as an impairment. No further depreciation is applied.

- If the asset is not expected to generate a receipt, the value of the asset is written off to the Statement of Comprehensive Net Expenditure.

1.23 If an asset will be withdrawn from service after the current financial year, depreciation is accelerated to reflect the fact that the asset's planned out of service date has been brought forward.

1.24 If an asset is due to remain in service but at a reduced capability, its carrying amount is impaired to reflect its revised service potential.

Changes During FY 2010-11 Which Have Affected the Preparation of These Annual Accounts

1.25 The main changes in accounting policies and accounting estimates in 2010-11 were:

- The Statement of Comprehensive Net Expenditure replacing the Operating Cost Statement.
- The removal of the notional cost of capital charge. In line with HM Treasury advice, prior period adjustments arising from the removal of the cost of capital charge were not included in Spring Supplementary Estimates for 2010-11, other than as a note, on the basis that the numbers could have been misleading. The impact of this accounting policy change on the Supply outturn for 2010-11 would have been a reduction in the outturn of £3,828m from £41,051m to £37,223m.
- All non-current asset impairments resulting from a clear consumption of economic benefit are now charged to the SOCNE. Such impairments were previously charged to the revaluation reserve.
- As a result of a change in IAS 17 – Leases, the land element of land and buildings leases must now be assessed against the situations and indicators of a finance lease. This resulted in the land element of a significant land and buildings lease being reclassified from an operating to a finance lease. The gross value of the land which is now accounted for as a finance lease is £3,559,068,000.
- The increase in the capitalisation threshold for non-current assets from £10,000 to £25,000. The impact of this is to decrease the non-current asset balance by £250,000,000.
- Withdrawing the Statement of Operating Costs by Departmental Strategic Objectives and replacing it with the disclosures required by IFRS 8 – Operating Segments. Details are provided in Notes 1.3 and 24.

Recent Changes to Regulations Affecting the Preparation of Future Annual Accounts

1.26 The 2011-12 FReM introduces a number of changes. Those most applicable to the Department are:

- The Departmental Accounting Boundary will be extended to include all those bodies listed in Statutory Instrument 2011 No. 723 – The Government Resources and Accounts Act 2000 (Estimates and Accounts) Order 2011, which came into force on 1 April 2011.
- The format of the Statement of Parliamentary Supply and its supporting note will be aligned to the revised format introduced by HM Treasury's Clear Line of Sight initiative.
- Assets donated by third parties will continue to be capitalised on receipt but their value will be recognised as income in the Statement of Comprehensive Net Expenditure unless the donation is subject to a condition which requires the income to be deferred. This differs from the current treatment of crediting the value to the Donated Asset Reserve. The balance on the Donated Asset Reserve at 31 March 2011 is £2,353,940,000.

Net Operating Costs

1.27 Costs are charged to the Statement of Comprehensive Net Expenditure in the period in which they are incurred and matched to any related income. Details of exit packages are included in the Remuneration Report. Costs of contracted-out services are included net of recoverable VAT. Other costs are VAT inclusive, although a proportion of this VAT is recovered via a formula agreed with HM Revenue and Customs. Surpluses and deficits on disposal of assets classified as held for sale and inventories declared for disposal are included within Notes 10 – Other Administration Costs and 11 – Other Programme Costs.

1.28 Income from services provided to third parties is included within operating income, net of related VAT. In accordance with IAS 10, as interpreted by the FReM, Trading Fund dividends are recognised as operating income on an accruals basis, whilst other dividends are recognised in the year in which they are declared.

Non-Current Assets

1.29 The Department's capitalisation threshold is £25,000. This was changed from £10,000 during the year. The impact of this change was a decrease in the non-current asset balance of approximately £250,000,000 and a corresponding charge to operating cost. Intangible and property, plant and equipment assets are expressed at their fair value through the application of the Modified Historical Cost Accounting Convention (MHCA). Prospective indices, which are produced by DASA, are applied at the start of each financial year to the non-current assets which fall within the categories listed below. These indices look ahead to the Reporting Period date and include calculations to reflect the difference between the actual change in prices during the prior year and the prospective indices used for that year. In addition, where there is a material difference between the indices for year end and those used throughout the year, the MHCA calculations are performed again, using the up to date indices at the year end. The value of the overseas estate assets is similarly adjusted to take account of the year-end exchange rates. Categories of indices used are:

- Land (by region and type);
- Buildings – Non Dwellings (UK and specific overseas indices);
- Buildings – Dwellings (UK and specific overseas indices);
- Single Use Military Equipment – Air Systems;
- Single Use Military Equipment – Sea Systems;
- Single Use Military Equipment – Land Systems;
- IT and Communications Equipment – Communications Equipment;
- IT and Communications Equipment – Office Machinery and Computers;
- Plant and Machinery – specific UK index covering all assets;
- Transport – Fighting Equipment;
- Transport – Other; and
- Assets Under Construction – index applicable to the underlying tangible asset category.

1.30 Property assets are also subject to a quinquennial revaluation by external professional valuers in accordance with IAS 16 – Property, Plant and Equipment, as interpreted by the FReM. Property assets are valued in one of two ways depending on their use. Non-specialist properties are valued at fair (i.e. market) value. For in-use non specialist properties, fair value is interpreted as market value for existing use. Specialist property for which there is no external market is valued at depreciated replacement cost. The majority of Service Families Accommodation is valued at depreciated replacement cost due to the positioning of housing in certain areas or as a result of the lack of an alternative market for certain holdings due to their remote geographic locations. Where market value for existing use is more appropriate, for example for small numbers of houses in a single location, this basis of valuation has been applied.

1.31 Assets under construction are valued at cost and are subject to indexation. On completion, balances are released from the project account into the appropriate asset category.

Intangible Non-Current Assets

1.32 Research costs are charged to the Statement of Comprehensive Net Expenditure in the period in which they are incurred.

1.33 Development costs are capitalised where the project is expected to result in an asset which will enter service. Those not capitalised are charged to the Statement of Comprehensive Net Expenditure. Capitalised development costs are amortised, on a straight line basis, over the planned operational life of the resultant asset, e.g. class of ship or aircraft. Amortisation commences when the asset type first enters operational service within the Department. If it is decided to withdraw the whole class of an asset type early, then any residual unamortised development costs relating to that class are written off to the Statement of Comprehensive Net Expenditure, along with the value of the underlying property, plant and equipment non-current assets.

1.34 Externally purchased software including licences (other than for the operating system which is treated as part of the computer hardware and where appropriate capitalised as a tangible non-current asset) are capitalised where they contribute to the provision of services or other Departmental outputs for a period in excess of one year. Capitalised software is amortised, on a straight line basis, over the shorter of either the economic life or the licence period.

Property, Plant and Equipment Non-Current Assets

1.35 The useful economic lives of property, plant and equipment non-current assets are reviewed annually and adjusted where necessary.

1.36 It is the Departmental capitalisation threshold which determines whether or not an asset is recorded on the Department's Non-Current Asset Register (NCAR). During the year this threshold was increased from £10,000 to £25,000 although Agencies are still permitted to apply a lower capitalisation threshold to those assets which form part of their own Statement of Financial Position.

1.37 The Departmental threshold of £25,000 is not applied to individual capital spares and assembled Guided Weapons Missiles and Bombs (GWMB). Instead, for accounting purposes, these items are treated as pooled assets and included within the Single Use Military Equipment category of non-current assets. GWMB and capital spares are depreciated and the depreciation charge in the Statement of Comprehensive Net Expenditure also includes the cost of GWMB fired to destruction.

1.38 The principal asset categories, together with their useful economic lives, are set out in the table below. All the assets are depreciated on a straight line basis.

	Category	Years
Land and Buildings	Land	Not depreciated unless it is held under a finance lease.
	Buildings (dwellings and non-dwellings):	
	– permanent	40 – 50
	– temporary	5 – 20
	Leasehold	Shorter of expected life and lease period
Single Use Military Equipment (including GWMB)	Air Systems – Fixed Wing	13 – 35
	Air Systems – Rotary Wing	25 – 30
	Sea Systems – Surface Ships	24 – 30
	Sea Systems – Submarines	28 – 32
	Land Systems – Armoured Vehicles	25 – 30
	Land Systems – Small Arms	10 – 15
Plant and Machinery	Equipment	10 – 25
	Plant and Machinery	5 – 25
Transport	Air Systems – Fixed Wing	25 – 35
	Air Systems – Rotary Wing	15 – 32
	Sea Systems – Surface Ships	20 – 30
	Land Systems – Specialised Vehicles	15 – 30
	Land Systems – Other Standard Vehicles	3 – 5
IT and Communications Equipment	Office Machinery	3 – 10
	Communications Equipment	3 – 30
Capital Spares	Items of repairable material retained for the purpose of replacing parts of an asset undergoing repair, refurbishment, maintenance, servicing, modification, enhancement or conversion.	As life of prime equipment supported
Operational Heritage Assets	Operational Heritage Assets are included within the principal asset category to which they relate.	As other non-current assets

Donated Assets

1.39 Donated assets (i.e. those assets that have been donated to the Department or assets for which the Department has continuing and exclusive use, but does not own legal title, and for which it has not given consideration in return) are capitalised at their current valuation on receipt and are revalued/depreciated on the same basis as purchased assets.

1.40 The Donated Asset Reserve represents the value of the original donation, additions and any subsequent professional revaluation and indexation (MHCA). Amounts equal to the donated asset depreciation charge, impairment costs and any in-year surplus/deficit on disposal are released from this reserve to the net operating cost section of the Statement of Comprehensive Net Expenditure.

Componentisation and Subsequent Expenditure

1.41 The Department's policy on componentisation (the recognition of the cost of replacing part of an asset) is as follows:

- Newly built property assets, with the exception of specialist assets, are not subject to componentisation at the point of initial capitalisation as the cost of any potential component is not significant to the total cost of the asset. Specialist assets such as runways are considered for componentisation.
- Where a property asset is refurbished or part of it replaced, the expenditure is recognised within the carrying amount of the overall asset. For assets above £500,000, the carrying amount of the part which is replaced is de-recognised. The QQR is used to adjust any short term valuation differences.

- Material expenditure on major refits and overhauls in the sea environment are accounted for separately when their value is consumed by the Department over a different period from the life of the corresponding core asset. Refurbishment costs are expensed within the air and land environments, as these costs are considered to be equivalent to an annual depreciation charge.

Impairment

1.42 Impairment charges to the Statement of Comprehensive Net Expenditure occur in circumstances which reduce the carrying amount of property, plant and equipment assets to their recoverable amount. All impairment losses (except for those arising from a clear consumption of economic value or service potential) are written off against the Revaluation Reserve (or Donated Asset Reserve, as appropriate) until the carrying amount of the asset reaches its depreciated historic cost. Impairment losses below this amount are charged to the net operating cost section of the Statement of Comprehensive Net Expenditure. Any reversal of an impairment charge is recognised in the Statement of Comprehensive Net Expenditure to the extent that the original charge was previously recognised there. Any remaining amount is recognised in the Revaluation Reserve.

1.43 All impairment losses arising from a clear consumption of economic value or service potential should be written off to the net operating cost section of the Statement of Comprehensive Net Expenditure. Any balance on the Revaluation Reserve (up to the level of the impairment) is transferred to the General Fund.

Disposal of Tangible Non-Current Assets

1.44 Disposal of assets is handled principally by two specialist internal organisations: Defence Estates for property assets and the Disposal Services Authority for non-property assets.

1.45 Non-current assets are reclassified as held for sale if their carrying amount will be recovered principally through a sales transaction rather than through continuing use. For this to be the case, the asset must be available for immediate sale, subject only to terms that are usual and customary for the sale of such assets. The sale must also be highly probable, being expected to complete within one year.

1.46 When assets are classified as held for sale, they are re-classified as current assets and valued at the lower of their carrying amount and their fair value less costs to sell. No further depreciation is applied.

Leased Assets

1.47 Assets held under finance leases are capitalised as non-current assets and a corresponding liability recognised. The assets are depreciated over the shorter of the lease term or their estimated useful economic life. Rentals paid are apportioned between reductions in the capital obligations included in payables and finance costs charged to the Statement of Comprehensive Net Expenditure. Expenditure under operating leases is charged to the Statement of Comprehensive Net Expenditure in the period to which the charge relates.

1.48 The Department may also enter into arrangements that do not take the legal form of a lease but which give the Department the right to use an asset in return for payment. IFRIC 4 – Determining whether an Arrangement Contains a Lease provides guidance on determining whether such arrangements contain leases. Where leases are identified, they should be classified as operating or finance leases in accordance with IAS 17 – Leases and accounted for in accordance with the accounting policies set out in Note 1.47.

1.49 The Department has not applied IFRIC 4 – Determining whether an Arrangement Contains a Lease to all of its contracts. It is believed that a limited number of significant, largely single source contracts, particularly strategic procurement arrangements with key contractors, would meet the IFRIC 4 definition of containing a lease if they were reviewed against IFRIC 4; and that some of these leases would meet the IAS 17 – Leases definition of a finance lease.

1.50 The impact on the financial statements of not applying IFRIC 4 – Determining whether an Arrangement Contains a Lease is that contractors' assets held under finance leases and the associated liabilities have been excluded from the Statement of Financial Position. Commitments under operating leases and finance leases have also been omitted from Notes 26.1 and 26.2.

Public Private Partnerships (PPP) including Private Finance Initiative (PFI) Transactions

1.51 Where PPP including PFI arrangements fall within the scope of the IFRIC 12 – Service Concession Arrangements definition of Service Concession Arrangements, the infrastructure assets and liabilities are reported on the Department's Statement of Financial Position. Unitary charges are apportioned between reduction in the capital obligation and charges to the Statement of Comprehensive Net Expenditure for service performance and finance costs.

1.52 Where PPP including PFI arrangements are outside the scope of IFRIC 12 – Service Concession Arrangements, the arrangement is assessed to establish whether it contains a lease under IFRIC 4 – Determining whether an Arrangement Contains a Lease. If it does contain a lease, the lease is accounted for as either a finance or an operating lease in accordance with IAS 17 – Leases. Where the arrangement does not contain a lease, the expenditure will be recognised as it falls due.

Financial Instruments

1.53 The Department has foreign currency forward contracts, denominated in US Dollars and Euros, and fuel fixed price swap contracts which are accounted for as derivatives and classified as Held For Trading financial instruments.

1.54 The foreign currency forward purchase contracts are measured at fair value with movements in fair value being charged or credited to the Statement of Comprehensive Net Expenditure. The fair value is measured as the difference between the currency's closing mid-market rate at the date of valuation (representing the spot rate) and the rate stipulated in the contract multiplied by the number of contracted units of currency. The Department obtains the closing mid-market rate from the Financial Times. The forward contracts will only have a fair value up to their date of settlement. Once each contract has been settled, it is removed from the Department's Statement of Financial Position. The forward contracts were purchased from the Bank of England. Details of existing contracts are at Notes 16.9 to 16.11 to the accounts.

1.55 The Department uses fixed price swap contracts to manage its risk of fuel price movements in respect of Aviation Turbine Fuel and Gas Oil. The contracts are measured at fair value with movements in fair value being charged or credited to the Statement of Comprehensive Net Expenditure. The fair value is measured as the difference between the closing average mid-market rate for the two commodities for the calendar month ending with the date of valuation (representing the spot rate) and the rate stipulated in the contract, multiplied by the contracted volumes, in the contracted currency. These values are converted to sterling using the closing mid-market rate on the day of valuation obtained from the Financial Times. The Swap contracts will only have a fair value up to their date of settlement. Once each contract is settled, it is removed from the Statement of Financial Position. Swap contracts are purchased by competitive tender using a panel of banks (the latter chosen following a comprehensive assessment) and the contracting process began in 2010-11 for supply in 2011-12 onwards. Details of existing contracts are at Notes 16.12 and 16.13 to the accounts.

1.56 The Department's loans to Trading Funds are classified within Loans and Receivables and carried at historic cost, less any impairment. Public Dividend Capital is not treated as a financial instrument in the Department's accounts because of the statutory rather than contractual, basis of the investment. The Department's investments in special or 'golden' shares are not recognised on the Statement of Financial Position. The entities in which the Department holds special shares are listed at Note 16.22.

1.57 Receivables, including trade receivables, staff loans and advances are classified as Loans and Receivables and are initially measured at fair value and subsequently at amortised cost. Discounting is relevant to those receivables and loans which carry no rate of interest or a subsidised rate. However, the Department's receivables that are due within 1 year are not discounted on the grounds of materiality. Provisions are only made for specific bad debts.

1.58 Liabilities covering trade payables and accruals are classified as Payables and Accruals and are initially measured at fair value and subsequently at discounted cost. This applies to those liabilities carrying a nil or a subsidised rate of interest. On the grounds of materiality, the Department's liabilities falling due within 1 year are not discounted.

1.59 The Department has not made a provision for arrangements that fall within the scope of a financial guarantee contract on the grounds that there is a very low probability of a claim maturing.

Inventories

1.60 Inventories, which are also referred to as Raw Materials and Consumables (RMC), are recognised on the Department's Statement of Financial Position from the point of acquisition to the point of issue for consumption, sale, write-off or disposal. The point of consumption for Land inventories is the point at which inventory is issued from depots. For Air and Navy inventories, the point of consumption is when inventories are issued from final depots such as an air base or a ship's hold.

1.61 RMC which are expected to be used are valued at the cost of replacing the materiel – i.e. at gross carrying amount or historic cost if not materially different. However, where there is no expectation of consumption or sale in the ordinary course of business, the value is abated by the creation of a financial provision to reduce it to Net Realisable Value. The creation of the financial provision is a charge to the Statement of Comprehensive Net Expenditure. On actual disposal both the gross carrying amount and the previously created provision are written off/released to the Statement of Comprehensive Net Expenditure.

1.62 Some items of RMC, for example munitions, have a limited shelf life and a financial provision is applied throughout the life of the item. This provision is created on a straight line basis. When the item is consumed, written off or disposed of the current cost is charged to the Statement of Comprehensive Net Expenditure along with the credit of any accumulated provision.

Cash and Cash Equivalents

1.63 The Department determines cash as cash in hand and demand deposits (repayable on demand) with any commercial bank or other financial institution. This includes gold coins and deposits denominated in foreign currencies after allowing for unpresented payments and uncleared deposits.

1.64 Cash equivalents are determined as short term, highly liquid investments that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value. Cash and cash equivalents in the Department's Statement of Financial Position comprise balances held at the Office of HM Paymaster General, commercial banks and cash in hand.

Provisions for Liabilities and Charges

1.65 Provisions for liabilities and charges have been established under the criteria of IAS 37 – Provisions, Contingent Liabilities and Contingent Assets and are based on realistic estimates of the expenditure required to settle legal or constructive obligations that exist at the Reporting Period date.

1.66 On initial recognition, the provision is charged to the Statement of Comprehensive Net Expenditure unless the expenditure will provide access to current and future economic benefits, in which case a capitalised asset is created. The carrying amount of the capitalised asset provision is depreciated and charged to the Statement of Comprehensive Net Expenditure over the remaining estimated useful economic life of the underlying asset. The rate advised by HM Treasury is used to discount provisions to current prices – the rate for financial year 2010-11 being 2.2% (2.2% for 2009-10). The discount is unwound over the remaining life of the provision and shown as an interest charge in the Statement of Comprehensive Net Expenditure.

Reserves

1.67 The Revaluation Reserve reflects the unrealised element of the cumulative balance of revaluation and indexation adjustments on non-current assets and inventories (excluding donated assets). The Donated Asset Reserve reflects the carrying amount of assets that have been donated to the Department.

1.68 The General Fund represents the balance of the Taxpayers' Equity.

Pensions

1.69 Present and past employees are mainly covered by the Civil Service pension arrangements for civilian personnel and the Armed Forces Pension Scheme (AFPS) for Service personnel. There are separate scheme statements for the AFPS and Civil Service pensions as a whole. Further details can be found at: www.civilservice-pensions.gov.uk and <http://www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/Personnel/Pensions/ArmedForcesPensionsAndRedundancy.htm>

1.70 Both the AFPS and the main Civil Service pension schemes are unfunded defined benefit pension schemes although, in accordance with the HM Treasury FReM, the Department accounts for the schemes in its accounts as if they were defined contribution schemes. The employer's charge is met by payment of an estimated Superannuation Contribution Adjusted for Past Experience (SCAPE), which represents the cost of providing future superannuation protection for all personnel currently in pensionable employment. For the Principal Civil Service Pension Scheme employer contributions (SCAPE) are calculated using four percentage rates (16.7%, 18.8%, 21.8% and 24.3%) of pensionable pay, based on four salary bands; for the AFPS the rates are approximately equivalent to 40.1% (Officers) and 25.6% (Other Ranks) of pensionable pay. In addition, civilian personnel contribute 1.5% of salary to fund a widow/widower's pension if they are members of classic, and 3.5% if they are members of premium, classic plus or nuvos. The Department's Statement of Financial Position will only include a payable in respect of pensions to the extent that the contributions paid to the pension funds in the year fall short of the SCAPE and widow/widower's pension charges due. Money purchase pensions delivered through employer-sponsored stakeholder pensions have been available as an alternative to all new Civil Service entrants since October 2002.

1.71 The pension schemes undergo a reassessment of the SCAPE contribution rates by the Government Actuary at regular intervals. Provisions are made for costs of early retirement programmes and redundancies up to the normal retirement age and are charged to the Statement of Comprehensive Net Expenditure.

1.72 The Department operates a number of small pension schemes for civilians engaged at overseas locations. The pension scheme liability is included within the total provisions reported at Note 23 – Provisions for Liabilities and Charges. The gain or loss on the change in the discount rate is shown as a movement in the reserves (General Fund).

1.73 The disclosures for the main pension schemes are included in: the Remuneration Report, Note 9 – Staff Numbers and Costs, (see paragraphs 9.3 and 9.4) and on the websites of the Civil Service Pension Scheme and the Armed Forces Pension Scheme.

Early Departure Costs

1.74 The Department provides in full for the cost of meeting pensions up to the normal retirement age in respect of military and civilian personnel early retirement programmes. Early departure provisions under pension scheme rules are discounted at the pensions' discount rate, issued annually by HM Treasury, 2.9% as at 31 March 2011 (1.8% as at 31 March 2010). Pensions payable after the normal retirement age are met by the Armed Forces Pension Scheme for military personnel and by the Civil Service pension arrangements for civilian personnel, however any additional element payable beyond normal retirement age, which derives from the enhancement of reckonable service, continues to be met by the Department. Redundancies are provided for in full.

Foreign Currency

1.75 All transactions that are denominated in a foreign currency are translated into Sterling using the General Accounting Rate (GAR), calculated by staff in the Department's central treasury function, at the date of each transaction. For each currency, the GAR is updated monthly based on spot rates. In respect of US Dollars and Euros the GAR is based on the published spot rate in the week immediately preceding the new month. Exchange differences will arise when a currency transaction is settled at a GAR which differs from the rate used when the transaction was initially recorded. In addition, monetary assets and liabilities are translated at the mid-market closing rate applicable at the Reporting Period date and the exchange differences are reported in the Statement of Comprehensive Net Expenditure. Prior to 1 September 2008, the GAR for the Department's major trading currencies, US Dollars and Euros, was based on the Department's foreign currency forward contract rates.

1.76 Overseas non-monetary assets and liabilities are subject to annual revaluation and are translated at the mid-market closing rate applicable at the Reporting Period date. The exchange differences are taken to the Revaluation Reserve for Departmentally owned assets or to the Donated Asset Reserve for donated assets.

VAT

1.77 The Department is registered for VAT and pays tax on its purchases in accordance with Value Added Tax Act 1994 (VATA94). As it is a non-business organisation, most of the VAT the Department incurs is non-recoverable and therefore a cost to the Department.

Third Party Assets

1.78 Third party assets are assets for which the Department acts as custodian or trustee but in which neither the Department nor the government has a direct beneficial interest. As they are not public assets they are not recorded in the Statement of Financial Position but are reported at note 19.1 to the accounts.

2. Analysis of Net Resource Outturn

Request for Resources 1 Provision of Defence Capability	2010-11							2009-10
	Administration Cost £000	Other Current Expenditure £000	Grants £000	Operating Appropriation in Aid £000	Total Net Resource Outturn £000	Total Net Resource Estimate £000	Total Net Outturn Compared with Estimate £000	Total Net Resource Outturn £000
TLB HOLDER / TLB								
Navy Command	-	2,337,723	12,616	(44,437)	2,305,902	2,306,406	504	2,223,297
Land Forces	-	7,343,371	87,951	(138,169)	7,293,153	7,305,852	12,699	6,635,318
Air Command	-	2,991,531	8,521	(158,285)	2,841,767	2,851,902	10,135	2,812,660
Chief of Joint Operations	-	484,225	441	(16,659)	468,007	428,386	(39,621)	448,750
Defence Equipment & Support	-	23,103,535	916	(330,926)	22,773,525	29,423,378	6,649,853	16,787,956
Central*	-	2,677,994	245,614	(297,095)	2,626,513	2,647,753	21,240	2,719,550
Defence Estates	-	5,067,644	26,330	(433,147)	4,660,827	5,388,373	727,546	3,620,719
Administration Costs	2,026,012	-	-	-	2,026,012	2,182,586	156,574	2,140,841
Total (RfR 1)	2,026,012	44,006,023	382,389	(1,418,718)	44,995,706	52,534,636	7,538,930	37,389,091

* Following a reorganisation, the Central Top Level Budget (TLB) area now includes the Science Innovation Technology TLB which was previously reported separately.

Request for Resources 2 Operations and Peace- Keeping	2010-11							2009-10
	Administration Cost £000	Other Current Expenditure £000	Grants £000	Operating Appropriation in Aid £000	Total Net Resource Outturn £000	Total Net Resource Estimate £000	Total Net Outturn Compared with Estimate £000	Total Net Resource Outturn £000
Programme Rest of the World	-	60,490	-	(785)	59,705	61,033	1,328	53,462
Peace Keeping Rest of the World	-	2,864,006	-	(33,217)	2,830,789	3,223,676	392,887	2,628,373
Total (RfR 2)	-	2,924,496	-	(34,002)	2,890,494	3,284,709	394,215	2,681,835

Request for Resources 3 War Pensions Benefits	2010-11							2009-10
	Administration Cost £000	Other Current Expenditure £000	Grants £000	Operating Appropriation in Aid £000	Total Net Resource Outturn £000	Total Net Resource Estimate £000	Total Net Outturn Compared with Estimate £000	Total Net Resource Outturn £000
War Pensions Benefits								
Programme Costs	-	-	934,606	-	934,606	972,441	37,835	979,641
War Pensions Benefits							-	-
Programme Costs – Far Eastern Prisoners of War	-	-	460	-	460	250	(210)	-
Total (RfR 3)	-	-	935,066	-	935,066	972,691	37,625	979,641
Total Resource Outturn	2,026,012	46,930,519	1,317,455	(1,452,720)	48,821,266	56,792,036	7,970,770	41,050,567

3. Reconciliation of Outturn to Net Operating Cost and Outturn Against Administration Budget

3.1 Reconciliation of Net Resource Outturn to Net Operating Cost

	Note	Outturn £000	Supply Estimate £000	2010-11 Outturn compared with Estimate £000	2009-10 Outturn £000
Net Resource Outturn (Statement of Parliamentary Supply)	2	48,821,266	56,792,036	7,970,770	41,050,567
Adjustment for Write On of Inventory in 2009-10			-	-	432,000
Less non-supply income (Consolidated Fund Extra Receipts included in operating income and interest)	5	(43)	-	43	(246,781)
Adjustment for impairments and impairment reversals included in resource outturn but not passing through Net Operating Cost	SoCITE	3,868	-	(3,868)	(27,993)
Less adjustment for the removal of the Cost of Capital Charge following a change in accounting policy	SoCITE	-	-	-	(3,827,560)
Prior year – add the additional cost (depreciation and impairment less the movement in payables not passing through the OCS) resulting from the change in accounting policy in respect of leased land.	SoCNE	(1,680,211)	-	1,680,211	662,512
Net Operating Cost		47,144,880	56,792,036	9,647,156	38,042,745

3.2 Outturn Against Administration Budget

	Budget £000	2010-11 Outturn £000	Outturn compared with Budget £000	2009-10 Outturn £000
Administration Costs Gross	2,182,586	2,026,012	156,574	2,140,841
Net Administration Costs	2,182,586	2,026,012	156,574	2,140,841

The Department's Administration Cost Regime separately identifies costs, other than the costs of direct frontline service provision or support activities, as Administration. In order to simplify the process two different approaches were applied for determining the Administration cost boundaries; whole budget areas or expenditure against certain accounting codes. Each TLB has agreed its own basis for allocating costs to Administration; an approach that reflects the varying nature of the activities carried out by TLBs.

4. Reconciliation of Net Resources Outturn to Net Cash Requirement

	Note	Estimate £000	Outturn £000	Outturn compared to Estimate £000
Resource Outturn	2	56,792,036	48,821,266	7,970,770
Capital:				
Purchase of non current assets		9,984,397	9,433,107	551,290
Non operating cost A in A:				
Proceeds on sale of non current assets and loan repayments by Trading Funds	7	(297,126)	(103,235)	(193,891)
Accruals adjustments:				
Non-cash transactions-				
Included in operating costs		(26,009,984)	(18,279,494)	(7,730,490)
Prior period adjustments	3.1	(1,923,500)	(1,680,211)	(243,289)
Included in reserves	3.1		3,868	(3,868)
Included in net interest payable			(130,632)	130,632
Non cash movement on derivative			(192,182)	192,182
Changes in working capital other than cash, excluding movements on payables falling due after one year		746,314	(457,731)	1,204,045
Increase in payables falling due after one year			(143,106)	143,106
Use of provisions for liabilities and charges		264,635	236,224	28,411
Adjustment for movements on cash balances in respect of collaborative projects			136,841	(136,841)
Net cash requirement		39,556,772	37,644,715	1,912,057

5. Analysis of income payable to the Consolidated Fund

In addition to Appropriations-in-Aid, the following income relates to the Department and is payable to the Consolidated Fund (cash receipts being shown in italics).

	2010-11 Forecast		2010-11 Outturn	
	Income £000	<i>Receipts</i> £000	Income £000	<i>Receipts</i> £000
Operating income and receipts – excess A in A Request for Resources 1	-	-	-	-
Operating income and receipts – excess A in A Request for Resources 2	-	-	-	-
Other operating income and receipts not classified as A in A	-	-	43	43
Subtotal operating income and receipts payable to the Consolidated Fund			43	43
Other amounts collectable on behalf of the Consolidated Fund	-	-	-	-
Total income payable to the Consolidated Fund	-	-	43	43

6. Reconciliation of income recorded within the Statement of Comprehensive Net Expenditure to operating income payable to the Consolidated Fund

	Note	2010-11 £000	2009-10 £000
Operating Income	12	1,316,348	1,408,555
Income included within other operating costs			
– Refunds of formula based VAT recovery		88,818	74,234
– Foreign exchange gains		41,490	53,903
– Less discounts provided		(60)	(63)
Interest Receivable		6,167	7,501
Gross Income		1,452,763	1,544,130
Income authorised to be appropriated in aid		(1,452,720)	(1,297,349)
Operating Income payable to the Consolidated Fund	5	43	246,781

7. Non-Operating income Appropriations-in-Aid

	Note	2010-11 £000	2009-10 £000
Principal repayments of voted loans	16.18	11,121	8,222
Proceeds on disposal of non-current assets		92,114	110,849
Totals		103,235	119,071

8. Non-Operating income not classified as Appropriations-in-Aid

	Income £000	Receipts £000
Cash receipts surrenderable to the Consolidated Fund	-	-

9. Staff Numbers and Costs

9.1 The average number of full-time equivalent persons employed during the year to 31 March 2011 was: Service 194,690 (2009-10: 196,420) and Civilian 74,858 (2009-10: 76,478). Source: Defence Analytical Services and Advice (DASA).

	Permanent Staff	Temporary Staff	Armed Forces	Ministers and Special Advisors	2010-11 Total	2009-10 Total
Analysis of Staff Numbers	74,670	180	194,690	8	269,548	272,898

In order to align with the total pay costs incurred during the year, shown at paragraph 9.2 below, the calculation of the number of staff uses monthly statistics to identify an average number employed for the year. The figures reflect the number of personnel in organisations within the Departmental Boundary for the Annual Accounts and therefore exclude those in the Trading Funds. The figures for Armed Forces personnel are subject to review. Locally Employed Civilians are all included as permanent staff because the additional detail required to analyse the figures between permanent and temporary is not available. Prior year figures for civilians have been restated following a change in the method of calculating the average civilian strength. More information on the Department's staff numbers, and the statistical calculations used, is available on the website: <http://www.dasa.mod.uk>

9.2 The aggregate staff costs, including grants and allowances paid, were as follows:

	2010-11 £000	2009-10 £000
Staff costs – Administration	1,669,656	1,653,573
Staff costs – Programme	11,095,970	10,577,316
	12,765,626	12,230,889
Made up of:		
Salaries and wages	9,710,409	9,534,374
Social security costs	678,689	657,969
Pension costs	2,187,308	2,045,529
Redundancy and severance payments*	189,220	(6,983)
	12,765,626	12,230,889
Paid to:		
Armed Forces	9,888,009	9,481,306
Civilian	2,877,617	2,749,583
	12,765,626	12,230,889

*Reductions in the value of provisions for early release during 2009-10 were greater than the value of increases and new provisions. The figure for 2010-11 includes provision for the cost of the Department's initial phases of reductions in personnel announced in the SDSR.

Principal Civil Service Pension Scheme

9.3 The Principal Civil Service Pension Scheme (PCSPS) is an unfunded multi-employer defined benefit scheme. The Ministry of Defence is unable to identify its share of the underlying assets and liabilities. The Scheme Actuary Hewitt Associates reviewed the scheme as at 31 March 2007; details can be found at www.civilservice-pensions.gov.uk.

For the year to 31 March 2011, of the total pension contributions in the table above, £335,551,000 were payable in respect of the various schemes in which MOD civilian staff were members. Contributions to the PCSPS in the same period were £316,316,000 (2009-10: £312,739,000) calculated using four percentage rates (16.7%, 18.8%, 21.8% and 24.3%) of pensionable pay, based on four salary bands. The scheme's Actuary reviews employer contributions, usually, every four years following a full scheme valuation. The contribution rates are set to meet the cost of the benefits accruing, to be paid when the member retires, not the benefits paid during the period to existing pensioners.

Employees can opt to open a partnership pension account, a stakeholder pension with an employer contribution. Employer contributions of £1,686,000 (2009-10 £1,614,000) were paid to one or more of the panel of three appointed stakeholder pension providers. Employer contributions are age-related and range from 3% to 12.5% (2009-10 from 3% to 12.5%) of pensionable pay. In addition, employer contributions of £109,000 (2009-10 £103,000) of pensionable pay were payable to the PCSPS to cover the cost of future provision of lump sum benefits on death in service and ill health retirement of these employees.

Armed Forces Pension Scheme

9.4 The Armed Forces Pension Scheme (known as AFPS 05) is an unfunded, non-contributory, defined benefit, salary-related, contracted out, occupational pension scheme. A formal valuation of the AFPS was carried out as at 31 March 2009 by the scheme's actuary, the Government Actuary's Department. Scheme members are entitled to a taxable pension for life and a tax-free pension lump sum if they leave the Regular Armed Forces at or beyond normal retirement age; those who have at least two years service who leave before age 55 will have their pensions preserved until age 65. Pensions may be payable to the spouse, civil partner, partner or to eligible children. Death-in-service lump sums are payable subject to nomination. AFPS 05 offers ill-health benefits if a career is cut short by injury or illness, irrespective of cause. Additionally, if the injury or illness is mainly attributable to service, compensation for conditions caused on or after 6 April 2005 will be considered under the Armed Forces Compensation Scheme (AFCS).

AFPS 05 members who leave before the age of 55 may be entitled to an Early Departure Payment, providing they have at least 18 years service and are at least 40 years of age. The Early Departure Payment Scheme pays a tax-free lump sum and income of between 50% and 75% of preserved pension between the date of the individual's departure from the Armed Forces and age 55. The income rises to 75% of preserved pension at age 55 and is index linked. At age 65, the Early Departure Payment stops and the preserved pension and preserved pension lump sum are paid.

For the year to 31 March 2011 total employer's pension contributions (including an estimate in respect of IAS 19 – Employee Benefits) payable to the AFPS were £1,854,419,000 (2009-10 £1,701,050,000) based on employer's contribution rates determined by the Government Actuary. For 2010-11, the employer's contribution rates were 40.1% of pensionable pay for Officers (2009-10 38.3%) and 25.6% of pensionable pay for Other Ranks (2009-10 23.8%). The contribution rates reflect benefits as they are accrued, not costs actually incurred in the period, and reflect past experience of the scheme. Further information on the AFPS and the AFCS can be found at: www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/Personnel/Pensions.

Other Pension Schemes

9.5 The Armed Forces Pension Scheme incorporates the following schemes: the Non-Regular Permanent Staff Pension Scheme, the Gurkha Pension Scheme and the Reserve Forces Pension Scheme. The membership of these schemes is approximately 3% of the AFPS total membership and the employer's contributions to the schemes are included in the figure payable to the AFPS, at paragraph 9.4.

Certain other employees are covered by schemes such as the National Health Service Pension Scheme and the Teachers' Pension Scheme. The figure for total employers' pension contributions at paragraph 9.3 includes contributions in respect of these schemes. Some employees are members of other schemes, for example Locally Employed Civilians in Germany, Cyprus and Gibraltar and the Merchant Navy Ratings Pension Fund; estimates of the liabilities for these schemes are included in the figure for provisions for liabilities and charges.

10. Other Administration Costs

	2010-11 £000	2009-10 £000
Other Administration Costs – Non-Cash Expenditure		
Auditors' remuneration – audit work only	3,100	3,600
(Surplus) / deficit arising on disposal of inventory (net)	(37)	(18)
Other Administration Costs – Sub Total Non-Cash Expenditure	<u>3,063</u>	<u>3,582</u>
Other Administration Costs – Cash Costs		
Fuel	1,217	996
Inventory consumption	1,348	1,220
Movements. Including: personnel travelling, subsistence / relocation costs and movement of stores and equipment	57,652	63,083
Utilities	33,454	32,725
Property management	27,208	26,982
Hospitality and entertainment	397	946
Accommodation charges	36,086	28,147
Equipment support costs	364	693
IT and telecommunications	34,515	74,133
Professional fees	104,336	140,763
Other expenditure	47,973	99,056
Research expenditure and expensed development expenditure	4,384	3,613
Service Concession Arrangements:		
– Property management	1,507	4,696
Rentals paid under operating leases – plant & equipment	183	245
Rentals paid under operating leases – other	3,487	4,205
Grants-in-Aid	21	-
Other Administration Costs – Sub Total Cash Expenditure	<u>354,132</u>	<u>481,503</u>
Total Other Administration Costs	<u>357,195</u>	<u>485,085</u>

11. Other Programme Costs

	2010-11 £000	2009-10 £000
Other Programme Costs – Non-Cash Expenditure		
Depreciation and amortisation:		
– Intangible assets (Note 14)	1,808,193	1,515,448
– Property, plant and equipment owned assets (Note 15)	7,138,058	5,510,808
– Property, plant and equipment held under finance leases (Note 15)	121,557	112,148 *
– Property, plant and equipment held under service concession arrangements (Note 15)	308,897	323,497
– Donated assets depreciation – release of reserve	(51,129)	(60,436)
Impairment on non-current assets		
– Arising on Quinquennial valuation	76,900	77,000
– Arising on Other items	1,817,549	1,565,135*
Donated asset impairment – release of reserve	(73,497)	(41,477)
Provisions to reduce inventory to net realisable value	340,638	322,282
Inventory written off (net)	638,355	374,442
(Surplus) on disposal of property, plant and equipment and intangible assets.	(46,191)	(31,958)
(Surplus) / deficit arising on disposal of inventory (net)	(6,993)	(8,878)
Intangible and property, plant and equipment assets written off / (written on) – net	4,926,854	(95,018)
Capital project expenditure write off / (write on)	1,253,980	52,582
Bad debts written off	5,111	9,902
Increase/(Decrease) in bad debts provision	7,361	1,097
Increase/(Decrease) in nuclear and other decommissioning provisions	(339,686)	436,972
Other Programme Costs – Total Non-Cash Expenditure	17,925,957	10,063,546
Other Programme Costs		
Fuel	626,634	480,938
Inventory consumption	1,152,997	1,111,122
Movements. Including: personnel travelling, subsistence / relocation costs and movement of stores and equipment	798,300	865,855
Utilities	301,351	324,310
Property management	1,601,436	1,598,409
Hospitality and entertainment	1,433	2,842
Accommodation charges	320,643	302,471
Equipment support costs	4,688,773	4,211,434
IT and telecommunications	961,416	811,688
Professional fees	211,280	167,541
Other expenditure	1,655,051	1,492,231
Research expenditure and expensed development expenditure	1,120,813	1,218,836
Service Concession Arrangements:		
– IT and telecommunications	450,735	507,542
– Property management	450,754	439,471
– Transport	56,935	63,261
– Equipment support	77,424	74,911
– Plant and Equipment	39,418	43,101
Rentals paid under finance leases		
– Equipment support	64,591	71,048
– Defence housing	57,152	111,026
Contractor Logistic Support and Integrated Operational Support contracts for equipment support	953,120	745,783
Movement on Derivatives	50,481	270,606
Rentals paid under operating leases – plant & equipment	36,605	42,974
Rentals paid under operating leases – other	189,050	158,540*
Grants-in-Aid	147,953	150,868
Exchange differences on foreign currencies: net deficit/(surplus)	626	(14,044)
War Pensions Benefits	935,066	980,296
Other Programme Costs – Sub Total	16,950,037	16,233,060
Total Other Programme Costs	34,875,994	26,296,606

* As a result of a change to International Accounting Standard 17 – Leases and a subsequent review by MOD of relevant accounting treatments, a lease for land was reclassified from an operating to a finance lease and the following changes were made to the 2009-10 Other Programme Costs:
 Depreciation on property, plant and equipment held under finance leases – increased by £10,487,000;
 Impairment on non-current assets arising on other assets – increased by £652,026,000; and
 Rentals paid under operating leases – other, reduced by £48,042,000.
 Further details of the adjustments are at Note 34 – Prior Period Adjustments.

12. Income

	RfR 1 £000	RfR2 £000	2010-11 Total £000	2009-10 Total £000
Rental income – property	28,845	-	28,845	29,922
Receipts – personnel	357,009	-	357,009	373,280
Receipts – sale of fuel	71,741	-	71,741	79,447
Receipts – supplies and services	313,966	-	313,966	329,678
Receipts – NATO/UN/US Forces/Foreign Governments	308,017	34,002	342,019	410,675
Reverse tasking *	34,644	-	34,644	34,981
Dividends from Financial Assets (Note 16.26)	42,498	-	42,498	24,160
Other	125,626	-	125,626	126,412
	1,282,346	34,002	1,316,348	1,408,555

* Receipts for invoiced goods and/or services supplied to the Trading Funds and QinetiQ Group plc by MOD.

Fees and Charges

12.1 Where the Department has spare capacity, it provides a range of services to external organisations. The majority of these services are in the form of military support to foreign governments and other government departments. Where appropriate, costs are recovered in accordance with Managing Public Money. Where a chargeable activity produces a tangible benefit to Defence, the Department has authority to abate charges below full costs.

13. Net Interest Payable

	Administration Cost £000	Programme Cost £000	Total 2010-11 £000	2009-10 £000
Interest receivable:				
Bank interest	(1,330)	(1,398)	(2,728)	(3,947)
Loans to Trading Funds	-	(3,439)	(3,439)	(3,554)
	(1,330)	(4,837)	(6,167)	(7,501)
Unwinding of discount on long term receivables and loans	-	(1,625)	(1,625)	(637)
Total interest receivable	(1,330)	(6,462)	(7,792)	(8,138)
Interest payable:				
Bank interest	-	-	-	189
Loan interest	-	2,760	2,760	2,891
Unwinding of discount on provision for liabilities and charges	-	130,075	130,075	126,700
Unwinding of discount on long term payables	-	2,182	2,182	(4,241)
Finance leases and Service Concession Arrangements*	491	334,697	335,188	319,113
Late payment of commercial debts	-	-	-	2,206
Total interest payable	491	469,714	470,205	446,858
Net interest payable	(839)	463,252	462,413	438,720

* The 2009-10 interest payable in respect of finance leases and service concession arrangements has been increased by £48,041,000 following a reclassification of a lease for land from an operating to a finance lease. Further details are at Note 34 – Prior Period Adjustments.

14. Intangible Assets

Intangible assets include development expenditure in respect of non current assets in use and assets under construction.

	Note	Single Use Military Equipment £000	Software £000	Others £000	Total £000
Cost or Valuation†					
At 1 April 2009		32,495,703	14,587	4,387,925	36,898,215
Additions	i	917,729	2,969	350,181	1,270,879
Disposals		(86,483)	-	(195)	(86,678)
Impairments	ii	25,419	(103)	56,408	81,724
Revaluations	iii	1,052,252	-	676,753	1,729,005
Reclassifications	iv	(4,368,749)	1,115	4,155,579	(212,055)
At 31 March 2010		30,035,871	18,568	9,626,651	39,681,090
Additions	i	859,205	(35)	505,490	1,364,660
Disposals††		(4,778,368)	-	-	(4,778,368)
Impairments	ii	(647,299)	3	30,287	(617,009)
Revaluations	iii	818,684	211	325,733	1,144,628
Reclassifications	iv	1,814,368	(2,329)	(1,595,997)	216,042
At 31 March 2011		28,102,461	16,418	8,892,164	37,011,043
Amortisation					
At 1 April 2009		(7,804,775)	(3,599)	(1,130,623)	(8,938,997)
Charged in Year		(1,071,736)	(726)	(442,986)	(1,515,448)
Disposals		29,866	-	46	29,912
Impairments	ii	(18,193)	(108)	15,109	(3,192)
Revaluations	iii	(267,393)	-	(182,596)	(449,989)
Reclassifications	iv	1,626,382	208	(1,296,400)	330,190
At 31 March 2010		(7,505,849)	(4,225)	(3,037,450)	(10,547,524)
Charged in Year		(1,428,149)	(303)	(379,741)	(1,808,193)
Disposals††		2,158,087	-	-	2,158,087
Impairments	ii	559,260	(3)	(22,134)	537,123
Revaluations	iii	(141,573)	(9)	(104,168)	(245,750)
Reclassifications	iv	11,218	527	(10,103)	1,642
At 31 March 2011		(6,347,006)	(4,013)	(3,553,596)	(9,904,615)
Net Book Value					
At 1 April 2009		24,690,928	10,988	3,257,302	27,959,218
At 31 March 2010		22,530,022	14,343	6,589,201	29,133,566
At 31 March 2011		21,755,455	12,405	5,338,568	27,106,428

Notes

i. Additions include accruals of £984,743,000 (2009-10: £829,026,000). Information on Frascati compliant R&D expenditure can be found on the DASA website: <http://www.dasa.mod.uk>.

ii. Capitalised development costs directly linked to a class of asset are only impaired if the whole class of the associated non current asset is impaired e.g. when a whole class of asset is withdrawn from service.

iii. Revaluations include changes due to Modified Historic Cost Accounting through indexation.

iv. Reclassifications include assets classified to or from property, plant and equipment.

† Intangible asset valuations are based on the actual costs incurred or derived by applying a ratio to the property, plant and equipment asset valuations based on the historical relationship between development and production costs.

†† For 2010-11 disposals includes writes-off of development costs totalling £3,452,931,000 where it has been possible to assess the impact of early SDRS decisions e.g. Nimrod development costs of £2,132,267,000 and Harrier development costs of £604,257,000.

14.1 Movement in the revaluation reserve relating to intangible assets

	2010-11 £000	2009-10 £000
Balance – 1 April	4,592,853	3,543,513
Revaluation	898,878	1,279,016
Transfers / reclassifications	247	21,099
Disposals	-	(8,382)
Realised reserve transferred to the General Fund	(379,501)	(242,393)
Balance – 31 March	5,112,477	4,592,853

14.2 Details of intangible assets with a net book value greater than £500M.

Description	Net Book Value 31 March 2011 £000	Remaining Useful Economic Life
Typhoon development costs	6,763,608	19 years
Type 45 destroyer development costs	1,908,798	23 years 8 months
Merlin helicopter development costs	1,747,558	18 years 11 months
Astute class submarine development costs	961,019	24 years
Spearfish torpedo development costs	607,210	38 years 11 months
Tornado airframe development costs	540,535	14 years

15. Property, Plant and Equipment

	Note	Land Dwellings £000	Land Other Buildings £000	Dwellings £000	Other Buildings £000	Single Use Military Equipment (SUME) £000	Plant and Machinery £000	Transport £000	IT and Communication Equipment £000	Assets under Construction (SUME) £000	Assets under Construction (Other) £000	Total £000
Cost or Valuation												
At 1 April 2009†		3,083,919	5,541,747	6,443,225	16,421,924	71,108,170	4,320,828	10,413,851	3,763,796	13,808,616	5,551,492	140,457,568
Additions	i	10	-	89,308	156,555	504,171	299,163	72,520	347,459	3,923,456	2,353,735	7,746,377
Capitalised Provisions	ii	-	-	-	26,041	5,083	-	-	-	-	-	31,124
Donations	iii	9,915	8,958	1,242	11,827	-	90	-	-	-	-	32,032
Disposals		(3,677)	(641,759)	(201,860)	(205,198)	(1,587,795)	(151,201)	(304,859)	(73,150)	-	(1,862)	(3,171,361)
Impairments	iv	(767,176)	(179,613)	(186,498)	(472,993)	(206,798)	32,872	(106,537)	139,255	(28)	(96,683)	(1,844,199)
Reclassifications	v	71,669	577,563	518,945	232,099	389,280	(389,441)	3,374,544	(78,226)	(3,442,743)	(2,207,111)	(953,421)
Revaluations	vi	65,335	58,949	230,210	(263,638)	2,399,925	123,153	1,042,895	94,204	688,993	(130,900)	4,309,126
At 31 March 2010		2,459,995	5,365,845	6,894,572	15,906,617	72,612,036	4,235,464	14,492,414	4,193,338	14,978,294	5,468,671	146,607,246
Additions	i	-	284	154,194	169,162	698,791	51,143	79,474	319,748	4,119,335	2,476,316	8,068,447
Capitalised Provisions	ii	-	-	-	4,411	1,857	-	-	-	-	-	6,268
Donations	iii	9,401	37,489	3,441	4,285	-	16,820	-	-	-	-	71,436
Disposals††		(132,803)	(461,651)	(103,715)	(348,932)	(7,535,292)	(499,250)	(1,130,404)	(175,508)	(1,001,776)	-	(11,389,331)
Impairments	iv	(134,352)	(32,068)	(237,924)	(572,228)	(1,169,017)	(5,000)	(462,495)	80,873	(4,923)	(301,999)	(2,839,133)
Reclassifications	v	2,254	3,195	211,131	1,739,019	5,461,736	84,451	2,054,152	(65,962)	(6,183,260)	(2,964,659)	342,057
Revaluations	vi	69,080	314,604	111,705	(807,424)	2,096,203	73,289	1,022,845	(20,804)	147,123	44,806	3,051,427
At 31 March 2011		2,273,575	5,227,698	7,033,404	16,094,910	72,166,314	3,956,917	16,055,986	4,331,685	12,054,793	4,723,135	143,918,417
Depreciation												
At 1 April 2009		(20,560)	-	(999,371)	(5,451,305)	(35,636,211)	(2,008,791)	(5,400,314)	(1,063,834)	-	-	(50,580,386)
Charged in Year		(10,487)	-	(250,800)	(745,847)	(3,594,960)	(258,974)	(667,589)	(417,796)	-	-	(5,946,453)
Disposals		-	-	51,974	87,226	1,282,148	68,202	180,007	62,485	-	-	1,732,042
Impairments	iv	8,578	-	6,591	32,095	174,717	(33,153)	(19,952)	(73,337)	-	-	95,539
Reclassifications	v	-	-	(35,073)	317,129	2,385,665	122,549	(653,497)	153,855	-	-	2,290,628
Revaluations	vi	-	-	(259,889)	(545,650)	(1,326,707)	(42,060)	(370,874)	(634)	-	-	(2,545,814)
At 31 March 2010		(22,469)	-	(1,486,568)	(6,306,352)	(36,715,348)	(2,152,227)	(6,932,219)	(1,339,261)	-	-	(54,954,444)

Note	Land Dwellings £000	Land Other Buildings £000	Dwellings £000	Other Buildings £000	Single Use Military Equipment (SUME) £000	Plant and Machinery £000	Transport £000	Communication Equipment £000	Assets under Construction (SUME) £000	Assets under Construction (Other) £000	Total £000
Charged in Year	(8,158)	-	(220,838)	(589,837)	(5,333,652)	(251,090)	(728,255)	(436,682)	-	-	(7,568,512)
Disposals	-	-	43,868	207,534	5,389,649	328,310	941,876	134,002	-	-	7,045,239
Impairments	1,669	-	21,248	107,602	856,456	181	179,380	(54,009)	-	-	1,112,527
Reclassifications	(8,578)	-	236,316	(426,800)	549,329	21,971	(449,494)	18,964	-	-	(58,292)
Revaluations	-	-	(34,043)	598,839	(1,186,288)	(49,995)	(595,277)	71,928	-	-	(1,194,836)
At 31 March 2011	(37,536)	-	(1,440,017)	(6,409,014)	(36,439,854)	(2,102,850)	(7,583,989)	(1,605,058)	-	-	(55,618,318)
Net Book Value											
At 1 April 2009	3,063,359	5,541,747	5,443,854	10,970,619	35,471,959	2,312,037	5,013,537	2,699,962	13,808,616	5,551,492	89,877,182
At 31 March 2010	2,437,526	5,365,845	5,408,004	9,600,265	35,896,688	2,083,237	7,560,195	2,854,077	14,978,294	5,468,671	91,652,802
At 31 March 2011	2,236,039	5,227,698	5,593,387	9,685,896	35,726,460	1,854,067	8,471,997	2,726,627	12,054,793	4,723,135	88,300,099
Asset Financing											
Owned	212,487	4,063,355	2,969,230	7,947,768	35,725,036	1,579,651	8,166,941	1,105,326	12,054,793	4,703,588	78,528,175
Donated	200,806	975,177	268,303	873,536	-	36,095	21	-	-	-	2,353,938
Long Lease	24,078	52,946	13,219	26,408	-	-	-	-	-	-	116,651
Short Lease	30	31,047	327	13,751	-	-	-	-	-	-	45,155
Operating Lease (Lessor)	-	-	-	6,166	-	-	-	-	-	-	6,166
Finance Lease	1,712,875	-	1,680,516	-	-	-	151,045	-	-	-	3,544,436
Service Concession Arrangements	85,763	105,173	661,792	818,267	1,424	238,321	153,990	1,621,301	-	19,547	3,705,578
At 31 March 2011	2,236,039	5,227,698	5,593,387	9,685,896	35,726,460	1,854,067	8,471,997	2,726,627	12,054,793	4,723,135	88,300,099

Notes:

- i. Additions include accruals of £2,633,411,000 (2009-10: £2,501,303,000).
ii. Property, plant and equipment as at 31 March 2011 include capitalised provisions of £449,313,000 (2009-10: £334,655,000).
iii. Donated Assets in use have been valued on the same basis as all other assets used by the Department.
iv. Assets are impaired for a variety of reasons e.g. loss, damage, unforeseen obsolescence, abandonment of assets under construction and those associated with disposals.
v. Includes assets reclassified to or from intangible assets of £207,962,000, assets written off of £1,002,904,000 and assets reclassified to or from inventories of £1,963,962,000.
vi. Revaluations include changes due to Modified Historic Cost Accounting through indexation, impairment and impairment reversals. Land and buildings are subject to quinquennial revaluation; overseas assets are also subject to adjustments to reflect movements in the Euro to Sterling exchange rate.
† The value of PPE as at 1 April 09 includes leased land added following a change in accounting policy. Further details are at Note 34.2 to the accounts.
†† For 2010-11 disposals also includes asset writes-off where it has been possible to assess the impact of early SDSR decisions e.g. Nimrod (£1,253,927,000), Harrier (£320,565,000) and 4 Type 42 frigates (£291,536,000).

15.1 All Property (Land and Buildings) with the exception of Assets under Construction, are subject to a quinquennial revaluation (QQR), which is conducted over a rolling 5 year programme with approximately 25% of the estate being revalued in each of the first 4 years allowing for any residual work to take place in year 5. Financial year 2010-11 represents the third year of the current QQR programme. Valuations for the UK estate were performed by the Valuation Office Agency and for the overseas estate in-house by Defence Infrastructure Organisation personnel and reviewed by GVA Grimley's. All valuations are undertaken in accordance with the Royal Institute of Chartered Surveyors Appraisal and Valuation Manual. Non-specialist properties are valued at fair value, interpreted as market value for existing use; Specialist properties, for which there is no external market, are valued at depreciated replacement cost.

15.2 Data from the 2010–11 quinquennial review resulted in a £471M increase in the value of Land and a £524M increase in the value of Buildings; accruals have been posted to cover some outstanding valuations.

15.3 The net debit to the SoCNE in respect of impairments arising from the movement in values against owned Land and Buildings is £76.9M. This is made up of: Land – Impairment Writes-Off £41.6M and Impairment Reversals £80.4M; Buildings – Impairment Writes-Off £185.2M and Impairment Reversals £69.5M.

16. Financial Instruments

16.1 IFRS 7 Financial Instruments – Disclosures, requires the Department to provide disclosures in respect of the role of financial instruments on performance during the period, the nature and extent of the risks to which the Department is exposed and how these risks are managed. For each type of risk arising from financial instruments, the Department is also required to provide summary quantitative data about its exposure to the risk at the reporting date.

16.2 The cash requirements of the Department are met through the Parliamentary Estimates process, financial instruments therefore play a more limited role in creating risk than would apply to a non-public sector body of a similar size. The majority of financial instruments relate to contracts for non-financial items in line with the Department's expected purchase and usage requirements and the Department is therefore exposed to little liquidity or cash flow risk.

16.3 The Department is subject to some credit risk. The carrying amount of receivables, which is net of impairment losses, represents the Department's maximum exposure to credit risk. Trade and other receivables consist of a large number of diverse customers spread over a wide geographical area. Receivables are impaired where there is sufficient knowledge to indicate that recovery is improbable including the probability that customers will enter bankruptcy or financial reorganisation, that the customer is facing financial difficulties or that economic conditions are likely to lead to non-payment. The following analysis provides details of receivables beyond their due date and the impairments made:

	0 – 3 Months £000	3 – 6 Months £000	6 – 12 Months £000	Over 12 months £000
Trade receivables before impairment	5,840	48,858	3,030	12,510
Impairment	(136)	(210)	(272)	(19,557)
Net carrying value of receivables beyond the due date	5,704	48,648	2,758	(7,047)

The impairments represent 0.55% of trade and other receivables (2009-10: 1.2%).

16.4 The Department is subject to exchange rate risk and enters into forward purchase contracts for Euros and US Dollars to mitigate against the risk that cash inflows and outflows will be affected by changes in exchange rates; foreign currency forward contracts were not in hedging relationships in accordance with IAS 39. In 2010-11 £1,876M of expenditure was undertaken in foreign currencies which are not funded through the forward purchase contracts.

Significant Accounting Policies

16.5 Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial instrument are disclosed in Note 1 to the financial statements.

Categories of Financial Instruments

16.6 Details of the Financial Instruments, by category, are:

	Note	Carrying Value		
		31 March 2011 £000	31 March 2010 £000	1 April 2009 £000
Financial Assets				
Fair value through Net Operating Cost – Held for Trading	SoFP	349,512	513,611	1,110,800
Loans and receivables (including cash and cash equivalents)		1,715,597	2,095,522	2,198,611
Held for Sale		1	1	1
		<u>2,065,110</u>	<u>2,609,134</u>	<u>3,309,412</u>
Financial Liabilities				
Payables and accruals		(9,474,920)	(8,166,280)	(8,346,708)
Fair value through Net Operating Cost – Held for Trading	SoFP	(102,976)	(30,984)	-
		<u>(9,577,896)</u>	<u>(8,197,264)</u>	<u>(8,346,708)</u>

16.7 The net gains and losses taken through Net Operating Cost or Other Comprehensive Expenditure in respect of financial instruments are listed below:

	31 March 2011		31 March 2010	
	Net Operating Cost £000	Other Comprehensive Expenditure £000	Net Operating Cost £000	Other Comprehensive Expenditure £000
Financial Assets				
Fair value through Net Operating Cost – Held for Trading	50,481	-	270,606	-
Interest on loans and receivables	(1,625)	-	(637)	-
Financial Liabilities				
Payables and accruals	2,182	-	(4,241)	-
	<u>51,038</u>	<u>-</u>	<u>265,728</u>	<u>-</u>

Interest Rate Risk Management

16.8 A significant proportion of the Department's financial assets and liabilities carry nil or fixed rates of interest. The exposure to interest risk is therefore not significant. Departmental cash requirements are met through the Parliamentary Estimates process.

Foreign Currency Risk

16.9 The Department undertakes certain transactions denominated in foreign currencies; as a result exposure to exchange rate fluctuations arises. Exchange rate exposures for the US Dollar and Euro are managed using forward purchase contracts with the Bank of England and covered 75% of the in-year expenditure (Request for Resources 1 (RfR1) – Provision of Defence Capability).

16.10 The table below details the forward purchase currency contracts outstanding as at 31 March 2011:

	Average Contract Exchange Rates	Foreign Currency	Contract Value	Financial Asset / (Liability)	Financial Asset / (Liability)	Financial Asset / (Liability)
		US \$ '000 Euro € '000 31 March 2011	31 March 2011 £000	Fair Value 31 March 2011 £000	Fair Value 31 March 2010 £000	Fair Value 1 April 2009 £000
Delivery 2010-11						
US Dollars (\$)		-	-	-	125,147	205,350
Euro (€)		-	-	-	182,375	344,384
Delivery 2011-12						
US Dollars (\$)	1.62	1,967,000	1,216,633	10,442	74,450	153,189
Euro (€)	1.20	1,815,000	1,506,837	99,927	86,873	222,649
Delivery 2012-13						
US Dollars (\$)	1.57	1,412,000	901,984	(21,135)	20,007	76,264
Euro (€)	1.15	1,383,000	1,206,112	18,215	(6,225)	108,964
Delivery 2013-14						
US Dollars (\$)	1.54	740,000	479,381	(17,746)	-	-
Euro (€)	1.18	893,000	757,488	33,057	-	-
Total			6,068,435	122,760	482,627	1,110,800

16.11 The fair value of the financial asset / liability arising from the forward purchase contracts is determined using the mid-market rate for 31 March published in the Financial Times.

Fuel Price Risk

16.12 The Department undertakes substantial purchases of aviation and marine fuels. Exposure to fluctuations in the market prices of these commodities is managed using Swap contracts for forward deliveries. The Swap contracts are placed with a small range of major financial institutions. No contracts matured in the year.

16.13 The table below details the Swap contracts outstanding as at 31 March 2011:

	Average Price US\$ / Tonne	Volume Tonnes	Contract Value		Financial Asset / (Liability) Fair Value	Financial Asset / (Liability) Fair Value
			31 March 2011	31 March 2011*	31 March 2011	31 March 2011*
			US\$000	£000	US\$000	£000
Delivery 2011-12						
Aviation Turbine Fuel	860	346,880	298,244	186,054	69,747	43,510
Gas Oil	777	134,206	104,331	65,085	25,238	15,744
Delivery 2012-13						
Aviation Turbine Fuel	880	260,180	228,883	142,784	47,132	29,402
Gas Oil	798	103,970	82,957	51,751	17,420	10,867
Delivery 2013-14						
Aviation Turbine Fuel	902	130,068	117,312	73,183	20,672	12,896
Gas Oil	818	52,026	42,562	26,551	7,667	4,783
Total			874,289	545,408	187,876	117,202

*US \$ values have been converted to sterling using the mid market exchange rate as at 31 March 2011 (£1 = \$1.603).

Embedded Derivatives

16.14 Derivatives embedded in other financial instruments or host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of host contracts and the host contracts are not measured at fair value with changes in fair value recognised in the Statement of Comprehensive Net Expenditure in accordance with IFRS 7. The Department operates a commercial framework whereby it does not currently hold financial risks of this nature and places restrictions on doing so in the future.

Fair Value of Financial Instruments

16.15 The carrying values of financial assets and financial liabilities are determined as follows:

- Financial assets at fair value through Statement of Comprehensive Net Expenditure: mid market rate at 31 March as published in the Financial Times.
- Loans and Receivables: Loans to MOD Trading Funds are valued at historical cost less any impairment, with the element due within one year treated as fair value. Receivables due in less than one year are valued at historic cost less any impairment. Receivables due in more than one year are discounted using either the higher of the interest rate intrinsic to the financial instrument or the HM Treasury rate of 2.2%.
- Available for Sale Assets are measured at book value.
- Payables and accruals: Payables and accruals due in less than one year are valued at historic cost less any impairment. Payables and accruals due in more than one year are discounted using the higher of the interest rate intrinsic to the financial instrument, the HM Treasury rate of 2.2% or, where applicable, the discount rate applicable to pension scheme provisions. Loans payable with a market rate of interest are valued at cost.
- Financial liabilities at fair value through Statement of Comprehensive Net Expenditure: mid market rate at 31 March as published in the Financial Times.

16.16 Details of the financial instruments by valuation method are:

	31 Mar 11 £000	31 Mar 10 £000	Carrying Value 1 Apr 09 £000
Financial Assets			
Fair value	349,513	513,612	1,110,801
Historic cost	1,479,228	1,832,943	1,720,857
Discounted cost	236,369	262,579	477,754
	<u>2,065,110</u>	<u>2,609,134</u>	<u>3,309,412</u>
Financial Liabilities			
Fair value	(102,976)	(30,984)	-
Historic cost	(9,292,707)	(7,995,442)	(8,210,542)
Discounted cost	(182,213)	(170,838)	(136,166)
	<u>(9,577,896)</u>	<u>(8,197,264)</u>	<u>(8,346,708)</u>

Financial Guarantee Contracts

16.17 The Department has entered into two financial guarantee contracts, neither of which is a contingent liability within the meaning of IAS 37 since the likelihood of transfer of economic benefit in settlement is too remote. The probability of payments under these guarantees is very low and the likely liability (fair value) as at year end is assessed as nil. Details of the guarantees are:

- Under the terms of the contract with TNT Ltd for the Government Records Management and Archive Service, MOD guarantees to pay the operator should any other government department fail to settle its outstanding invoices. The total value of invoices outstanding against all government departments as at 31 March 2011 was £304,000.
- MOD provides an indemnity to towage companies who are contracted to tow foreign warships in to UK ports, should the foreign nation default on payment of the invoice.

16.18 Investments in Other Public Sector and Non-Public Sector Bodies

	Non-Current Assets Financial Assets		Total £000
	Public Dividend Capital £000	Loans £000	
Balance at 1 April 2009	145,869	71,331	217,200
Additions	-	15,079	15,079
Repayments	-	(8,222)	(8,222)
Balance at 31 March 2010	<u>145,869</u>	<u>78,188</u>	<u>224,057</u>
Additions / Transfers			
Repayments / Transfers			
dstl	-	(3,220)	(3,220)
UKHO	-	(538)	(538)
Met Office	-	(5,698)	(5,698)
DSG	-	(1,665)	(1,665)
Balance at 31 March 2011	<u>145,869</u>	<u>67,067</u>	<u>212,936</u>

16.19 Public Dividend Capital (PDC) and Loan Balances by Trading Fund

	Public Dividend Capital (PDC) 31 Mar 11 £000	Loans 31 Mar 11 £000	Interest Rates %p.a.
Defence Science and Technology Laboratory	50,412	28,980	2.75-4.53
UK Hydrographic Office	13,267	8,692	8.55
Met Office	58,867	1,105	1.06-4.45
Defence Support Group	23,323	28,290	4.6
Totals	145,869	67,067	

16.20 Analysis of Loans Repayable by Instalments

	Due Within One Year £000	Due After One Year £000	Total £000
Defence Science and Technology Laboratory	3,220	25,760	28,980
UK Hydrographic Office	585	8,107	8,692
Met Office	1,105	-	1,105
Defence Support Group	1,664	26,626	28,290
Balance at 31 March 2011	6,574	60,493	67,067

16.21 Department's Share of Net Assets and Results of Trading Funds

	Net Assets (after loans due to MOD) 31 Mar 11 £000	Turnover £000	Surplus / profit for the Year (before financing) £000
Defence Science and Technology Laboratory	277,680	563,609	41,333
UK Hydrographic Office	102,001	129,505	38,669
Met Office	197,397	196,118	9,422
Defence Support Group	121,891	209,062	8,200
Total	698,969	1,098,294	97,624

Other Financial Assets

16.22 As at 31 March 2011, investments, including Special Shares, were held in the following:

7.5% Non-cumulative Irredeemable Preference Shares at £1 each	
The Chamber of Shipping Limited	688 Shares
The British Shipping Federation Limited	55,040 Shares

Preferential Special Shares at £1 each	
Devonport Royal Dockyard Limited	1 Share
Rosyth Royal Dockyard Limited	1 Share
AWE plc	1 Share
AWE Pension Trustees Limited	1 Share
QinetiQ Group plc	1 Share
QinetiQ Holdings Limited	1 Share
QinetiQ Limited	1 Share
BAE Systems Marine (Holdings) Limited	1 Share

Non Preferential Shares of £1 each	
International Military Services Limited	19,999,999 Shares

16.23 The Department has a 100% interest in the non-preferential shares of International Military Services Limited, a company registered in England. International Military Services Limited ceased trading on 31 July 1991. Following settlement of outstanding contracts, the company will be liquidated and any remaining value distributed in accordance with the company's constitution. The Department has written down the value of the investment to nil.

16.24 The 7.5% Non-cumulative Irredeemable Preference Shares in Chamber of Shipping Limited and British Shipping Federation Limited are valued at 1p each reflecting the value at which shares would be recovered by the two companies should membership by the Department be ceded, as laid down in the Articles of Association of the respective companies.

16.25 Special Shares confer on the Secretary of State for Defence special rights regarding ownership, influence and control, including voting rights in certain circumstances, under the individual Articles of Association of the relevant companies in which the shares are held. Further detailed information can be obtained from the companies' annual reports and accounts, which can be obtained from:

Company	Registration Number
Devonport Royal Dockyard Limited, Devonport Royal Dockyard, Devonport, Plymouth PL1 4SG	02077752
Rosyth Royal Dockyard Limited, c/o Babcock BES, Rosyth Business Park, Rosyth, Dunfermline, Fife KY11 2YD	SC101959
AWE plc, AWE Aldermaston, Reading, Berkshire RG7 4PR	02763902
AWE Pension Trustees Limited, AWE Aldermaston, Reading, Berkshire RG7 4PR	02784144
QinetiQ Group plc, 85 Buckingham Gate, London SW1E 6PD	04586941
QinetiQ Holdings Limited, 85 Buckingham Gate, London SW1E 6PD	04154556
QinetiQ Limited, 85 Buckingham Gate, London SW1E 6PD	03796233
BAE Systems Marine (Holdings) Limited, Warwick House, PO Box 87, Farnborough Aerospace Centre, Farnborough, Hants, GU14 6YU	01957765

Dividends from Investments

16.26 The following dividends are shown as income in Note 12.

	2010-11 £000	2009-10 £000
Defence Science and Technology Laboratory*	8,500	4,000
UK Hydrographic Office*	18,498	11,160
Met Office	8,200	4,500
Defence Support Group*	2,300	4,500
Other	5,000	-
Total	42,498	24,160

*The figures for 2009-10 include Special Dividends of: £5.995M from UKHO, £0.5M from DSG and £1M from Dstl. The UKHO figure for 2010-11 includes a Special Dividend of £10M.

17. Impairments

Details of impairments and impairment reversals through Net Operating Costs and Other Comprehensive Expenditure, for the year, are:

	Net Operating Cost Impairment £000	Net Operating Cost Impairment Reversal £000	Other Comprehensive Expenditure Impairment £000	Other Comprehensive Expenditure Impairment Reversal £000
Intangibles	95,729	(15,844)	-	-
Land	406,582	(240,163)	-	-
Property (including assets held for sale)	804,918	(124,890)	-	(392)
Single Use Military Equipment (SUME)	312,562	-	-	-
Plant & machinery	6,325	(1,506)	-	-
Transport	283,115	-	-	-
IT	3,006	(29,871)	-	-
Assets under construction	326,124	(15,726)	-	(3,476)
Assets held for sale	84,088	-	-	-
	2,322,449	(428,000)	-	(3,868)

18. Assets Held For Sale

The Department has the following non-current assets held for sale:

	31 March 2011 £000	31 March 2010 £000	1 April 2009 £000
Land and property	42,821	74,183	120,154
Plant and equipment	80,078	8,879	4,666
	122,899	83,062	124,820

18.1 During 2010-11 no assets over £1M were reclassified from property, plant and equipment to current assets – assets held for sale.

18.2 Disposal of plant and equipment is managed through the Disposal Services Authority. Disposal of land and property is managed by Defence Estates. Assets are held at the lower of market value or net book value with any movement in valuation taken to the revaluation reserve up to historic cost and then to Net Operating Cost as an impairment. Costs of impairing the assets to the net realisable value were charged to the operating costs statement and are included in Note 11 – Other Programme Costs.

18.3 During 2010-11 assets held for sale which were actually sold (with sales proceeds shown in brackets) included: RAF Sealand – South Site (£6M), Silver (£4.7M), Fremington Training Group and Limekilns (£3.4M), Penhale Training Area (£1.5M), Chelsfield Ammunition Depot (£1.1M), the NE Quadrant of Pickpit Hill (£1M), TAC Worcester (£7.8M), HMS Roebuck (4.4M), Glasgow 6 & 7 Lowther Terrace (£2.3M), HMS Dumbarton Castle (£1.2M) and HMS Leeds Castle (£1.2M).

19. Inventories

	31 Mar 2011 £000	31 Mar 2010 £000	1 April 2009 £000
Work in progress	-	6	95,785
Raw materials and consumables	7,719,661	7,183,837	6,551,589
Held for sale	12	12	12
	<u>7,719,673</u>	<u>7,183,855</u>	<u>6,647,386</u>

19.1 Where MOD has a Memorandum of Understanding with another country, inventory (including major components such as gas turbines and other supporting inventory) belonging to and held on behalf of that country is included in MOD's inventory systems. The assets may physically be at the contractor, in stores or both. The value of these items is not included in the figures above.

19.2 The write-down in the value of inventory which has been recognised in Net Operating Cost during the year is £1,122,864,000. During the year, individual reversals of write-downs greater than £1M which had previously been recognised in the Statement of Comprehensive Net Expenditure amounted to £772,095,000 and resulted mainly from the annual review of inventory provisions in accordance with inventory plans.

20. Trade receivables and other current assets

20.1 Analysis by type

	31 March 2011 £000	31 March 2010 £000	1 April 2009 £000
Amounts falling due within one year:			
Trade receivables	188,324	170,442	387,493
Deposits and advances	81,524	84,178	49,882
Value Added Tax	468,853	420,336	362,498
Other receivables	217,083	379,040	173,999
Staff loans and advances*	37,551	33,152	21,998
Prepayments and accrued income	1,377,081	1,374,298	1,188,952
Current part of Service Concession Arrangement prepayment	2,553	6,012	45,356
Under issue of Supply from the Consolidated Fund	127,641	239,885	-
	<u>2,500,610</u>	<u>2,707,343</u>	<u>2,230,178</u>
Amounts falling due after one year:			
Trade receivables	165,490	193,310	403,621
Other receivables	5,309	7,711	8,280
Staff loans and advances*	65,458	61,360	65,853
Prepayments and accrued income	650,461	620,211	610,576
	<u>886,718</u>	<u>882,592</u>	<u>1,088,330</u>
Total Receivables	<u>3,387,328</u>	<u>3,589,935</u>	<u>3,318,508</u>

* Staff loans and advances includes loans for house purchase. The number of staff with house purchase loans was 14,517 (2009-10:13,486).

20.2 Intra-Government Balances

	Amounts falling due within one year			Amounts falling due after more than one year		
	31 March	31 March	1 April	31 March	31 March	1 April
	2011	2010	2009	2011	2010	2009
	£000	£000	£000	£000	£000	£000
Balances with other central government bodies	482,937	439,040	405,392	-	1	-
Balances with local authorities	2,310	1,277	102,411	-	-	-
Balances with NHS Trusts	626	6,774	4,695	-	-	-
Balances with public corporations and trading funds	12,230	10,158	45,028	-	-	-
<i>Subtotal: intra-government balances</i>	498,103	457,249	557,526	-	1	-
Balances with bodies external to government	2,002,507	2,250,094	1,672,652	886,718	882,591	1,088,330
Total Receivables	2,500,610	2,707,343	2,230,178	886,718	882,592	1,088,330

The table above provides an analysis of the balances in Table 20.1 by customer type.

21. Cash and Cash Equivalents

	£000
Balance at 1 April 2009	913,570
Net Cash Inflow/(Outflow):	
Received from Consolidated Fund	37,184,813
Utilised	(37,421,026)
Increase / (decrease) during year	(236,213)
Balance at 31 March 2010	677,357
Net Cash Inflow/(Outflow):	
Received from Consolidated Fund	37,517,074
Utilised	(37,510,530)
Increase / (decrease) during year	6,544
Balance at 31 March 2011	683,901

	31 March 2011 £000	31 March 2010 £000	1 April 2009 £000
The following balances were held at:			
Government Banking Service	297,528	485,468	560,944
Commercial Banks and Cash in Hand	386,373	191,889	352,626
Totals	683,901	677,357	913,570

The cash at bank balance includes £344,062,000 (2009-10: £207,221,000) of sums advanced by foreign governments to the Department on various collaborative projects where the United Kingdom is the host nation. Advances made by foreign governments for the procurement of defence equipment on their behalf are also included in this amount. The corresponding liability for these advances is shown under payables due within one year.

The Department holds \$40,000,000 in an account with the US Government as a Termination Liability Reserve. This is a US legal requirement in order to trade with US defence contractors through Foreign Military Sales. The balance is accounted for as a prepayment in Note 20 Trade Receivables and other non-current assets.

21.1 Reconciliation of Net Cash Requirement to Increase / (Decrease) in Cash

	2010-11 £000	2009-10 £000
Net Cash Requirement	(37,644,715)	(37,424,698)
From the Consolidated Fund to clear prior year receivable	239,885	-
From the Consolidated Fund (Supply) – current year	37,517,074	37,064,006
From the Consolidated Fund (Supply) – prior year (deemed funding)	-	120,807
Amounts due to the Consolidated Fund – received and not paid	-	242,541
Amounts due to the Consolidated Fund – received in the prior year and paid over	(242,541)	(242,794)
Movement on collaborative projects	136,841	3,925
Increase / (decrease) in cash	6,544	(236,213)

22. Trade Payables and Other Current Liabilities

22.1 Analysis by type

	31 March 2011 £000	31 March 2010 £000	1 April 2009 £000
Amounts falling due within one year			
VAT	38,337	37,833	15,301
Other taxation and social security	260,999	249,233	257,197
Trade payables	370,274	363,252	447,918
Other payables*	1,443,997	1,259,061	879,948
Payments received on account	2,497	3,439	4,922
Accruals and deferred income	7,831,551	6,897,837	6,913,855
Current part of finance leases	24,156	23,495	22,940
Current part of imputed finance lease element of Service Concession Arrangement contracts	174,919	167,646	170,670
Current part of NLF loans***	2,407	2,270	2,141
Amounts issued from the Consolidated Fund for supply but not spent at year end (Supply payable)	-	-	120,807
Consolidated Fund extra receipts due to be paid to the Consolidated Fund	-	242,541	242,795
	10,149,137	9,246,607	9,078,494
Amounts falling due after more than one year			
Other payables	78,621	67,432	64,094
Accruals and deferred income	103,592	97,575	66,072
Finance leases**	1,833,989	1,862,513	1,877,675
Imputed finance lease element of Service Concession Arrangement contracts	3,485,730	3,328,899	3,260,468
NLF loans***	37,594	40,001	42,271
	5,539,526	5,396,420	5,310,580
Total Payables	15,688,663	14,643,027	14,389,074

* Other payables includes amounts advanced by foreign governments to the Department, in respect of various collaborative projects where the United Kingdom is the host nation and for the procurement of defence equipment on their behalf, of £344,062,000 (2009-10: £207,221,000).

** Liabilities under finance leases include the addition of £848,716,000 in respect of a Prior Period Adjustment to add the liability for Service housing as at 1 April 2009. Further details are at Note 34 – Prior Period Adjustments.

*** Under the Armed Forces (Housing Loans) Acts 1949, 1958 and 1965, £94M was borrowed from the National Loans Fund for the construction of married quarters over the period 1950/51 to 1967/68. These loans are fully repayable between 2012 and 2028, with the last instalment due on 20 February 2028. Interest on the loans is payable at rates ranging from 4% to 7% per annum.

22.2 Intra-Government Balances

	Amounts falling due within one year			Amounts falling due after more than one year		
	31 March 2011 £000	31 March 2010 £000	1 April 2009 £000	31 March 2011 £000	31 March 2010 £000	1 April 2009 £000
Balances with other central government bodies	536,717	587,620	642,063	37,594	40,001	-
Balances with local authorities	1,204	346	332	-	-	-
Balances with NHS Trusts	10,942	5,128	12,924	165	-	-
Balances with public corporations and trading funds	23,345	99,491	135,189	-	-	-
<i>Subtotal: intra-government balances</i>	<i>572,208</i>	<i>692,585</i>	<i>790,508</i>	<i>37,759</i>	<i>40,001</i>	<i>-</i>
Balances with bodies external to government	9,576,929	8,554,022	8,287,986	5,501,767	5,356,419	5,310,580
Total Payables	10,149,137	9,246,607	9,078,494	5,539,526	5,396,420	5,310,580

The table above provides an analysis of the balances in Table 22.1 by contractor type.

23. Provisions for Liabilities and Charges

	Nuclear Decommissioning £000	Other Decommissioning and Restoration Costs £000	Early Retirement Commitments £000	Other £000	Total £000
At 1 April 2009	4,227,976	76,047	336,988	1,093,193	5,734,204
Increase in provisions in-year	481,507	216	47,940	124,191	653,854
Provisions written back and reclassifications	(44,535)	(828)	(82,571)	(511,716)	(639,650)
Provisions utilised in year	(56,888)	(9,318)	(94,216)	(128,082)	(288,504)
Unwinding of discount	97,618	463	9,775	107,785	215,641
Provisions capitalised	31,124	-	-	-	31,124
At 31 March 2010	4,736,802	66,580	217,916	685,371	5,706,669
Increase in provisions in-year	230,947	6,563	173,465	217,350	628,325
Provisions written back and reclassifications	(570,633)	(5,305)	(2,966)	(92,774)	(671,678)
Provisions utilised in year	(57,474)	(6,521)	(61,657)	(128,597)	(254,249)
Unwinding of discount	104,097	608	(1,281)	(33,717)	69,707
Provisions capitalised	6,268	-	-	-	6,268
At 31 March 2011	4,450,007	61,925	325,477	647,633	5,485,042

23.1 Analysis of expected timing of discounted cash flows

	Nuclear Decommissioning £000	Other Decommissioning and Restoration Costs £000	Early Retirement Commitments £000	Other £000	Total £000
In the year to 31 March 2012	79,146	20,756	183,939	111,094	394,935
Between April 2012 and March 2017	847,505	40,615	97,663	269,131	1,254,914
Between April 2017 and March 2022	792,049	296	30,218	47,069	869,632
Thereafter	2,731,307	258	13,657	220,339	2,965,561
At 31 March 2011	4,450,007	61,925	325,477	647,633	5,485,042

Included in the amounts not expected to be called until after 2022 are:

	Nuclear Decommissioning £000	Other Decommissioning and Restoration Costs £000	Early Retirement Commitments £000	Other £000	Total £000
Amounts not expected to be called until the period beginning April 2022	2,209,575	258	13,657	220,168	2,443,658
Amounts not expected to be called until the period beginning April 2060	302,985	-	-	171	303,156
Amounts not expected to be called until the period beginning April 2085	218,747	-	-	-	218,747
	2,731,307	258	13,657	220,339	2,965,561

Nuclear Decommissioning

23.2 Nuclear decommissioning provisions relate principally to the cost of decommissioning of facilities and the treatment and storage of nuclear waste arising from operations at MOD sites and the operation of Royal Navy submarines. The liabilities include the costs associated with decommissioning and care and maintenance of redundant facilities (the conditioning, retrieval and storage of contaminated materials), research and development and the procurement of facilities to handle the various waste streams. MOD is also responsible for the Atomic Weapons Establishment.

In applying accounting policies it is necessary to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. The nuclear provisions are based on the most recently available estimates discounted at 2.2% per annum in line with HM Treasury guidance. These estimates are necessarily based on assumptions of the processes and methods most likely to be used to discharge the obligations reflecting a combination of the latest technical knowledge available, the timescales involved and the requirements of the existing regulatory regime, Government policy and commercial agreements. However, there remains a significant degree of uncertainty in the future Government strategy, programme interdependencies and the processes involved, cost estimates and possible technological advances. The uncertainties that surround nuclear provisions mean that quantifying the incremental financial impact of various possible outcomes is very difficult, given the risk included in these activities. In context, risk means the financial implications of a large range of possible outcomes associated with nuclear decommissioning for example a change in the discount rate of 0.1% would result in a change in the valuation of the liability of approximately £100M.

For decommissioning operations with an end date costs have been calculated to that date; for operations of an ongoing nature (e.g. storage of materials) costs have been calculated for a period of 150 years. The latest estimate of the undiscounted cost of dealing with the MOD's nuclear liabilities is £10,126,295,000 (2009-10: £9,343,264,000). The estimate of £4,450,007,000 (2009-10: £4,736,802,000) at 31 March 2011 represents the liabilities discounted at 2.2% to the reporting date.

Other Decommissioning and Restoration

23.3 Other decommissioning and restoration provisions relate primarily to contaminated sites where the Department has a constructive or a legal obligation to restore the sites for normal use. The estimated payments are discounted by the Treasury discount rate of 2.2% in real terms. During 2010-11 existing provisions have been used to offset expenditure for the removal of asbestos in the UK, and restitution of former ranges and training areas.

Early Retirement Pensions

23.4 The Department meets the additional costs of benefits beyond the normal civil service pension scheme benefits in respect of employees who retire early by paying the required amounts annually to the pension schemes over the period between early departure and normal retirement date. The Department provides for this in full when the early retirement programme becomes binding by establishing a provision for the estimated payments discounted by the Treasury discount rate applicable to such provisions (currently 2.9%). During 2010-11 a new provision was created for the first year of a MOD wide Voluntary Early Release Scheme (£130,000,000). Increases of £27,865,000 were made to existing schemes and early retirement / redundancy costs charged to provisions during the period amounted to £61,657,000.

Other

23.5 The balance on Other provisions of £647,632,000 includes: costs arising from the disposal of non current assets, redundancy and relocation costs associated with reorganisation and restructuring (£345,967,000 – which includes £344,997,000 in respect of Locally Employed Civilian pensions) and amounts payable under guarantees, litigation and contractual arrangements (£301,665,000). During 2010-11 provisions have been increased for legal claims (£174,104,000) and Locally Employed Civilian pensions (£43,246,000 – offset by a reduction of £55,800,000). Costs charged to provisions during the period amounted to £128,597,000 and included £115,935,000 in respect of legal claims and £12,662,000 for Locally Employed Civilian pensions.

23.6 The movement in provisions includes a reduction in respect of pension schemes covering some locally employed civilians overseas. The reduction follows a change in the calculation of the scheme benefits which, for the purposes of index-linked features, now uses the Consumer Price Index (CPI); previously the Retail Price Index (RPI) was used.

23.7 In line with all central Government reporting entities where RPI has been used for inflation indexing for many years, the change from RPI to CPI has been recognised as a negative past service cost in accordance with IAS 19. The question of whether, as regards the main public service pensions schemes, there is a legitimate expectation that RPI will be used for inflation indexing is currently before the courts in judicial review proceedings. The Government case is that no legitimate expectation exists and that, in any event, even if there was a legitimate expectation this was overridden by the clear public interest in making very substantial savings at a time when the Government had adjudged that deficit reduction was a fundamental objective for the country. If the Government's case is proven, there would be no change to the accounting treatment adopted in these accounts.

24. Segmental Analysis

24.1 Information on operating activities, financial results, forecasts and plans is presented to and reviewed by the Defence Board on an aggregated basis. This reflects the way in which the Department manages its business in that the resources and activities of each of the Top Level Budget areas (see Note 2) must be aggregated in order to determine the overall cost of delivering the Department's principal output of providing the UK's defence capability.

24.2 For financial reporting purposes, the Department is therefore considered to have a single operating segment.

25. Capital Commitments

Capital commitments, for which no provision has been made in these financial statements, are:

	31 March 2011 £000	31 March 2010 £000
Intangible assets	1,479,783	2,642,846
Property, plant and equipment	16,582,564	20,544,090
	18,062,347	23,186,936

26. Commitments Under Leases

The total of future minimum lease payments under operating and finance leases for the periods: not later than one year; later than one year but less than five years and later than five years set out below:

26.1 Operating leases:

	31 March 2011 £000	31 March 2010 £000
Obligations under operating leases comprise:		
Land		
Not later than one year	897	808
Later than one year and not later than five years	2,492	2,058
Later than five years	1,391	3,741
	4,780	6,607
Buildings		
Not later than one year	52,867	58,120
Later than one year and not later than five years	148,255	171,116
Later than five years	203,066	239,168
	404,188	468,404
Other		
Not later than one year	117,138	74,384
Later than one year and not later than five years	171,086	190,687
Later than five years	77,808	119,547
	366,032	384,618

26.2 Obligations under finance leases (restated to include commitments in respect of leased land included in the accounts for the first time following a change in accounting policy):

	31 March 2011 £000	31 March 2010 £000
Obligations under finance leases comprise:		
Land		
Not later than one year	48,042	47,925
Later than one year and not later than five years	192,168	191,815
Later than five years	8,839,729	8,746,317
	9,079,939	8,986,057
Less interest element	(8,231,225)	(8,132,771)
	848,714	853,286
Buildings		
Not later than one year	47,848	47,734
Later than one year and not later than five years	191,393	190,886
Later than five years	8,804,041	8,828,488
	9,043,282	9,067,108
Less interest element	(8,197,995)	(8,224,108)
	845,287	843,000
Other		
Not later than one year	39,322	33,596
Later than one year and not later than five years	111,466	106,657
Later than five years	147,584	131,904
	298,372	272,157
Less interest element	(68,656)	(77,865)
	229,716	194,292

27. Commitments Under IFRIC 12 Service Concession Arrangements

27.1 All PPP / PFI arrangements have been assessed in accordance with IFRIC 12 – Service Concession Arrangements as adopted by HM Treasury. Any arrangements not fulfilling the criteria for IFRIC 12 have subsequently been assessed against IFRIC 4 (Determining whether an arrangement contains a lease) and IAS 17 (leases). The following PFI arrangements fulfilled the criteria for IFRIC 12 and the assets have been accounted for as assets of the Department:

Project Description	Contract Start*	Contract End
Training, Administration and Financial Management Information System: Provision of training administration and financial management information systems to the Army Recruiting and Training Division	Aug 1996	Nov 2012
Defence Fixed Telecommunications System: Integration of 50 fixed telecommunications networks used by the Armed Forces and MOD, including the delivery of voice, data, LAN interconnect and other WAN services	Jul 1997	Jul 2015
Medium Support Helicopter Aircrew Training Facility: Provision of 6 flight simulator training facilities, covering three different types of helicopter, at RAF Benson	Oct 1997	Oct 2037
Service Personnel & Veterans Agency: Provision of personnel administration, pay and pensions services for military personnel – interim contract	Nov 2009	Nov 2012
Hawk Synthetic Training Facility: Provision of replacement simulator training facilities at RAF Valley	Dec 1997	Dec 2015
Joint Services Command and Staff College (JSCSC): Design and delivery of a new tri-Service Command and Staff Training College infrastructure and supporting services, including single residential accommodation and married quarters	Jun 1998	Aug 2028
RAF Lossiemouth Family Quarters: Redevelopment and re-provision of 279 Service family quarters	Jun 1998	Aug 2020
Attack Helicopter Training Service: Provision of full mission simulator, 3 field deployable simulators, ground crew, maintenance and armament training	Jul 1998	Sep 2017
Family Quarters Yeovilton: Provision of married quarters accommodation for 88 Service families at RNAS Yeovilton	Jul 1998	Jul 2028
RAF Lyneham Sewage Treatment: Refurbishment of existing sewage treatment facilities, serving a population of 7,000, to meet regulatory standards at RAF Lyneham	Aug 1998	Aug 2023
VEOLIA PFI (formerly Thames Water and Tidworth Water and Sewage): Pathfinder project providing water, sewerage and surface water drainage, serving a population of 12,000 military and dependants at Tidworth	Feb 1998	Aug 2018
RAF Mail: Provision of informal messaging services for the RAF	Nov 1998	Mar 2011
RAF Fylingdales: Provision of guaranteed power supply	Dec 1998	Mar 2024
RAF Cosford/RAF Shawbury Family Quarters: Provision of married quarters accommodation for 145 Service families at RAF Cosford and RAF Shawbury	Mar 1999	Jun 2025
Fire Fighting Training Units: Provision of fire fighting training for the Royal Navy	Apr 1999	Dec 2020
Tornado GR4 Synthetic Training Service: Provision of aircraft training service at RAF Marham and RAF Lossiemouth	Jun 1999	Jun 2031
Central Scotland Family Quarters: Provision of married quarters accommodation for 164 Service families in Central Scotland	Aug 1999	Jan 2021
Army Foundation College: Provision of teaching and training facilities for the further vocational education and military training of high-quality school leavers	Feb 2000	Dec 2029
Main Building Refurbishment: Redevelopment and management services for MOD Main Building	May 2000	May 2030
Tri-Service Material Handling Equipment: Provision of Tri-Service materials handling capability	Jun 2000	Jan 2011
Defence Electronic Commerce Service: Strategic partnership to deliver e-business environment to share information between MOD and trading partners	Jul 2000	Jul 2010
E3D Sentry Aircrew Training Service: E3D Sentry simulators instructors and maintainers at RAF Waddington	Jul 2000	Dec 2030
Lynx MK 7 and 9 Aircrew Training Service: Provision for simulator training facility for Lynx MK 7 and 9 helicopter aircrew	Jul 2000	Jul 2025
Family quarters at Wattisham: Provision of married quarters accommodation for 250 Service families	May 2001	Mar 2028
Astute Class Training: Provision of a training environment for crewmen and maintainers to support Astute Class submarines for 30 years	Sep 2001	Sep 2037
Defence Housing Information Systems: Provision of a management information system for Defence Housing	Oct 2001	Oct 2011
Family quarters at Bristol/Bath/Portsmouth: Provision of accommodation for 317 Service families	Nov 2001	Sep 2028
Heavy Equipment Transporters: Provision of vehicles to replace existing fleet and meet future requirements	Dec 2001	Jul 2024
Field Electrical Power Supplies: Provision of generator sets to support operational electrical requirements in the field	Jun 2002	Jun 2022
Material Handling Equipment: Provision of Tri-Service material handling equipment for Army, Navy and RAF storage depots	Aug 2002	Jan 2011
Flight Simulation and Synthetic Trainers: Provision of a Flight Simulation and Synthetic Trainers Integrated Aircrew Synthetic Training Service	Oct 2002	Mar 2017
Aquatrine Project A: Provision of water and waste water services	Apr 2003	Nov 2028

Project Description	Contract Start*	Contract End
Aquatrine Project B: Provision of water and waste water services	Sep 2004	Mar 2030
Aquatrine Project C: Provision of water and waste water services	Oct 2004	Mar 2030
Naval Communications: Submarine fleet communications service	Jun 2003	Dec 2030
Defence High Frequency Communications Services: Provision of High Frequency communication services	Jun 2003	Jun 2018
Defence Sixth Form College: Development of a sixth form college to help meet the future recruitment requirements in the Armed Forces and MOD Civil Service	Jun 2003	Aug 2033
Skynet 5: Range of satellite services, including management of existing Skynet 4 satellites	Oct 2003	Feb 2020
Colchester Garrison: Redevelopment, rebuilding and refurbishment to provide accommodation and associated services (messing, education, storage, workshops)	Feb 2004	Feb 2039
Devonport Armada Single Living Accommodation: Provision of Support Services and Fleet Accommodation Centre services at Devonport Naval Base	Jul 2004	Mar 2029
C Vehicles: Provision of Earthmoving and Specialist Plant, Engineer Construction Plant and Material Handling Equipment and support services	Jun 2005	Jun 2021
Portsmouth 2 Housing: Provision of 148 Family quarters in Portsmouth	Oct 2005	Oct 2030
Project Allenby/Connaught: Rebuild, refurbishment, management and operation of facilities for Service accommodation at Aldershot, Tidworth, Bulford, Warminster, Larkhill and Perham Down	Mar 2006	Apr 2041
Defence Medical Information Capability Programme: provision of information capability system for the Defence Medical Services	May 2006	Apr 2016
Northwood: Rebuild, refurbishment, management and operation of facilities for the Permanent Joint Headquarters	Jul 2006	Oct 2031
Combined Aerial Targets (CATS): Provision of aerial targets and associated ground equipment and support services	Dec 2006	Mar 2028
Provision of Marine Services: Provision of marine services at UK Dockyard Ports at Portsmouth, Devonport and Clyde and support to military exercises, training and deep water trials, worldwide	Dec 2007	Dec 2022
Future Strategic Tanker Aircraft (FSTA): FSTA is an innovative PFI programme that will provide modern air-to-air refuelling and passenger air transport capabilities	Mar 2008	Mar 2035
Corsham Development Project: Rebuild, refurbishment, management and operation of facilities at the Basil Hill site	Aug 2008	Jul 2033
UK Military Flying Training System: Advanced Jet Trainer, Ground Based Training Equipment Element: Management and provision of Fast Jet Phase IV training	May 2008	May 2033

* Date when contract signed

27.2 The substance of an arrangement accounted for under IFRIC 12 is that the Department has a finance lease with the provider with payments comprising an imputed finance lease charge, a repayment of capital and a service charge. Payments are accounted for within the Statement of Comprehensive Net Expenditure – Service Concession Arrangements (SCA) and charges for 2010-11 were £1,076,773,000 (2009-10 £1,132,982,000). Total obligations under SCA (consisting of the minimum lease payments, interest and any minimum service charges) analysed by time periods are shown in the table below:

	31 March 2011 £000	31 March 2010 £000
Total obligations under Service Concession Arrangements for the following periods comprise:		
Not later than one year	401,772	382,776
Later than one year and not later than five years	1,882,210	1,492,220
Later than five years	4,097,574	4,285,515
	6,381,556	6,160,511
Less interest element	(2,720,908)	(2,663,966)
	3,660,648	3,496,545

27.3 The following table is a forecast of the total expenditure likely to be incurred under Service Concession Arrangements. The expenditure is based currently expected levels of usage and covers the minimum lease payments, the financing charge and payments for service delivery. The expenditure is analysed according to the periods when the payments are expected to be made.

	31 March 2011 £000
Total payments committed	
Not later than one year	1,437,922
Later than one year and not later than five years	4,878,083
Later than five years and not later than ten years	4,199,127
Later than ten years and not later than fifteen years	2,876,879
Later than fifteen years and not later than twenty years	2,030,214
Later than twenty years and not later than twenty five years	1,364,784
Later than twenty five years and not later than thirty years	951,107
	17,738,116

28. Contingent liabilities and contingent assets disclosed under IAS 37

Contingent Liabilities

28.1 The following quantifiable contingent liabilities have been identified:

Description	Liability at 31 March 2011 £000
Indemnity to contractors in respect of nuclear risks and decontamination	279,886
Restricted – not disclosed due to reasons of commercial confidentiality and / or national security	160,842
Indemnity to contractors for third party risks	144,455
Statutory liability for International Military Sales	100,000
Liability for redundancy following contractorisation	24,125
Redundancy costs associated with the rationalisation of basing arrangements in Germany	31,232
Indemnity for utilities and services following the sale of Service housing	17,031
Environmental clean up costs	12,875
Underwriting costs associated with Defence Training Review	3,500
Indemnity for non-MOD personnel in operational theatres	3,052
Legal claims (personal)	1,574
Indemnity for excavation of the wreck of British warship Sussex	1,185
Contractor claim relating to project deferment	539
Total quantifiable contingent liabilities	780,296

The Department has a number of unquantifiable liabilities in accordance with IAS 37:

- Indemnities to AWE Management Ltd for non-nuclear risks
- Standard shipbuilding indemnity in respect of Vanguard and Astute class submarines
- Service Life Insurance – providing access to life insurance for service personnel. Details of the scheme and key features can be found at www.servicelifeinsurance.co.uk
- Guarantee to NAAFI
- Indemnity to Services Sound and Vision Corporation (SSVC) for costs arising from the early termination of the contract
- Strategic Defence and Security Review (SDSR) – Contracts affected by SDSR decisions are being renegotiated. Where settlements have already been reached with industry the financial impact has been included in the 2010-11 accounts. The Department will have to assess and potentially renegotiate up to 500 contracts and cannot estimate the potential scale of future cancellation and restructuring claims.
- The Department has a number of sites where it may be necessary to carry out decontamination work. As it is not practicable or cost effective to identify all contamination at those sites, any possible liability is not quantifiable, so possible future site remediation exposure is recognised as an unquantifiable contingent liability under IAS 37.

Contingent assets

28.2 A US salvage company, Odyssey Marine Exploration, has found what is believed to be the wreck of the British warship Sussex, which sank in the Western Mediterranean in 1694 carrying gold and silver coins estimated to be valued at the time at £1 million. If confirmed as the Sussex, the wreck and its contents are legally the property of Her Majesty's Government.

A licensing agreement was signed on 27 September 2002 between the Disposal Services Authority of the Ministry of Defence, on behalf of Her Majesty's Government, and Odyssey for further archaeological exploration of the wreck and recovery of artefacts. Full responsibility for the project, including the sale of the artefacts has been transferred to the Department. Proceeds from the sale of any artefacts will be surrendered to HM Treasury. The Department will be responsible for the preservation of any part of the wreck brought up as part of the salvage effort.

Contingent liabilities not required to be disclosed under IAS 37

28.3 The MOD has entered into the following quantifiable contingent liabilities by offering guarantees, indemnities or by giving letters of comfort. None of these is a contingent liability within the meaning of IAS 37 since the likelihood of a transfer of economic benefit in settlement is too remote.

Quantifiable – unrestricted

	1 April 2010 £000	Increase in year £000	Liabilities crystallised in year £000	Obligation expired in year £000	31 March 2011 £000	Amount reported to Parliament by Departmental Minute £000
Unrestricted – Indemnities						
Residual liability for the remediation of unidentified contamination in parts of the former Rosyth Naval Base which has been sold to Rosyth 2000 plc	Up to 1,000				Up to 1,000	1,000
Liabilities arising from insurance risk of exhibits on loan to the museums of the Royal Navy, Army and Royal Air Force	2,600			(390)	2,210	
Indemnity to Help for Heroes and Royal British Legion should recovery centres have a change in use within ten years		28,400			28,400	28,400
Remediation costs associated with the discovery of unknown environmental contamination at the Fleetlands site	14,000				14,000	14,000
Uninsured liability during Typhoon Field Evaluation Trial		45,000		(45,000)		

Quantifiable – restricted

28.4 Details of restricted indemnities are not given due to reasons of commercial confidentiality and / or national security.

Unquantifiable – unrestricted

28.5 The MOD has entered into the following unquantifiable contingent liabilities by offering guarantees, indemnities or by giving letters of comfort. None of these is a contingent liability within the meaning of IAS 37 since the possibility of a transfer of economic benefit in settlement is too remote.

- Indemnity given in relation to the disposal of Gruinard Island in the event of claims arising from the outbreak of specific strains of anthrax on the Island.
- Indemnities to the Babcock Group in respect of nuclear risks under the Nuclear Installations Act 1965.
- Indemnities to the Babcock Group in respect of non-nuclear risks resulting from claims for damage to property or death and personal injury to a third party.
- Indemnity to Rolls-Royce Power for the non-insurance of the Rolls-Royce Core Factory and the Neptune Test Reactor facility for death and personal injury to a third party.
- Indemnity for residual commercial contracts claims liabilities arising from the disbanding of DERA as a MOD Trading Fund and the formation of QinetiQ on 1 July 2001.
- Indemnity for residual employee disease liability arising from the disbanding of DERA as a MOD Trading Fund and the formation of QinetiQ on 1 July 2001.
- Indemnity for residual public liability arising from the disbanding of DERA as a MOD Trading Fund and the formation of QinetiQ on 1 July 2001.
- Indemnity for environmental losses incurred by QinetiQ arising from certain defined materials at specific properties before the formation of QinetiQ on 1 July 2001.

Unquantifiable – restricted

28.6 Details of restricted indemnities are not given due to reasons of commercial confidentiality and / or national security.

29. Losses and Special Payments

29.1 Losses

CLOSED CASES: these are losses that have been formally signed off following completion of all the relevant case work. Closed cases include some cases which in previous years were shown as Advance Notifications.	Arising in 2010-11 £000	Reported in 2009-10 as Advance Notifications £000
Total Losses (excluding gifts) under £250,000 each: 16,068 cases	34,177	
Total Losses (excluding gifts) over £250,000 each: 27 cases (detailed below)	76,769	179,389
Totals	110,946	179,389
Total Value of Closed Cases – Arising in 2010-11 and Reported in 2009-10 as Advance Notifications	290,335	
Details of the Closed Cases over £250,000 each are:		
Bookkeeping Losses		
Write-off of unsupported balances following asset verification exercises. The loss consists of balances that could not be verified with the information available.	863	
	863	-
Fruitless Payments		
The value of 8 Chinook Mk3 helicopters which did not meet the operational requirement and could not acquire Military Aircraft Release were originally written down by £205M pending a decision on the future of the aircraft. This value has previously been reported in the MOD accounts as an advanced notification of a potential loss. The MOD has now successfully converted the Mk3 airframes to a modified standard and all 8 aircraft were accepted into service during 2010. As a result the final value of the loss has now been calculated at £103m; £94M to recognise the additional (fruitless) payment incurred in bringing these aircraft into service and £9m which reflects the difference between the planned capability of the original MK3 aircraft and the revised standard of the aircraft brought into service.		103,000
A Fruitless Payment arising from the unsuccessful development of a demolition device and a disablement device due to technical complexities.	4,875	
Unsuccessful procurement of Commercial Off The Shelf weapon system that subsequently failed quality and critical Safe and Suitability for Service trials.	1,982	
A loss has arisen due to the need for early cancellation of the Synergy mobile managed service contract.		1,885
After a furniture contract ended the company commenced court action for recovery of stock they had purchased and held on MOD's behalf. An out of court settlement has been reached.	1,691	
During testing at the Naval Air Warfare Center in China Lake, California a warhead ignited causing damage to the test house and some equipment.	1,088	
Delay to HMS Lancaster's Standard Support Period (Docking) ⁴ resulted in a claim by the contractor for regeneration work.	606	
Legal costs of defending an unfair dismissal claim by two members of the Gibraltar Service Police and unrecovered salary paid while they were suspended and the case was being handled in the courts.		431
	10,242	105,316
Constructive Losses		
As a result of the Dublin Diplomatic Conference it was agreed to cease the use, development, production and transfer of Cluster Munitions resulting in a Constructive Loss.		55,287
The MOD has reviewed its requirement for a Typhoon General Purpose Automatic Test Equipment (GPATE) capability and determined that the majority of the GPATE is no longer needed which has resulted in a constructive loss.	27,200	
Cancellation of the Systems Engineering Facility to support research and development of non-nuclear components for Trident in favour of a more cost effective approach.	16,825	
Termination of the Ballistic Sensor Fused Munition project as a result of technical difficulties has resulted in a Constructive Loss.		11,587
The MOD has reviewed its requirement for a Typhoon Ground Loading Station capability and determined that it is no longer needed resulting in a constructive loss.	10,984	
Cancellation of work on a facility to build a nuclear reactor core has resulted in a Constructive Loss.		2,520
A Constructive Loss has occurred from the cancellation of three new build projects due to the closure of RAF Cottesmore.	564	
Contract amendments due to de-scoping of a capability requirement resulted in a Constructive Loss.		546
A constructive loss has arisen following the re-design of the General Service Respirator Haversack.	510	
Procurement of security system that was not fit for purpose.	510	

CLOSED CASES: (continued)	Arising in 2010-11 £000	Reported in 2009-10 as Advance Notifications £000
A decision was taken not to proceed with the procurement of the dummy round element of the Next generation Light Anti-armour Weapon Training Solution. During the development phase MOD identified an alternate solution to meet the requirement at lower cost without loss of capability.	495	
A Constructive Loss has arisen on a contract for the refurbishment of Kitchener Hall at the Defence Academy, Shrivenham, following a change in requirement for the use of the premises.		281
	57,088	70,221
Claims waived or abandoned		
Charges waived for non-delivery of equipment due to bankruptcy of contractor.	4,086	
Claim waived against a contractor on the WATCHKEEPER Programme due to late delivery of equipment. Benefits valued at £9.3m were received in lieu.	3,232	
A Generator Contract – Claim abandoned as a result of a misunderstanding of a contract's indexation provisions.	758	
A failure to invoice NAAFI Support Services for payroll administration costs (dating back to 1999).		720
Claim waived against a contractor for late delivery of equipment. As consideration for waiving the claim MOD was offered and accepted equipment due for delivery from another contract valued at £550k.	500	
The loss represents the expected difference (the amount waived) between the maximum level of charges which the Department could raise against EDS for its failure to deliver contract requirements and the level of charges actually raised during the year.		3,132
	8,576	3,852
Gifts		
Total under £250,000 each: 25 cases	686	
Total over £250,000 each: 1 cases (detailed below)	1,686	
	Total	2,372
Detail of the gift over £250,000 is:		
Notified during the year		
Fibre glass helmets and body armour to the Government of Uganda.	1,686	
International Courtesy Rules		
Supplies and services provided on a reciprocal basis to Commonwealth and Foreign Navy vessels during visits to British Ports at Clyde, Portsmouth, Devonport and Gibraltar.	605	

Losses – Advanced Notifications

ADVANCE NOTIFICATIONS: these are losses, which arose during 2010-11 and prior years, but where the cases have not yet been formally signed off because all the work necessary to establish the validity of the loss, and the exact amount thereof, has not yet been concluded. The amounts shown below are, therefore, estimates, and it is likely that the final value of these losses will differ when they are reported as closed cases in future years. Should the final value be less than £250,000, they will not be separately identified.	Arising in 2010-11 £000	Reported in 2009-10 as Advance Notifications £000
Total Advance Notifications over £250,000 each	6,532,479	76,578
	6,609,057	
Notified in prior years		
Bookkeeping and Cash Losses		
A potential loss has been identified in respect of an overpayment made to a MOD contractor. Whilst repayment is being actively pursued, there is no assurance that the overpayment can be recovered owing to statute of limitation restrictions.		372
Potential false claims of Continuity Education Allowance.	500	
	500	372
Stores Losses		
Loss of a Typhoon aircraft which crashed on landing at US Naval Air Weapons Station, California and was damaged beyond economic repair.		49,420
Write-off of unsupported balances following verification of inventory holdings. The loss consists of balances that could not be verified with the information available.	36,000	
Vehicle fire during exercise training completely destroying the vehicle.	256	
	36,256	49,420
Claims waived or abandoned		
Costs may not be fully recovered for support provided by the UK to other nations contributing to the International Security Assistance Force.	–	
	–	–
Fruitless Payments		
Non-refundable flying training tuition fees, incurred over a four year period, following a change to a better value for money option.		24,400
Costs associated with the grounding of HMS ASTUTE and subsequent towing incident	2,359	
Between April 2008 and January 2010, a total of four Gnome helicopter engines were damaged by transportation in the incorrect orientation, necessitating corrective engineering work by Rolls Royce.		711
Between February 2009 and January 2010, a total of fourteen Gnome helicopter engines were damaged by being incorrectly packaged in their Special-to-Type Containers, necessitating corrective engineering work by Rolls Royce.		1,675
	2,359	26,786
Constructive Losses		
A joint radiographic and hydrodynamics facility with France resulted in the termination of Project Hydrus.	120,446	
Following a capability review a decision was made that the Shielder Anti-Tank mine canisters and associated vehicles were no longer required.	44,267	
A constructive loss has occurred due to a change of requirement for the Joint Combat Aircraft.	8,910	
Project Soothsayer: contract terminated. The matter is subject to arbitration and may result in a Constructive Loss.		–
A project was cancelled as it was considered that the main contractor had failed to achieve the anchor milestone, and therefore the contract was terminated. Litigation is likely.	–	
SDSR Constructive Losses		
Cancellation of Nimrod MRA4.	3,626,020	
Early withdrawal from service of the Harrier fleet.	1,843,510	
Early withdrawal from service of 5 Royal Navy and 3 Royal Fleet Auxiliary vessels. The amount does not include potential contract termination costs as negotiations have not yet commenced.	725,411	
Settlement of additional SDSR related costs.	124,800	
	6,493,364	–
Gifts		
Notified in prior years		
Gifting of sites in Northern Ireland		26,500

29.2 Special Payments

CLOSED CASES: these are special payments that have been formally signed off following completion of all the relevant case work. Closed cases include some cases which in previous years were shown as Advance Notifications.	Arising in 2010-11	Reported in 2009-10 as Advance Notifications
	£000	£000
Total (excluding War Pensions Benefit) under £250,000 each: 131 cases	607	
Total (excluding War Pensions Benefit) over £250,000 each: 2 cases (detailed below)	12,000	6,812
Total War Pensions Benefit under £250,000 each: 7 cases	42	
Total War Pensions Benefit over £250,000 each: 335 cases	1,638	
	14,287	6,812
Totals	21,099	
Details of the 2 cases over £250,000 are:		
Employment Tribunal Compensation payments to former Part Time members of the Royal Irish Regiment.		6,812
Extra-Contractual payment in respect of the Land Environment Air Picture Provision project	12,000	
	12,000	6,812
Special Payments – War Pensions Benefit cases over £250K		
Total number of payments made during the year was 342 at a total cost of £1,680,407. These payments were for War Disability Pensions, and were made under the authority of Treasury Dispensing Instruments but outside the scope of the Service Pension order. These relate to the following payments:		
(a) Far Eastern Prisoners of War Ex-gratia payments		
In the 2000 pre-Budget speech, the Chancellor of the Exchequer announced that ex-gratia awards of £10,000 would be paid to surviving members of British groups held prisoner by the Japanese during the Second World War or their surviving spouses, including the Gurkhas from November 2003. Although, the majority of cases have been paid in previous financial years, 46 claims were processed and paid in 2010-11.	460	
(b) Empire Air Training Scheme Pensions		
These Payments relate to members of the Royal Australian Air Force who were trained under the Empire Air Training Scheme and were subsequently selected for service in the RAF. The British Government agreed in June 1942 that it would contribute towards pensions in respect of disablement or death due to service with the RAF. The number of cases in 2010-11 was 155.	794	
(c) Noise Induced Sensorineural Hearing Loss		
During financial year 2010-11 134 payments were made.	384	
	1,638	
Notified during the year - Advanced Notification		
Extra-Contractual payments to indemnify a contractor for the redundancy costs of former MOD staff transferred under TUPE arrangements.	1,800	

30. Related Party Transactions

30.1 The Defence Science and Technology Laboratory, the UK Hydrographic Office, the Met Office, and the Defence Support Group operate as Executive Defence Agencies financed by Trading Fund. The Navy Army Air Force Institutes (NAAFI) and the Oil and Pipelines Agency are Public Corporations.

The Trading Funds, the Oil and Pipelines Agency and the NAAFI are regarded as related parties outside the Departmental Boundary with which the Department has had material transactions. Transactions are carried out on terms which are contracted for on an arms-length basis, and are subject to internal and external audit. The values of transactions with some of these organisations are set out below and balances with the Trading Funds (excluding loans and dividends, which are shown at Note 16) at year end, are in the following table:

Organisation	Receivables Balances £000	Payables Balances £000
Defence Science and Technology Laboratory	2,914	10,070
UK Hydrographic Office	3,190	(106)
Met Office	221	7,869
Defence Support Group	5,739	13,329

Oil and Pipelines Agency (Public Corporation)

Agency Fees (excluding VAT): £3,095,000 (2009-10: £2,220,000)

Director Finance Defence Equipment & Support (DE&S), Commercial Director DE&S and the Head of Financial Management Policy and Development for the MOD are members of the Board of Directors.

Navy Army Air Force Institutes (NAAFI)

The NAAFI Council acts as the most senior NAAFI body responsible for approving the policy and direction of NAAFI's business. The rules governing the NAAFI Council and its proceedings are laid out in NAAFI's Memorandum and Articles of Association. The Council's membership consists of: Deputy Chief of Defence Staff (Personnel & Training) (President); Assistant Chief of Naval Staff, Adjutant General, Deputy Commander-in-Chief Personnel, Director Service Personnel Policy, Chief of Joint Operations, DE&S – Head of Commercial Command and Centre; as well as the Chairman and Deputy Chairman of NAAFI. During 2010-11 receipts from NAAFI were £350,000 (2009-10: £97,000); payments to NAAFI were £19,811,000 (2009-10: £21,509,000). During 2010-11 the contract with NAAFI for provision of services on German bases was extended until 2018.

Executive Non-Departmental Public Bodies (NDPBs)

30.2 The following are Executive NDPBs of the MOD. They are designated NDPBs under the National Heritage Act 1983 and produce their own annual accounts, in accordance with the Charities (Accounts and Reports) Regulations 2005, on an accruals basis, and are regarded as related parties. During the period 1 April 2010 to 31 March 2011, each Executive NDPB had a material transaction with the Department, as listed below:

National Army Museum

Grant-in-Aid: £6,312,000 (2009-10: £5,515,000)

Further information can be found at: www.national-army-museum.ac.uk

Royal Air Force Museum

Grant-in-Aid: £7,552,000 (2009-10: £7,367,000)

Further information can be found at: www.rafmuseum.org.uk

The National Museum of the Royal Navy

Grant-in-Aid £2,797,000 (2009-10: £3,237,000)

Further information can be found at: www.royalnavy.mod.uk

Other

30.3 The Department also pays a number of grants to other bodies outside the Departmental Boundary. These include Grants-in-Aid to: the Council of Reserve Forces and Cadets Associations (£62.8M), the Commonwealth War Graves Commission (£44.6M), the Royal Hospital Chelsea (£10.8M), the Marine Society & Sea Cadets (£9.2M), the Gurkha Welfare Scheme (1.4M).

30.4 The MOD works closely with many charitable organisations and this can include representation on governing bodies, for example: The Secretary of State for Defence is trustee of Greenwich Hospital; The Minister for International Security Strategy is a trustee of the Vulcan to the Sky Trust (the trust paid MOD £267,000 for supplies and services during 2010-11 and had a further balance, due to be paid, of £149,000; payments by MOD to the trust totalled £9,000); 2nd PUS is an ex officio trustee of the Imperial War Museum; PUS is a trustee of the Whitehall Industry Group (the Group had transactions of £16,000 with MOD during 2010-11), Chief of the Air Staff is a trustee of the Yorkshire Air Museum and the former Chief of Defence Material was a trustee of SSAFA Forces Help (the Department made payments to SSAFA of £17,021,000 and received £1,685,000 from the charity). In addition the Office of National Statistics has classified ABF The Soldiers' Charity as a public sector body sponsored by the Department; MOD has no financial transactions with the charity.

30.5 The MOD has also had a number of transactions with other government departments and central government bodies. Most of the transactions have been with: the Foreign & Commonwealth Office, the Security and Intelligence Services, the Home Office, the Skills Funding Agency, UK Trade and Investment, the Procurator General and Treasury Solicitor, the Cabinet Office, the Department for Work and Pensions, the Department for Environment Food and Rural Affairs, HM Revenue and Customs and the Department for International Development.

Joint Ventures

30.6 There are no Joint Ventures within the Departmental accounting boundary. Some of the Trading Funds have set up Joint Ventures and the Department is involved in collaborative projects with various foreign countries for the development and production of Single Use Military Equipment.

31. Events After The Reporting Date

31.1 These accounts have been authorised for issue by the Accounting Officer on the same date as the C&AG's Audit Certificate.

31.2 The Secretary of State has announced further work is to be conducted in order to finalise the impact of the Strategic Defence and Security Review. This will complete in the summer of 2011. The outcome of the work may lead to further announcements on the scale of equipment to be withdrawn from service, reductions in capability and/or cancellation of new and existing equipment programmes. These decisions are, therefore, likely to impact the overall value of the Statement of Financial Position (SoFP) and lead to write off action which will in turn result in an increase in the net operating costs of the Department during 2011-12 and beyond.

32. Non-Operational Heritage Assets

32.1 The Department owns a range of non-operational heritage assets from historically significant defence equipment, through archive information, to museum and art collections. In accordance with the FReM, non-operational heritage assets are valued except where the cost of obtaining a valuation for the asset is not warranted in terms of the benefits it would deliver or where it is not possible to establish a sufficiently reliable valuation.

On the above basis, no non-operational heritage assets, except land, were valued at the year-end.

32.2 The scope and diversity of the holdings of non-operational heritage assets which are not valued are illustrated by the examples detailed in the table below:

Item	Location	Description
HMS Victory	Portsmouth	HMS Victory is the world's oldest commissioned warship and is most famous for her role as Lord Nelson's Flagship at the Battle of Trafalgar. HMS Victory is open to the public, details are available at: www.hms-victory.com
Army Historic Aircraft Flight	Middle Wallop	Formed in 1977, the flight consists of seven aircraft and makes public appearances between May and September.
Battle of Britain Memorial Flight	RAF Coningsby	The Memorial Flight operates eleven mainly World War II aircraft that appear at several hundred public events each year and can also be viewed at their hangar at RAF Coningsby. Further information is available at: www.bbmf.co.uk/index.html
Statue of King George II	Citadel Plymouth	Lead statue of King George II dressed as a Roman Emperor.
Enigma Machine	RAF Cosford	Cryptographic equipment captured during World War II and used at Bletchley Park to assist in the breaking of German signal traffic.
Artefacts, records and artworks	Various locations	Over one hundred Regimental and Corps Museums and collections exist across the country. Ownership of the buildings and contents of the museums varies between the MOD, local authorities and regimental associations. The museums, which are open to the public, trace the history of the regiments and comprise displays of uniforms, weapons, medals and records. Further information is available at: http://www.army.mod.uk/events/museums/default.aspx
MOD Art Collection	Various locations	The MOD Art Collection comprises approximately 800 works of fine art and 250 antiques such as clocks and furniture. Many other miscellaneous items, such as photographs and manuscripts are contained in the archive. At the core of the collection are works commissioned by (and bequeathed to) the Admiralty during the 19 th century, and those given to the Admiralty and to the War Office by the War Artists Commission at the end of the Second World War. Items from the MOD art collections are displayed in conference rooms and senior officers' accommodation throughout the Defence estate. The most important items are on permanent public display in the National Maritime Museum and on temporary loan to many other public museums and galleries. Further information is available at: www.mod.uk/DefenceInternet/AboutDefence/WhatWeDo/DefenceEstateandEnvironment/MODArtCollection
Records and artworks	London, Gosport, Stanmore	The Admiralty and Institute of Naval Medicine Libraries and the Air Historical Branch (RAF) comprise text and records of historical and research items. Although not open to the public, access is available on application.

33. Entities within the Departmental Boundary

The entities within the boundary during 2010-11 were as follows:

On Vote Agencies*
Defence Vetting Agency
Ministry of Defence Police and Guarding Agency
People, Pay and Pensions Agency*
Service Children's Education
Service Personnel and Veterans Agency*
Advisory Non-Departmental Public Bodies
Advisory Committee on Conscientious Objectors
Advisory Group on Military Medicine
Armed Forces Pay Review Body
Central Advisory Committee on Pensions and Compensation
Defence Nuclear Safety Committee
Defence Scientific Advisory Council
National Employer Advisory Board
Nuclear Research Advisory Council
Review Board for Government Contracts
Science Advisory Committee on the Medical Implications of Less Lethal Weapons
Veterans Advisory and Pensions Committees
Independent Monitoring Board for the Military Corrective Training Centre, Colchester

* Agency status was removed from the Defence Storage and Distribution Agency on 31 July 2010. The Service Personnel and Veterans agency ceased to be an Agency with effect from 16 June 2011. The People, Pay and Pensions Agency ceased to be an Agency with effect from 6 July 2011.

33.1 Changes to entities within the Departmental boundary for 2011-12

On 1 April 2011 Statutory Instrument 2011 No. 723 – The Government Resources and Accounts Act 2000 (Estimates and Accounts)
Order 2011 came into force. As a result the accounting boundary for the 2011-12 accounts is expected to expand to include the following bodies which are designated in the order:
National Museum of the Royal Navy
Royal Navy Submarine Museum
Royal Marines Museum
Royal Naval Museum
ABF The Soldiers' Charity
Council of Reserve Forces and Cadet Associations
National Army Museum
Royal Air Force Museum
Royal Hospital, Chelsea

34. Prior Period Adjustments

Additional details of the impact of prior period adjustments on taxpayers' equity are provided below:

Reconciliation of taxpayers' equity from 31 March 2009 to 1 April 2009						
	Notes	£000	General Fund £000	Revaluation Reserve £000	Donated Asset Reserve £000	Total £000
Taxpayers' equity at 31 March 2009*	SoCITE		83,431,462	22,401,843	2,479,450	108,312,755
Increase the worth of the General Fund by adding the value of leased land being accounted for in accordance with the revised policy on leased assets (IAS 17)		3,599,068	-	-	-	-
Reduction in value of the land as a result of the application of indexation factors under Modified Historic Cost Accounting (MHCA)		(997,139)	-	-	-	-
Depreciation of leased land		(20,560)	-	-	-	-
Reduction in the worth of the General Fund as a result of creating a liability for the future lease payments**		(848,717)	1,732,652	-	-	1,732,652
Taxpayers' equity at 1 April 2009***	SoCITE		85,164,114	22,401,843	2,479,450	110,045,407

* As published in the 2009-10 accounts.

** The value of the future lease payments (£848,717,000) is significantly lower than the value of the land (£3,599,068,000) mainly because the payments are discounted to present values and a higher proportion of the value of the repayments are made towards the end of the 200 year lease.

*** Following HM Treasury direction, the non-cash notional Cost of Capital Charge (CoCC) is no longer included in the accounts. The total charge included in the accounts in the period since the introduction of Resource Accounting in 2001-02, to 31 March 2009 was £29,504,852,000. HM Treasury directed that removal of the CoCC should not be included as a Prior Period Adjustment in the 2010-11 Resource Outturn. The net impact of the notional CoCC on the General Fund is nil and its removal therefore also has no impact on the General Fund balances.

34.1 Changes to Net Operating Costs are as follows:

	Notes	2009-10 £000
Net operating costs for 2009-10 prior to adjustments*		41,207,793
Reduction as a result of the removal of the Cost of Capital Charge for 2009-10		(3,827,560)
Reduction in other programme costs as a result of the reclassification of the lease for land from an operating lease to a finance lease under the revised International Accounting Standard 17 (IAS 17)	11	(48,042)
Increase in other programme costs – the cost of depreciation in respect of leased land which was added following the reassessment of the lease under the revised IAS 17		10,487
Impairment to the value of the land	11	652,026
Increase in interest payable as a result of the reclassification of lease payments, in respect of leased land, as interest on finance leases	13	48,041
Restated net operating costs for 2009-10	SoCNE	38,042,745

* As published in the 2009-10 accounts.

34.2 Reconciliation of Property Plant and Equipment from 31 March 2009 to 1 April 2009:

	Notes	£000
Total Property Plant and Equipment at cost or valuation as at 31 March 2009*		137,855,639
Add the value of leased land accounted for in accordance with the revised policy on leased assets (IAS 17)	34	3,599,068
Reduction in value of the land as a result of the application of indexation factors under Modified Historic Cost Accounting (MHCA)	34	(997,139)
Total Property Plant and Equipment at cost or valuation as at 1 April 2009	15	140,457,568
Less		
Total depreciation as at 31 March 2009*		(50,559,826)
Cumulative depreciation on the land added under IAS17	34	(20,560)
Total depreciation as at 1 April 2009	15	(50,580,386)
Total Property Plant and Equipment less depreciation as at 1 April 2009	SoFP	89,877,182

* As published in the 2009-10 accounts.

34.3 Reconciliation of Property Plant and Equipment as at 31 March 2010:

	Notes	£000
Total Property Plant and Equipment at cost or valuation as at 31 March 2010*		144,665,921
Impairments and revaluations in respect of leased land accounted for in accordance with the revised policy on leased assets		1,941,325
Total Property Plant and Equipment at cost or valuation as at 31 March 2010	15	146,607,246
Less		
Total depreciation as at 31 March 2010*		(54,931,975)
Cummulative depreciation on the leased land added under IAS17		(22,469)
Total depreciation as at 31 March 2010	15	(54,954,444)
Total Property Plant and Equipment less depreciation as at 31 March 2010	SoFP	91,652,802

* As published in the 2009-10 accounts.

34.4 Reconciliation of Trade and Other Payables due Within One Year:

	Notes	£000
Trade and other payables due within one year as at 31 March 2009*		9,078,493
Increase in the value of trade and other payables due within one year as a result of the inclusion of the liability for lease payments in respect of leased land added under IAS 17		1
Trade and other payables due within one year as at 1 April 2009	SoFP	9,078,494
Trade and other payables due within one year as at 31 March 2010*		9,246,606
Increase in the value of trade and other payables due within one year as a result of the inclusion of the liability for lease payments in respect of leased land added under IAS 17		1
Trade and other payables due within one year as at 31 March 2010	SoFP	9,246,607

* As published in the 2009-10 accounts.

34.5 Reconciliation of Non Current Liabilities – Other Payables:

	Notes	£000
Non current liabilities – other payables as at 31 March 2009*		4,461,864
Increase in the value of non current liabilities – other payables as a result of the inclusion of the liability for lease payments in respect of leased land added under IAS 17		848,716
Non current liabilities – other payables as at 1 April 2009	SoFP	5,310,580
Non current liabilities – other payables as at 31 March 2010*		4,547,705
Increase in the value of non current liabilities – other payables as a result of the inclusion of the liability for lease payments in respect of leased land added under IAS 17		848,715
Non current liabilities – other payables as at 31 March 2010	SoFP	5,396,420

* As published in the 2009-10 accounts.

35. Votes A Statement – Statement of Approved Maximum Armed Forces Numbers

35.1 Votes A provide the formal mechanism by which Parliament sets limits for and monitors the maximum numbers of personnel retained for service in the Armed Forces. They are presented to the House shortly before the start of each financial year (late February), and form part of the Parliamentary Supply process.

35.2 Votes A numbers represent uppermost limits for Service manpower; they neither predict actual strengths nor act as a control over numbers in the Services. Votes A includes a contingency margin to cover unforeseen circumstances. Manpower levels are monitored routinely, and if it is anticipated that the numbers could be breached, then a Supplementary Estimate may be required to increase the limit.

35.3 The tables included below compare, for each service, the numbers voted by the House of Commons with the maximum numbers maintained and the date at which this peak occurred. The aggregate maximum numbers maintained may not equal the sum of Officers plus Men and Women as these categories peak at different times of the year. The “Men and Women” categories represent the Services’ Ratings and Other Ranks.

35.4 Maximum numbers of personnel to be maintained for service with the Armed Forces:

		Numbers voted by the House of Commons	Maximum Numbers Maintained	Peak Dates
NAVAL SERVICE				
Royal Navy	Officers	7,100	6,680	October 2010
	Men and Women	26,500	24,130	April 2010
	Aggregate	33,600	30,780	June 2010
Royal Marines	Officers	1,050	890	September 2010
	Men and Women	7,900	7,410	February 2011
	Aggregate	8,950	8,280	February 2011
ARMY SERVICE				
Army	Officers	15,860	14,860	October 2010
	Men and Women	103,840	94,230	April 2010
	Aggregate	119,700	108,870	April 2010
Commonwealth, Colonial, etc, troops abroad and Gurkhas	Officers	160	160	May 2010
	Men and Women	4,170	3,960	March 2011
	Aggregate	4,330	4,100	March 2011
AIR FORCE SERVICE				
Royal Air Force	Officers	10,520	9,820	April 2010
	Men and Women	36,880	34,230	April 2010
	Aggregate	47,400	44,050	April 2010

35.5 Maximum numbers of personnel to be maintained for service with the Reserve Forces:

		Numbers voted by the House of Commons	Maximum Numbers Maintained	Peak Dates
RESERVE NAVAL AND MARINE FORCES				
Royal Fleet Reserve (Naval Officers and Ratings)	Officers	4,000	3,745	May 2010
	Men and Women	7,000	4,327	May 2010
	Aggregate	11,000	8,072	May 2010
Royal Fleet Reserve (Marine Officers and Marines)	Officers	400	246	May 2010
	Men and Women	2,000	1,477	May 2010
	Aggregate	2,400	1,723	May 2010
Royal Naval Reserve	Officers	950	745	April 2010
	Men and Women	1,430	1,266	December 2010
	Aggregate	2,380	2,002	December 2010
Royal Marines Reserve	Officers	105	65	September 2010
	Men and Women	912	763	September 2010
	Aggregate	1,017	828	September 2010
Royal Naval Reserve (List 7)	Officers	910	876	February 2011
RESERVE LAND FORCES				
Army Reserve	Officers	14,000	11,606	April 2010
	Men and Women	45,300	37,727	April 2010
	Aggregate	59,300	49,333	April 2010
Territorial Army	Officers	7,500	4,800	April 2010
	Men and Women	39,500	28,290	April 2010
	Aggregate	47,000	33,090	April 2010
RESERVE AIR FORCES				
Royal Air Force Reserve	Officers	4,100	3,773	April 2010
	Men and Women	6,500	5,167	April 2010
	Aggregate	10,600	8,940	April 2010
Royal Auxiliary Air Force	Officers	400	242	February 2011
	Men and Women	2,300	1,466	May 2010
	Aggregate	2,700	1,670	May 2010

35.6 Maximum numbers to be maintained for service as Special Members of the Reserve Forces:

		Numbers voted by the House of Commons	Maximum Numbers Maintained	Peak Dates
SPECIAL MEMBERS OF THE RESERVE NAVAL FORCES				
Royal Naval Reserve	Officers	923	147	January 2011
	Men and Women	630	115	July 2010
	Aggregate	1,553	259	May 2010
SPECIAL MEMBERS OF THE RESERVE LAND FORCES				
Territorial Army	Officers	5	-	
	Men and Women	150	130	April 2010
	Aggregate	155	130	April 2010
SPECIAL MEMBERS OF THE RESERVE AIR FORCES				
Royal Air Force Reserve	Officers	110	58	April 2010
	Men and Women	270	75	April 2010
	Aggregate	380	133	April 2010

Figures for Regular Forces are rounded to the nearest 10; figures for Reserve Forces are not rounded.

Annex A

Accountability to Parliamentary

A.40 Ministers have accounted to Parliament during the financial year 2010-11 on all aspects of the Ministry of Defence's business. 3684 Parliamentary Questions were tabled, Defence Ministers participated in 15 debates on Defence issues in the House of Commons and four in the House of Lords and responded to eight Adjournment Debates in Westminster Hall. Ministers made two oral statements to the House of Commons and one to the House of Lords. They also made 76 written ministerial statements to the House of Commons and the House of Lords. Details are published in Hansard.

Ministerial Correspondence

A.41 From 1 April 2010 – 31 March 2011, Defence Ministers received 6057 items of correspondence from Members of Parliament and Peers (and some members of the public to which a Ministerial response was deemed appropriate) of which 4307 (71%) were answered within a target of 15 working days.

Evidence to House of Commons Defence Committee (HCDC)

A.42 Since 1 April 2010 the Ministry of Defence has also given evidence to the House of Commons Defence Committee on a number of occasions covering a wide range of issues, and the Government has responded to a number of the Committee's reports. All Committee publications, including published evidence given to the Committee, are available at: <http://www.parliament.uk/business/committees/committees-a-z/commons-select/defence-committee/publications/>

Reports published during this reporting period are listed below.

Table A.1 – Parliamentary Session 2010-11 Reports (Government Responses are listed in brackets after the report they relate to)

Report	Title	Publication Date
First Report HC 345 (HC 638)	The Strategic Defence and Security Review	15 September 2010
HC 451	The Strategic Defence and Security Review	20 January 2011
HC 554	Operations in Afghanistan	23 July 2010
HC 554	The strategic defence and security review and national security strategy	23 July 2010
HC 760	The performance of the MOD 2009-10	3 March 2011
HC 761	The strategic defence and security review and national security strategy	14 March 2011

A.43 The Defence Committee also visited the Armed Forces in the UK and overseas as part of its inquiries, as shown in Table A.3.

Table A.2

Date of Visit	Establishment	Related Inquiry
9 Nov 10	Permanent Joint Headquarters, Northwood	Inquiry into UK operations in Afghanistan
17-21 Jan 11	Afghanistan	Inquiry into UK operations in Afghanistan
9-10 Feb 11	Flag Officer Sea Training (FOST), Plymouth	General visit to see a Thursday War exercise

Evidence to Select Committees of the House of Commons and House of Lords

A.44 Since 1 April 2010 the Ministry of Defence has also given written and oral evidence on various issues to the House of Commons and House of Lords EU Scrutiny Committees to keep both Houses apprised of routine EU business in accordance with Government undertakings. All Committee publications including transcripts and correspondence between Ministers and the Committees are to be found at: http://www.parliament.uk/parliamentary_committees/european_scrutiny.cfm (Commons), http://www.parliament.uk/parliamentary_committees/lords_s_comm_c.cfm (Lords)

Evidence given during this reporting period is listed below:

Table A.3 – Parliamentary Session 2010-11 Reports/evidence

Select Committee	Subject	Publication Date
House of Lords EU Committee – Sub Committee C (Foreign Affairs, Defence and Development Policy)	Somalia Piracy – Operation ATALANTA HL 103	14 April 2010
House of Lords EU Committee – Sub Committee C (Foreign Affairs, Defence and Development Policy)	British-French Defence Relations	11 March 2011

Evidence to Other Select Committees of the House of Commons and House of Lords

A.45 Since 1 April 2010 the Ministry of Defence has also given written and oral evidence on various issues to the following Select Committees of the House of Commons and House of Lords: All Committee publications, including published evidence given to the Committee, are available at: <http://www.parliament.uk/business/committees.cfm>

Evidence given during this reporting period is listed below:

Table A.4 – Parliamentary Session 2010-11 Reports/evidence

Select Committee	Subject	Publication Date
Public Administration Committee	Who does UK National Strategy HC 435	18 October 2010
House of Commons Science and Technology Committee	The UK Space Agency HC 445-w	22 November 2010
House of Commons Environmental Audit Committee	The impact of UK overseas aid on environmental protection and climate change adaptation and mitigation	18 January 2011
Public Administration Select Committee	Good Governance – effective use of IT	16 February 2011
House of Commons Administration Committee	Catering Services in the House of Commons	21 February 2011
House of Commons Transport Committee	Impact on transport of recent adverse weather conditions	22 February 2011
House of Commons Science and Technology Committee	Scientific advice and evidence in emergencies HC 498	2 March 2011
Armed Forces Bill Committee	The Armed Forces Bill HC 779	10 March 2011

A.46 A copy of the Public Accounts Committee Recommendations can be found online at the following link:
[Insert link]

Complaints to Parliamentary Ombudsman

A.47 During the year no investigations have been reported on by the Parliamentary and Health Service Ombudsman, nor has the Department been made aware of any complaints being accepted for investigation.

Annex B

Trading Funds

UK Hydrographic Office (UKHO)

B.1 UKHO's vision is to be the world leader in the supply of digital hydrographic information and services. The products and services supplied to Defence, primarily the Royal Navy, are crucial to the conduct of operations globally. UKHO also plays a central role in support of the Maritime and Coastguard Agency in discharging the UK's treaty obligations under the UN Safety of Life at Sea convention. In addition, UKHO has established a significant commercial business, supplying navigational charts, publications and other services to mariners throughout the world. Commercial business currently represents 91% of the UKHO's total turnover.

B.2 During the year we launched Admiralty e-Navigator. This is an integrated digital catalogue, holdings management and updating service, product viewer and passage planning tool that makes every stage of navigation and fleet management smarter, simpler and safer for the mariner. We will continue to roll out e-Navigator to distributors and vessels during the forthcoming year.

B.3 Our Defence Section has continued to support operations. Of particular note has been the assistance provided by UKHO during the recent evacuation of civilians from Libya (Operation DEFERENCE).

B.4 The UKHO enjoyed a further successful year. All five Key Targets, encompassing Safety, Defence, Finance, Organisational Excellence and Efficiency & Value for Money, were achieved. Turnover increased to £129.5m (compared to £116.6m in 2009-10) and future digital product sales increased by 33% to £9.2m. Net profit grew by 13.1% to £37.9m and the Return on Capital Employed was 32.5%.

Met Office

B.5 The Met Office is a leading weather and climate service. Its aim is to be recognised as the best weather and climate service in the world. During 2010-11, the overall accuracy of Met Office forecasts continued to improve and those issued during the exceptionally cold weather last winter have been widely recognised for providing consistently good advice, both to the public and to emergency responders. In March, the Met Office launched improvements to the National Severe Weather Warning Service that will bring clearer, more targeted warnings based on the likely impacts that severe weather can bring.

B.6 The quality of Met Office science was recognised in a number of external reports. Sir John Lawton concluded that the Met Office Hadley Centre is one of the leading group of modelling institutes world-wide and Sir John Beddington confirmed it represents a critical national capability, with a central role in meeting the Government's requirements for climate evidence and advice¹¹. The Met Office also strengthened its scientific collaboration with academia and launched the *Met Office Academic Partnership* with a number of leading UK universities to advance further the science and skill of weather and climate prediction.

B.7 In collaboration with other public sector bodies, particularly the Environment Agency, the Met Office developed plans for a Natural Hazard Centre to provide a single, authoritative voice for Government with respect to natural hazards including severe weather, flooding, landslides, volcanic activities and geomagnetic storms. In this context, in January, an agreement was signed between the Met Office and the Space Weather Prediction Center of the U.S. National Oceanic and Atmospheric Administration for wide-ranging cooperation and data sharing in the space-weather domain.

B.8 Met Office staff received a number of awards in 2010-11, including a MOD Chief Scientific Adviser's Commendation, recognising the contribution of the team which responded to the eruption of the Eyjafjallajökull volcano, and an Air Officers Commanding Team Commendation for meritorious service, recognising the tireless hard work of the Mobile Meteorological Unit in support of operations in Afghanistan and elsewhere. The Met Office was also recognised for its innovative approach to improving the sustainability and efficiency of its supercomputers through the use of evaporative cooling and DC power.

¹¹ <http://www.bis.gov.uk/go-science/science-in-government/global-issues/climate-change>

B.9 The Met Office delivered a sound financial performance in 2010-11. Turnover increased to £196.1m – compared to £192.0 million in 2009/10 – largely driven by growth in commercial revenue streams from £29.4 million in 2009/10 to £32.2m in 2010/11. Net profit amounted to £9.4m compared to £6.5m for 2009-10 and the Return on Capital Employed was 4.7%.

Defence Science and Technology Laboratory (Dstl)

B.10 Dstl's purpose is to maximise the impact of Science and Technology (S&T) for the defence and security of the UK. As the Government's in-house defence S&T organisation, we work with industry, academia and international partners to deliver advances in military capability, support government decision-making and ensure against current and future threats and risks. We also work with Other Government Departments, exploiting our expertise and knowledge to improve the safety and security of UK citizens, and with international partners to support wider diplomatic aims.

B.11 The new Defence S&T Programme Office, based at Dstl, is responsible for drawing on a wide supplier base to address MOD customers' most pressing priorities. This includes placing and managing work with industry and academia.

B.12 Defence research continues to focus on key areas, including countering improvised explosive devices, armour protection and combat casualty care – which aims to enhance the treatment of casualties on the battlefield. At the heart of Dstl's current programme of work is its support to operations in Afghanistan. We now have 19 established staff posts in Afghanistan and one in Bahrain. In total, we have directly supported more than fifty Urgent Operational Requirements. Dstl continues to work closely with colleagues in MOD's Defence Equipment and Support (DE&S) organisation. This year, for example, Dstl staff have helped to pioneer generic vehicle architecture – a way of managing vehicle design that could generate cost savings of up to 20-25% over the life of a vehicle platform. In 2010-11, Dstl analysts provided critical technical advice to the Strategic Defence and Security Review. Dstl helped Ministers to understand the impact of different policy options and force structures on defence costs.

B.13 Dstl continues to meet all of its financial targets. Turnover for the year was £563.6m (compared to £435.3m in 2009-10). The increase in turnover reflects the inclusion of the MOD's research programme into Dstl's accounts from April 2010, although this has had no effect on the profit. Efficiencies and cost controls have enabled a net profit of £40.3m, which has been achieved while reducing charge-out rates in real terms. This year, Dstl provided a Return on Capital Employed of 14.6% and controlled non-staff costs to approximately 28% of income.

Defence Support Group (DSG)

B.14 The DSG delivers expert in-house equipment maintenance, repair, overhaul (MRO) and upgrade services to the UK's Armed Forces and aims to excel in supporting Defence.

B.15 The dominating factor throughout this trading year has been DSG's increased level of activity supporting Front Line operations in Afghanistan. A significant highlight was the Defence Secretary's opening of DSG's Regeneration Capability facility in Camp Bastion in January 2011 which is being provided under the banner of PJHQ's Equipment Sustainability System.

B.16 DSG has also worked hard over the last year to expand its portfolio of services in support of the MOD. It is in the process of taking over management responsibility for the MOD's Joint Support Chain Services (JSCS) vehicle storage business at Ashchurch, Catterick, Longmoor and Warminster, with full ownership of the activity and the associated JSCS staff being the longer term goal. This will deliver additional revenue for DSG and significantly improve equipment availability to the MOD customer and the Front Line Commands.

B.17 The major challenge now facing DSG going forward is restructuring the business to realign its capacity and capability with MOD customers' reducing requirement for traditional equipment MRO. This is planned to be achieved primarily through voluntary staff reductions across DSG's functional and corporate areas by 2013, as the Minister for Defence Equipment, Support and Technology announced to Parliament on 28 October 2010.

B.18 A further key challenge facing DSG is preparing for the sale of the business to the private sector by no later than 2014-15, as set out in the Strategic Defence and Security Review White Paper published in October 2010, whilst continuing to maintain in parallel its critical support to MOD and the Armed Forces.

B.19 In summary, DSG's trading performance during the year was solid. It once again met or exceeded all of its Key Targets, with improved turnover against plan of £209m and reducing costs across the corporate and business areas of £202m contributing to a net profit of £6.9m. The Return on Capital Employed was 8.0%.

Annex C

Government Standards

Fraud

C.1 The MOD has a zero tolerance policy which was simplified, updated and reissued in August 2010, along with a clear process on how to report suspicions of fraud, theft, bribery and corruption. The department has set up a Defence Crime Board, chaired by the Director General Finance, to bring together the various investigation agencies – MOD Police, Defence Fraud Analysis Unit, and Service Police Authorities – to take a strategic approach and to direct its working group to tackle specific issues. We are now focussing more on prevention and deterrence, as well as targeted detection with data mining activities, while still investigating all reported suspicions. The department has appointed a Counter Fraud Champion to take forward work as directed by the Counter Fraud Taskforce which meets under the chair of Francis Maude, Cabinet Office Minister.

Freedom of Information

C.2 In 2010-11, the MOD received 3,135¹ requests for information under the Freedom of Information Act 2000. The MOD's record on timeliness in respect to its responses to Freedom of Information requests has improved over the previous year. 65% of requests were answered within the 20 working day statutory time limit, and 60% of 'resolvable' requests were answered in full. MOD refused only 13% of requests in full, on the grounds that information was exempt from disclosure under the provisions of the FOI Act 2000.

C.3 We keep our internal operating procedures under regular review. Formal training, seminars and workshops establish and maintain the necessary levels of expertise in business units. In-house guidance is regularly updated to reflect the evolving views of the Information Commissioner, the Information Tribunal, and policy developments issued by the Ministry of Justice.

C.4 Notwithstanding this improved performance, the department was one of a number of public authorities that was monitored by the Information Commissioner's Office (ICO) and we have entered into an Undertaking with the ICO aimed at further improving our performance and reducing the backlog of requests that have still to be answered.

Table C1 – Requests for information under the Freedom of Information Act in Financial Year 2010-11 (All data is published on the Ministry of Justice website)

Category	MOD performance	Total for Central Government Departments
Number of requests received ¹	3,135	28,220
Of these:		
% of requests responded to within 20 working days	65%	84%
% of requests answered 'in time' ²	71%	89%
Total of 'resolvable requests' ³	2,691	21,284
Of these:		
% of resolvable requests answered in full	60%	57%
% of resolvable request refused in full	13%	12%
% of resolvable requests refused in part	6%	23%
% resolvable requests yet to receive a response at the time these statistics were collected	21%	8%

Notes:

1. This includes requests received by MOD Executive Agencies and Trading Funds

2. In time means those receiving a substantive response within 20 working days, plus those where an extension to the timescale for response has been applied during the initial 20-working day period, under the terms of section 10 of the FOI Act 2000

3. Resolvable requests are those to which a substantive response can be given, and excludes lapsed or on-hold requests, or those where the information is not held or where clarification was required.

C.5 The Transparency Framework forms part of the Government's drive to open up access to publicly held information, promoting transparency and enabling wider economic and social gain. As part of the Transparency agenda, the MOD has met, or is working towards meeting, the publishing commitments made by the Prime Minister in May 2010 and regularly publishes business data on the department's website and signposts it on www.data.gov.uk.

Corporate Memory – The national Archives

C.6 In 2010-11, the routine review and transfer of records to The National Archives (TNA) resulted in around 5,400 files being reviewed. Almost all of these were related to the 1982 Falklands Crisis and are not due to be made publicly available at TNA until January 2013, although about 80 files have been released for general access. In addition, MOD has continued to support TNA in dealing with FOI requests for files that are held by TNA but not available to the public.

Commercial sponsorship within MOD during 2010-2011

C.7 The sponsorship return satisfies the Cabinet Office requirement to publish details of commercial sponsorship deals with a value of £5,000 or greater, excluding VAT, where they supplement Government funding of Departmental core business.

Table C2

Activity	TLB	Individual Sponsors	Company Contribution £ EX VAT
HMS Albion	Naval Command	Land Rover UK	16,464
HMS Bulwark		Land Rover UK	16,464
HMS Ocean		Land Rover UK	7,932
Royal Navy Presentation Team		Jaguar Cars Ltd	6,443
RNAS Culdrose Air Day 2010		The Gosling Foundation/ Lockheed Martin Ltd/ Rolls Royce Ltd/ Westland Helicopters Ltd	53,000
RNAS Yeovilton		Jaguar Cars Ltd	11,400
2010 Chinook Display Team	Land Command	Boeing	10,000
Corps Recruiting Team		Volkswagen (UK)	13,300
D Inf Parachute Display Team – The Red Devils		Gencon	1,000
		Seat Sport UK	35,000
		UK Victorinox	4,000
		Chemring	20,000
		Signbox Ltd	3,500
		Suunto	4,000
Exercise Cambrian Patrol		Jaguar Land Rover UK	5,089
Silver Stars Parachute Display Team		Surefire Group	16,500
Royal Signals Motorcycle Display Team		L F Harris International	10,000
Tigers Parachute Display Team		Army Benevolent Fund	10,000
REME Recruiting Team		Volkswagen UK	13,300

Table C2

Activity	TLB	Individual Sponsors	Company Contribution £ EX VAT
RAF Aerobatic Display Team – The Red Arrows	Air Command	Breitling	24,000
		BAE Systems	40,000
		Leeds Commercial	3,540
		Aquila ATMS	13,500
		BMB Mensware Ltd/Barbour/Ping/Oakley/m2c2	15,000
		Pitscards/Kodac/Grant International/Rolls Royce/XS Creativity	16,500
		Landrover	17,309
Battle of Britain Memorial Flight			BAe Systems Ltd
		Rolls Royce	10,000
		Land Rover	5,759
		Jetbrokers	10,140
		Pullman Wincanton	3,531
Typhoon Display Team		Selex Galileo Ltd	21,000
Elementary Flying Training School (EFTS) and Tutor Display Team		Land Rover	12,108
RAF Falcons Parachute Display Team		Peli Products (UK) Ltd	25,000
		Kia Motors (UK) Ltd	10,164
RAF Presentation Team		Jaguar	8,046
		Bose	2,000
Support to the Defence Medical School Training Group	Central	In Training NTP Limited	6,000
Total			£520,989

Better Regulation

C.8 Reducing regulation is a central theme for the Coalition in creating the right conditions for businesses to grow, innovate and diversify. The better regulation strategy has five key principles, which state that any regulation should be: transparent, accountable, proportionate, consistent, and targeted – only at cases where action is needed.

C.9 To avoid increases in the burden of bureaucracy on business, the one-in, one-out system was introduced by the Better Regulation Executive (part of BIS) from Autumn 2010. This requires each Department to assess the net cost to business of complying with any proposed regulation and to find a deregulatory measure which relieves business of the same net cost.

C.10 It has been agreed with BIS that the one-in, one-out rule does not apply to MOD regulations because they do not impact on business. The main exception is the one set of regulations being prepared to implement the EU Directive on Defence Security Procurement, which is the first EU Directive on this issue.

C.11 However, the Armed Forces and Reserve Forces (Compensation Scheme) Order 2011 is an example of the MOD making a new consolidating order and revoking eight earlier Orders.

Alternatives to Regulation

C.12 The MOD has recently introduced the Armed Forces Bereavement Scholarship Scheme, in response to a coalition commitment to pay university scholarships to the children of personnel who die due to service. This was implemented through administrative action by publication of Defence Internal Notice (DIN), instead of regulation.

