HM TREASURY

Whole of Government Accounts

Unaudited Summary Report for the year ended 31 March 2010

Cm 8127

July 2011

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Unaudited Summary Report for the year ended 31 March 2010

Presented to Parliament by
the Chancellor of the Exchequer by Command of
Her Majesty

July 2011

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Introduction

1.1 Whole of Government Accounts (WGA) is a consolidated set of financial statements for the UK public sector. The aim of WGA is to enable Parliament and the public to better understand and scrutinise how taxpayers' money is spent. The publication today of summarised figures from the 2009-10 WGA is a key step in increasing the transparency and accessibility of the public finances.

1.2 WGA consolidates the audited accounts of more than a thousand organisations across the public sector, in order to produce a comprehensive, accounts-based picture of the fiscal position in any one year. It offers new insights into the long-term sustainability of the public finances.

1.3 WGA is based on International Financial Reporting Standards (IFRS), the system of accounts used internationally by the private sector. It complements the National Accounts figures, produced by the Office for National Statistics (ONS), by providing a set of financial statements based on standards familiar to the commercial sector and the wider accountancy profession.

1.4 This document is an important milestone towards the production of WGA. It reports key figures from the main 2009-10 financial statements, with summarised explanatory notes. It does not present a full and final audited account. The external audit by the Comptroller and Auditor General (C&AG) is ongoing, and the final audit opinion will be published later in the year, together with the first audited WGA for 2009-10.

1.5 Today, the Office for Budget Responsibility will publish its *Fiscal sustainability report*, setting out its assessment of the long-term fiscal position. The publication of summary WGA figures in advance of the final audit opinion provides the OBR with the best available data for its report, reflecting the new insights into fiscal sustainability that WGA offers.

1.6 WGA brings together, for the first time, financial information from central government, local government, the NHS and public corporations. As a result, it makes public a number of metrics which it has previously been difficult or impossible to calculate. In particular, the account includes:

- a consolidated Statement of Revenue and Expenditure;
- a consolidated Statement of Financial Position, showing public sector assets and liabilities;
- financial sector interventions, including equity investments in the public sector banks;
- the net public service pensions liability;
- the Government's commitments under Private Finance Initiative (PFI) contracts;
- total provisions; and
- contingent liabilities.

1.7 As this is the first year in which WGA will be published, there is no historical data for comparison. Over time, annual publications of WGA will allow the user to build up a clear and consistent picture of trends and changes in the Government's fiscal position. WGA is the most ambitious financial consolidation of public sector accounts carried out so far. In time, WGA will allow for international comparisons of fiscal balance sheets to be made, provided that other countries' accounts are produced on a comparable basis.

1.8 The following commentary brings together key figures from the summary accounts, explains elements of the main financial statements with particular relevance to the *Fiscal sustainability report*, and provides a reconciliation with National Accounts figures. Finally, it sets out the next steps for the WGA initiative. The commentary is then followed by explanatory notes to the accounts.

Summarised Statement of Revenue and Expenditure

Prepared on an unaudited consolidated basis

For the year ended 31 March 2010

UNAUDITED	Note	£bn
Revenue		
Taxation revenue	3	(488.4)
Other revenue		(97.1)
Total operating revenue		(585.5)
Expenditure		
Social benefit payments	4	195.6
Staff costs	5	180.4
Other expenditure		292.7
Total operating expenditure		668.7
Net financing cost and gains and losses on assets		80.9
Net deficit for the year	2	164.1

Summarised Statement of Financial Position

Prepared on an unaudited consolidated basis

As at 31 March 2010

UNAUDITED	Note	£bn
Assets		
Property, plant and equipment	6	708.0
Equity investment in public sector banks	7	65.3
Other assets		432.0
Total assets		1,205.3
Liabilities		
Net public service pension liability	8	(1,133.3)
Gilt edged securities	9	(803.8)
Provisions	10	(105.0)
Other liabilities		(379.4)
Total liabilities		(2,421.5)
Net liabilities		(1,216.2)
Financed by future revenues:		
General reserves		1,421.4
Revaluation reserve		(205.2)
Liabilities to be funded by future revenues		1,216.2

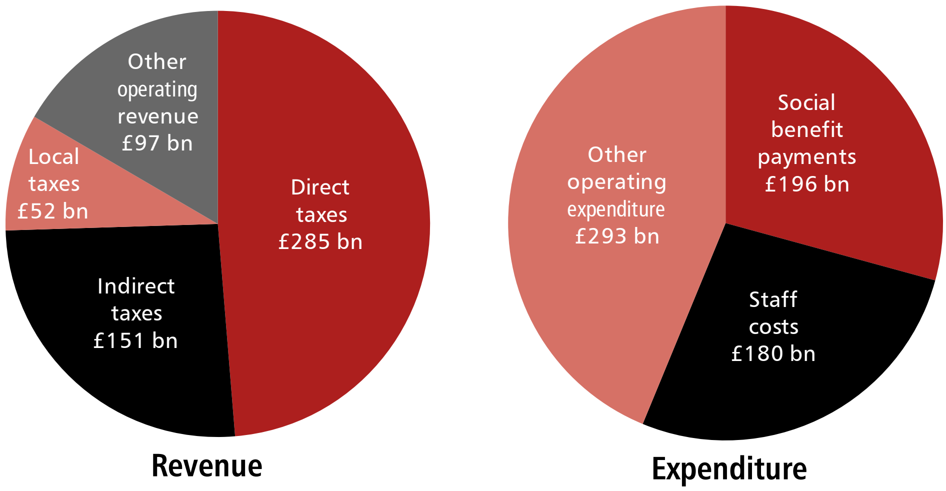
Commentary

Key figures

1.9 The summarised Statement of Revenue and Expenditure above sets out the scale and nature of the flows to and from the Government. It shows that in 2009-10, on an unaudited consolidated basis, the public sector:

- received £585.5 billion in taxation and other operating revenue, including income of £285.2 billion from direct taxation, £151.0 billion from indirect taxation, and £52.2 billion in local taxation;
- spent £688.7 billion, including £195.6 billion on social benefit payments, and £180.4 billion employing staff. The largest elements of social benefit were the state pension at £69.5 billion, and tax credits at £38.7 billion. Staff costs included £147.0 billion in wages and salaries;
- incurred £80.9 billion on financing the deficit, debt accrued in previous years, interest on the pension liability, and gains and losses on assets; and therefore
- faced a total net deficit on an IFRS basis of £164.1 billion (11.7 per cent of GDP).

Chart 1.1: Composition of revenue and expenditure on an unaudited consolidated basis

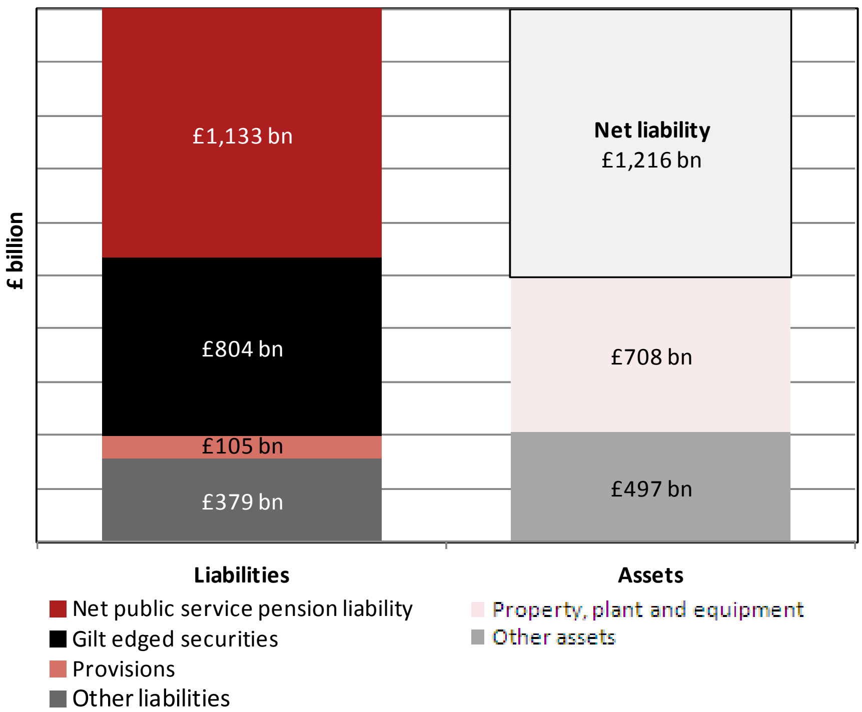


1.10 The summarised Statement of Financial Position sets out the assets held and liabilities owed by the Government, in a snapshot of the public sector balance sheet as at 31 March 2010. On an unaudited consolidated basis, it shows that at 31 March 2010 the public sector:

- held assets valued at £1.2 trillion, including:
  - £708.0 billion of property, plant and equipment, including buildings, infrastructure, equipment, hardware and software, PFI assets, plant and machinery, transport assets, and a range of other assets;
  - £65.3 billion of equity investments in public sector banks; and
  - £432.0 billion of other assets, including £80.6 billion of accrued tax revenue, £57.5 billion of loans and advances by HM Treasury to financial institutions, £51.1 billion of other monies owed to the Government, £27.9 billion of student loans, £25.8 billion of tax receivables before provisions, and other assets such as intangible fixed assets, investment property, loans, prepayments, accrued income, deposits, cash, and inventories.
- had total liabilities of £2.4 trillion, including:

- a £1.1 trillion liability for public service pensions (see paragraphs 1.15-1.22 below);
  - £803.8 billion of debt in the form of government gilts;
  - £105.0 billion of provisions; and
  - £379.4 billion of other liabilities such as borrowings including Treasury bills, and trade and other payables.
- the public sector therefore faced a total net liability of £1.2 trillion on an IFRS basis, or 84.5 per cent of GDP[1].

Chart 1.2: Summary of assets and liabilities on an unaudited consolidated basis



Economic and fiscal context

1.11 The financial position of the Government in 2009-10 reflects the performance of the economy in that year, the structural levels of receipts and expenditure, the financial position in previous years, and Government policy decisions. The year was dominated by the financial crisis and recession, with the economy 5.5 per cent smaller than pre-crisis levels. The public sector fiscal deficit was at a post-war peak. Tax receipts are closely linked to the performance of the economy, and therefore reflected reduced employment, earnings and profits. Public spending reflected the impact of the recession on cyclical areas of expenditure, such as social security, and the policy decisions of the Government of the day. Claimant count unemployment was 1.58 million, while the unemployment rate was 7.9 per cent. Financing expenditure was driven by the existing debt stock, the quantity of debt issued over the course of the year and the long-term interest rates which applied at the time. The weighted average interest rate on conventional gilts (debt issued by central government) was 3.6 per cent. Total net debt reflected the impact of the 2009-10 issuance of new debt, in addition to the stock of debt at the start of the year.

Financial sector interventions

1.12 In response to the financial crisis, the Government of the day made a number of interventions in the financial sector. These included equity investments in banks which are now classified to the public sector, as well as the creation of the Special Liquidity Fund, the Bank of England Asset Purchase Facility

[1] Nominal GDP centred on 31 March 2010.

Fund and the Asset Protection Scheme. These all hold assets against Government liabilities, and the Government stands behind these schemes and has provided financial guarantees and indemnities. To the extent that these guarantees and indemnities are expected to be drawn upon, amounts have been included in the accounts. Otherwise they are shown as contingent liabilities (see paragraph 1.30 below and Explanatory Note 12). The Government has also provided support to financial institutions in the form of loans and advances.

1.13 UK Financial Investments Limited (UKFI) was established to manage the Government's shareholdings in UK financial institutions acquired through recapitalisation and other financial stability interventions in 2008 and 2009. UKFI is responsible for managing the Government's shares in Royal Bank of Scotland Group Plc, Lloyds Banking Group Plc, Northern Rock Plc, Northern Rock (Asset Management) Plc and Bradford & Bingley Plc (see Explanatory Note 7).

1.14 The financial statements of the public sector banks have not been included in WGA. Their scale would dwarf other aspects of WGA, distorting the accounts and therefore making it difficult to determine trends. Furthermore, there is no intention for the Government to retain the assets and liabilities of public sector banks in the long term and, in due course, they will return to the private sector. However, where the financial interventions have had a direct effect on the public sector balance sheet, such as through the purchase of equity, this is reflected in the accounts.

Net public service pension liability

1.15 The Government operates a range of defined benefit pension schemes for past and present public servants. Schemes may be funded or unfunded and may be administered by central government departments, devolved administrations or other public entities (such as local government entities) or independent trustees. Information on the specific schemes can be found in the annual report of the responsible entities.

1.16 Public service pensions form a significant part of the Government's total liabilities, with a total net liability of £1,133 billion as at 31 March 2010 on an unaudited consolidated basis. The pension liability increased by £331.3 billion in the year ended 31 March 2010, largely reflecting a decrease in the rate at which future payments are discounted to reflect their present value. Much of the information behind this increase has already been made available through publications by the major public service pension schemes. An analysis of the liability is provided in Explanatory Note 8 to the accounts.

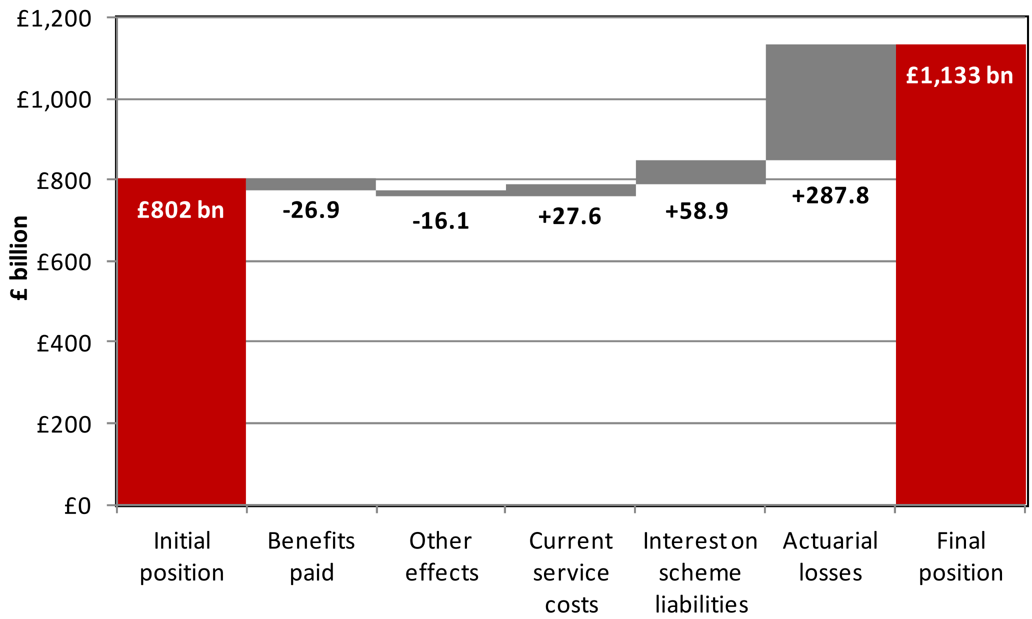
1.17 The scale of the net pension liability is determined by the way public service pension schemes are run, and how accounting standards stipulate it must be recorded. Total pension liabilities reflect the net present value of the total liability owed to current pensioners, deferred pensioners who are no longer in employment but are waiting to receive a pension when they reach retirement age, and current employees who will receive a pension on retirement. The liability allows for salaries projected to retirement or earlier leaving date, but only reflects the number of years of service to date. The liability does not reflect the pension that may be paid to current employees in respect of future years of service to retirement or to future employees. Hence, while the balance of liabilities versus assets does represent the total liability faced by the public sector as calculated under accounting standards, it represents only a partial assessment of how pensions will affect the public finances in the future.

1.18 The major public service schemes, with the exception of the local government scheme, are unfunded. For these unfunded schemes, expenditure on pension payments is met from general taxation. The liability will be paid out over time as employees retire and draw their pension over a number of years.

1.19 There are a number of key assumptions that are used to calculate public service pension liabilities. These include the rate of increase in salaries and pensions inflation as well as the discount rate. As with all long-term economic projections, these assumptions are inherently subject to significant uncertainty. The value of the public service pension liability is very sensitive to changes in these assumptions.

1.20 The chart below shows an analysis of the change in the liability over 2009-10. Actuarial gains and losses are the largest source of movement in the pension liability, with the majority of this change relating to the movement in the discount rate.

Chart 1.3: Change in the public service pension liability in 2009-10 on an unaudited consolidated basis



1.21 The accounting standards require that entities set the discount rate reflecting the yield on high quality corporate bonds. Central government schemes use a centrally set real discount rate determined by HM Treasury, having obtained advice from the Government Actuary's Department. Other entities set their own discount rate, generally after obtaining the advice of an actuary. The centrally set discount rate in excess of the Retail Prices Index (RPI) changed from 3.2 per cent as at 31 March 2009 to 1.8 per cent as at 31 March 2010, reflecting movements in real yields on high quality corporate bonds, which are used as the basis for the discount rate calculation.

1.22 The central government inflation assumption reflects the long-term assumption for the RPI used in Treasury forecasting at that time. As announced in the June 2010 Budget, from 2010-11 the inflation assumption for public service pensions will be based on the Consumer Prices Index (CPI) rather than the RPI. CPI is generally lower than RPI over the long term, which is likely to reduce the value of the pension liability in the individual accounts of WGA entities, for the 2010-11 accounting period onwards.

Provisions

1.23 Provisions represent the best estimate of the liability for an expected future expense, arising from events that have happened in the past. The Government's obligations are reviewed on a regular basis and provisions are updated accordingly. As at 31 March 2010, provisions amounted to £105 billion on an unaudited consolidated basis, as shown in Explanatory Note 10. The most significant provisions are the nuclear decommissioning provision and the provision for clinical negligence.

1.24 The provision of £60.6 billion for nuclear decommissioning includes the cost of dealing with radioactive waste, nuclear fuels and materials, capital facilities, redundant facilities and contaminated materials. The provision and recoverable balances are expressed at current price levels to take account of the time value of money for the very long timescales over which work will be carried out, currently expected to be over 100 years. The ultimate liability will vary as a result of the subsequent information and events, and may result in significant changes to the overall costs of decommissioning.

1.25 The clinical negligence provision of £15.8 billion reflects an actuarially determined assessment of individual incidents that have occurred, where it is more than 50 per cent probable that the claim will be successful and the amount of the claim can be reliably estimated, taking into account likely costs to resolve the claim and historic probability factors. Clinical negligence claims which may succeed, but which are less likely or cannot be reliably estimated, are disclosed as contingent liabilities.

1.26 . The Government also holds a number of other provisions including provisions for European Economic Area medical costs and industrial diseases such as asbestos-related diseases.

Private Finance Initiative

1.27 Private Finance Initiative (PFI) projects are schemes involving the private sector in the delivery of public sector infrastructure. PFI contracts transfer risk to the private sector, including the design, construction, maintenance and operation of the asset. In return, the Government pays an annual charge over the lifetime of the contract, which is typically 25-30 years.

1.28 There are three key elements to the annual charge: the service element to run the project (which could include cleaning, catering, maintenance and security), repayment of the capital asset built and interest on the capital. Explanatory Note 11 shows the Government's commitments to PFI contracts as at 31 March 2010.

1.29 The majority of the 609 PFI contracts reported by entities included in WGA are held by central government (including the NHS) and local government. At 31 March 2010, on an unaudited consolidated basis, the net book value of PFI assets was £30.8 billion, and the associated liability for capital repayments was £29.9 billion. The present value of future obligations was £35.8 billion, which includes some life cycle replacement costs, but does not include future service charges. The interest payable on these existing capital commitments is expected to total £33.2 billion. Over the course of the 2009-10 financial year, 39 PFI projects were signed, with a total capital value of £4.4 billion.

Contingent liabilities

1.30 Contingent liabilities are liabilities associated with events that, while possible, are considered sufficiently improbable (or unquantifiable) that they are not included in the Statement of Financial Position. This report includes those contingent liabilities that are discloseable in accordance with accounting standards, and also goes further to show other commitments even though the likelihood of them occurring is considered remote.

1.31 The majority of the Government's contingent liabilities arise from the guarantees and indemnities provided as part of the financial stability interventions. As detailed in HM Treasury's 2009-10 accounts, they include:

- the Special Liquidity Scheme (£165 billion);
- an agreement to provide contingent capital to the Royal Bank of Scotland (£8 billion);
- an agreement to provide capital to meet regulatory requirements of Northern Rock Plc and Northern Rock (Asset Management) Plc (£1.6 billion);
- financial stability interventions where the likelihood of the liability crystallising is remote, e.g. the Bank of England Asset Purchase Facility (£200 billion), the Asset Protection Scheme (£153.8 billion), the Credit Guarantee Scheme (£125 billion), and guarantees and indemnities in relation to Northern Rock Plc (£23 billion) and Bradford & Bingley Plc (£6.8 billion);
- non-quantifiable contingent liabilities arising from the financial interventions, including indemnities to the directors of UK Financial Investments Limited, Northern Rock Plc, Northern Rock (Asset Management) Plc, Bradford & Bingley Plc, and the Bank of England Asset Purchase Facility Ltd, a guarantee to the Financial Services Authority that it will ensure that Bradford and Bingley will meet its regulatory capital requirements, and the financial consequences should any affected party request the valuers of Northern Rock Plc, Bradford & Bingley Plc and Dunfermline Building Society to reconsider their assessments.

1.32 There are a number of other potentially significant contingent liabilities, details of which can be found in the accounts of the relevant department. These include:

- legal claims, compensation claims and tribunal cases made against a range of WGA entities, for which no reliable estimate of liability could be made;
- commitments made by a number of WGA entities to provide funding for pension liabilities of individual pension schemes, should those schemes require deficits to be funded. This includes

the Financial Assistance Scheme in relation to certain fully funded pensions and other associated benefits in qualifying schemes, as detailed in the 2009-10 accounts of the Department for Work and Pensions;

- indemnities to cover civil nuclear liabilities and claims for damage caused by nuclear matter in the course of carriage, as detailed in the 2009-10 accounts of the Department for Business, Innovation and Skills;
- indemnities and guarantees in respect to rail franchising agreements, and the Network Rail debt issuance programme and standby credit facility, as detailed in the 2009-10 accounts of the Department for Transport;
- the UK's share of European Commission guarantees to EU Member States and Third Countries in respect borrowing and lending operations, guarantees to the European Investment Bank (EIB) in respect of lending to UK Overseas Territories, and callable capital on investments in international financial institutions, including the EIB and regional development banks, as detailed in the 2009-10 accounts of the Consolidated Fund and the Department for International Development;
- the notes in circulation backed by assets that are not represented by Government securities, and the value of UK coins in circulation, as detailed in the 2009-10 accounts of National Loans Fund and the Consolidated Fund;
- reinsurance arising from acts of terrorism, as detailed in the 2009-10 accounts of HM Treasury; and
- guarantees, indemnities and letters of comfort in respect to the Olympic and Paralympic games, as detailed in the 2009-10 accounts of the Department for Culture, Media and Sport and the Olympic Delivery Authority.

Institutional framework

1.33 WGA sits within a broad framework of institutions and publications that contribute toward public understanding and trust in Government accounts and fiscal statistics. In summary:

- the independent Office for National Statistics publishes timely economic and fiscal statistics, consistent with the internationally-agreed National Accounts framework. These figures are the primary indicators used for fiscal policy-making, and for international and historical comparisons;
- each public sector entity publishes audited annual accounts consistent with its agreed accounting framework;
- the National Audit Office, the Audit Commission, audit bodies in the devolved administrations and private sector audit bodies scrutinise and challenge these accounts, and produce an audit report on each;
- WGA consolidates these accounts to produce a consistent snapshot of the public sector financial position in a given year. As well as providing a coherent set of financial statements, this offers insights into the long-term sustainability of the public finances; and
- the Office for Budget Responsibility independently reports on the future sustainability of the public finances through its annual *Fiscal sustainability report*, which, among other sources of information, draws on the aggregates published in WGA.

1.34 As with the National Accounts, WGA does not offer the Government a set of policy prescriptions. Nor is it the primary tool for controlling expenditure and ensuring value for money. Its role is to provide a consolidated view of the Government's finances, with particular added value in the presentation of forward-looking liabilities.

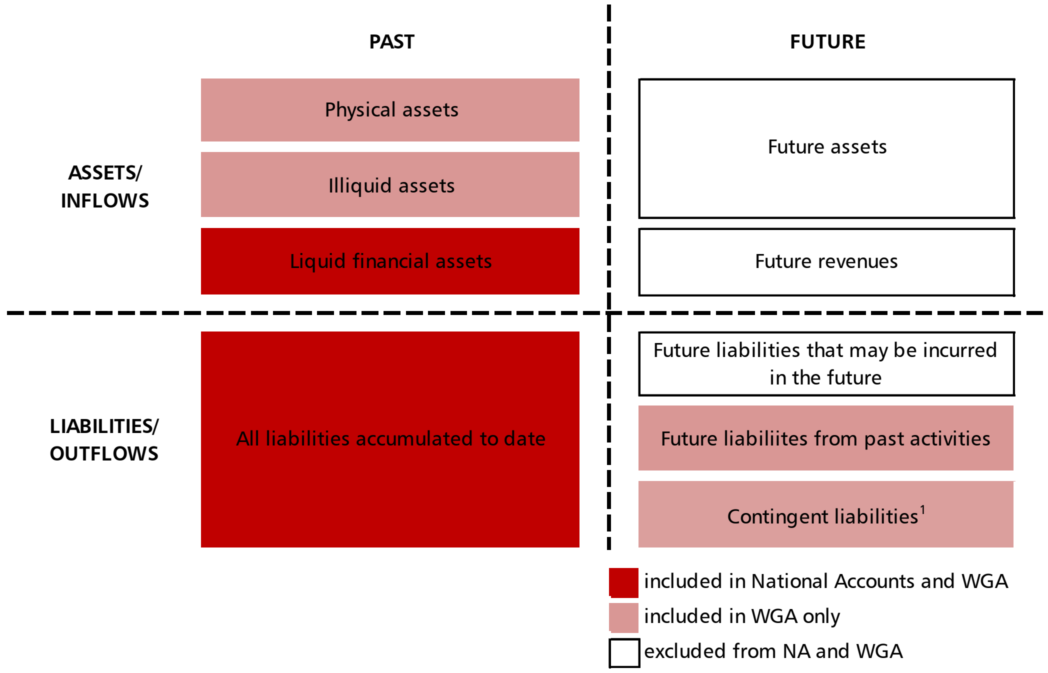
Comparison with National Accounts

1.35 WGA is a complement to, rather than a substitute for, the financial information the Government and other independent bodies already publish. WGA does not replace the statistics published by the independent Office for National Statistics (ONS), which follow the internationally-agreed National Accounts system. The two systems of accounting have evolved independently of each other, use different international standards and have been designed to suit different purposes. While the National Accounts remain the measures used to assess the economic and fiscal position of the UK for policy purposes, WGA provides an accounting standards-based presentation to offer new insights into long-term sustainability, as well as presenting the figures in a format familiar to the commercial sector and the wider accountancy profession.

1.36 The diagram below compares the coverage of IFRS-based WGA measure of net liabilities and the National Accounts measure of net public sector debt. It offers a simple presentation of the differences between what National Accounts and WGA cover, split into the past and the future, and assets and liabilities. The key differences are that WGA measures of net assets and liabilities using IFRS include a full assessment of the Government's assets, including physical and illiquid financial assets, and include liabilities on future payments, such as public service pensions. WGA also discloses contingent liabilities.

1.37 Neither National Accounts nor WGA provide a complete assessment of the future fiscal position of the public sector. Both exclude future tax revenue, future assets, and liabilities that will be incurred in the future, such as future benefit and pension payments. WGA does include future liabilities from past activities and contingent liabilities, and so offers greater coverage of some future liabilities than what is covered in the National Accounts.

Chart 1.4: Coverage of WGA net liabilities and National Accounts measure of public sector net debt



[1] Contingent liabilities are reported in WGA but not included in the Statement of Financial Position

1.38 The ONS has recently published an article *Comparison between Public Sector Finance measures from the National Accounts and Whole of Government Accounts* (June 2011), which explains the main conceptual differences between the National Accounts and WGA. These conceptual differences have a direct impact on the calculation of fiscal aggregates which are sourced from the National Accounts.

1.39 Two key fiscal aggregates published in the National Accounts are public sector net debt and the current deficit. The nearest equivalents in WGA are the total net liabilities and net deficit for the year. The key differences between the 2009-10 WGA and National Accounts[2] measures are explained below.

[2] As per the May 2011 ONS Public Sector Finances release, excluding financial interventions

High level reconciliation of public sector net debt

	£bn
Net liabilities (WGA)	1,216
Net public service pensions liability	(1,133)
Provisions	(105)
PFI contracts	(25)
Unamortised premium or discount on gilts	(16)
Tangible and intangible fixed assets	759
Payables and receivables	40
Investments	16
Other	8
Public sector net debt (National Accounts)	760

Prepared on an unaudited consolidated basis

High level reconciliation of current deficit

	£bn
Net deficit for the year (WGA)	164
Public service pensions	(51)
Impairment of assets	(24)
Capital grants	(16)
Depreciation of assets	(6)
Provisions	27
Military expenditure not capitalised	5
Other	8
Current deficit (National Accounts)	107

Prepared on an unaudited consolidated basis

Differences in relation to pensions

1.40 The main difference between the WGA measures of net liabilities and net deficit and the National Accounts measures of public sector net debt and current deficit relate to public service pensions. WGA is prepared on an accruals basis in accordance with accounting standards. It takes into account all future pension liabilities from the service already provided by past and current public servants. Therefore, WGA net liabilities include the net public service pension liability for public sector pension schemes. The National Accounts only include the cash payments and receipts associated with these pensions. It therefore has no public service pension liability. There are similar differences between WGA net deficit and National Accounts current deficit in relation to interest on pension liabilities of £49 billion which is included in WGA but not National Accounts and in relation to the recording of pension contributions net of pension payments of £2 billion.

Differences in relation to assets

1.41 The other large difference is in relation to non-current assets such as property, plant and equipment, intangible fixed assets, payables and receivables, investments, and other illiquid financial assets. These are included in the WGA measure of net liabilities in accordance with IFRS, but are not included in the National Accounts measure of public sector net debt.

1.42 While fixed assets are not included in public sector net debt, they do form part of National Accounts. However, there are conceptual differences in the valuation of fixed assets and measurement of impairment and depreciation. The National Accounts are constructed using its Perpetual Inventory Method (PIM) to calculate net capital stock and capital consumption (depreciation), whereas WGA recognises fixed assets and depreciation in accordance with accounting standards.

1.43 The WGA measure of net deficit includes depreciation and impairments resulting from an annual review of asset values. The National Accounts measure of current deficit includes impairments and depreciation based on the PIM. This model only takes account of those impairments caused by normal obsolescence or accidental damage, whereas WGA includes all impairments, no matter what their cause.

Differences in relation to provisions

1.44 WGA measures of net liabilities and net deficit include provisions and movements in provisions to take account of liabilities that will be paid in the future arising from events that have occurred in the past and that create a legal or constructive obligation that can be reliably measured. The National Accounts measures of public sector net debt and current deficit do not record these items, and the National Accounts only recognise expenditure in the accounting period that the cash was paid.

Differences in relation to PFI

1.45 Differences arise in relation to PFI contracts as WGA takes into account PFI contracts that are not included in the National Accounts. The National Accounts recognition of PFI contracts is determined by judgements on the balance of risks and rewards arising from the contract, whereas the WGA recognition of a PFI contract is determined by judgments on the balance of control in accordance with IFRS. These PFI contracts are included within current liabilities, with their associated assets included in property, plant and equipment. If these PFI schemes were included in the National Accounts, the value of the PFI contract would increase public sector net debt.

Differences in relation to capital grants

1.46 Capital grants are treated differently between WGA and the National Accounts. WGA treats capital grants as expenditure as the investment does not create assets directly for public sector bodies. The National Accounts treat capital grants as a capital charge and therefore they do not form part of the current deficit.

Publishing audited 2009-10 Whole of Government Accounts

1.47 HM Treasury recognise that as the numbers contained in these extracts are unaudited there is a risk that they may change as the audit process continues. Any audit points could lead to the amendment of the unaudited numbers, qualification of the numbers, or both. The audit opinion on the 2009-10 accounts is required by statute by 31 October 2011, and WGA is required to be published by 31 December 2011. Audit work will be completed as soon as is practicable to enable the Comptroller and Auditor General to conclude on his audit opinion.

1.48 Producing WGA is a major step forward in transparency, and the most ambitious financial consolidation of the public sector being carried out by any government. Teething problems are inevitable, as there were when accruals based accounting was first introduced into the public sector in 2000. However, over time, these transitional issues will be resolved. While the 2009-10 WGA is at a stage where these transitional issues are outstanding, it will nevertheless make a major contribution to the richness and accessibility of information about the public sector finances. The publication of these summarised accounts on an unaudited basis is a significant milestone in this process.

Explanatory Notes

Note 1. Background

The Whole of Government Accounts has been prepared by HM Treasury in accordance with the 2009-10 Government *Financial Reporting Manual* (FReM). The accounting policies contained in the FReM apply EU-adopted International Financial Reporting Standards (IFRS) as adapted or interpreted for the public sector context.

In preparing these accounts, there have been two material departures from the FReM as set out below.

- WGA has been prepared without consolidating the public sector banks, with the banks included as equity investments. This reflects the fact that their scale would dwarf other aspects of WGA, distorting the accounts and making it difficult to determine trends. It also reflects the Government's intention to return the banks to the private sector in due course; and
- Local government did not fully adopt IFRS in 2009-10, continuing to use the Local Government Statement of Recommended Practice (SORP). It will move fully to IFRS for the 2010-11 Account. While this will harmonise the accounting framework, there will remain a difference in the valuation method of highways infrastructure assets between central and local government until at least 2012-13. As allowed under IFRS, local government values highways at their historic cost. This produces a lower figure than the approach adopted by central government based on current day values.

HM Treasury is required to prepare WGA in accordance with the *Government Resources and Accounts Act* 2000, which allows HM Treasury to decide which entities should be included within WGA. This effectively provides a statutory override to the requirement to adopt the accounting standard on consolidation.

The Comptroller & Auditor General is not required to provide an audit opinion on these summary accounts but must, under statute, provide an audit opinion on the complete 2009-10 Whole of Government Accounts by 31 October 2011, and HM Treasury must publish the audited accounts by 31 December 2011. The 2009-10 accounts will be the first WGA to be prepared for audit. HM Treasury has identified a number of improvements that need to be made to the account and has plans to implement these improvements in future years.

Consolidated entities

WGA consolidates a group of entities that appear to HM Treasury to exercise functions of a public nature, or to be entirely or substantially funded from public money. This group includes central government departments, non-departmental public bodies, government agencies, public corporations, local authorities, the National Health Service, and the devolved administrations.

The banks classified to the public sector have been included as equity investments in these statements, and have not been fully consolidated. A few entities that are not controlled by an executive arm of government are also not consolidated, but these are not material to WGA. In addition, there is a small number of entities that have not been included in WGA at this point because of agreed and pending consolidation decisions. Minor entities, which by virtue of their size are not material to WGA, have not been included in WGA if they meet certain criteria. The full WGA document will include a list of all consolidated entities.

Note 2. Net deficit for the year

Revenue and expenditure are accounted for using the accruals convention. Revenue is recognised in the period in which services are provided, and expenditure is recognised in the period in which it is incurred.

The revenues and expenditures, and assets and liabilities, of WGA entities have been added together line by line. All material balances and transactions between entities included in the consolidation have been eliminated. Where necessary, adjustments have been made to the financial statements of WGA entities to make the accounting policies consistent with the accruals accounting concept.

Note 3. Taxation revenue

	£bn
Income tax	152.6
Social security and National Health Service contributions	90.4
Corporation tax	37.8
Capital gains tax	1.9
Inheritance tax	2.5
Taxation revenue from direct taxes	285.2
Value added tax	77.2
Hydrocarbon oils duty	26.3
Excise duties	27.0
Stamp duties	8.1
Licence fee income	3.0
Lottery income	1.6
Other indirect taxes	7.8
Taxation revenue from indirect taxes	151.0
Council tax	29.4
National non-domestic rates	22.8
Taxation revenue from local taxes	52.2
Total taxation revenue	488.4

Prepared on an unaudited consolidated basis

Income Tax includes an amount of £2.5 billion for the Bank Payroll Tax, which was introduced in the Finance Bill 2010, but does not include tax credits. These are categorised as an expense and included within benefits in Explanatory Note 4.

Other indirect taxes include: petroleum revenue tax, betting and gaming duties, air passenger duty, insurance premium tax, landfill tax, climate change levy, aggregates levy, and regulatory fees. Further information is available on the HM Revenue and Customs website.

Tax revenues are estimated by HM Revenue and Customs using a statistical model. The Comptroller and Auditor General has included in his Audit Certificate on the 2009-10 Trust Statement of Tax Revenues and Expenditure an Emphasis of Matter paragraph noting that there is significant uncertainty in the estimates of accrued tax revenue receivable and accrued tax revenue payable. Further information is set out in the 2009-10 accounts of HM Revenue and Customs.

Note 4. Social benefit payments

	£bn
State Retirement Pension	69.5
Tax credits	38.7
Local government housing and other benefits	27.9
Disability Living Allowance	17.7
Income Support	8.7
State Pension Credit	8.2
Incapacity Benefit	6.1
Jobseeker's Allowance	6.1
Carer's Allowance	1.5
Other benefits	11.2
Total cost of social benefit payments	**195.6**

Prepared on an unaudited consolidated basis

The State Retirement Pension is the pension paid to the public. Pension payments to former public sector employees are shown in Note 8.

The majority of social security payments are paid by the Department for Work and Pensions. The Comptroller and Auditor General qualified his regularity opinion of the Department's 2009-10 accounts in respect of error and fraud in benefit payments. Further information is set out in the Department's 2009-10 accounts.

Tax credits are administered by HM Revenue and Customs and include adjustments to income tax as well as direct benefit payments. The Comptroller and Auditor General qualified his regularity opinion on the 2009-10 Trust Statement of Tax Revenues and Expenditure in respect of error and fraud in tax credits, as the department had no estimate of the total levels of potential fraud in 2009-10. It estimated in 2008-09 that error and fraud resulted in overpayments to which the claimants were not entitled, of between £2.0 billion and £2.3 billion and underpayments of between £0.2 billion and £0.3 billion. Further information is set out in the 2009-10 accounts of HM Revenue and Customs.

Note 5. Staff costs

Staff costs comprise:

	Total £bn
Salaries and Wages	147.0
Social Security Costs	10.5
Staff Pension Costs	13.9
Pension Scheme Costs	28.4
Contract & Agency Staff	4.2
Total Unconsolidated Staff Costs (pre-eliminations)	**204.0**
Less intra-government balances	(23.6)
TOTAL Consolidated Staff Costs	**180.4**

Prepared on an unaudited consolidated basis

This note has been prepared to show the full cost of the public sector workforce before items internal to the public sector, which are disclosed as 'intra-government balances' are removed. Intra-government balances include national insurance contributions which would otherwise form part of tax revenue (see Note 3) and employers' pension contributions (see Note 8).

'Staff Pension Costs' consist mainly of employer contributions to internal and external schemes. 'Pension Scheme Costs' include the public service pension scheme expenses such as current service cost, past service cost, enhancements, gains/losses on settlements and curtailments and expenses for the transfer in of new members.

Note 6. Property, plant and equipment

Property, plant and equipment are valued at current cost or on a modified historical cost basis as a proxy for current cost.

	Net Book value £bn
Dwellings	113.7
Land	23.4
Buildings	216.8
Infrastructure assets	232.9
Military equipment	37.1
Assets under construction	40.6
Other	43.5
Total	708.0

Prepared on an unaudited consolidated basis

Other includes transport assets, plant and machinery, IT hardware, software and equipment, and furniture and fittings. Assets such as heritage assets, donated assets, and PFI assets are included in different asset categories as appropriate.

Note 7. Equity investment in public sector banks

The Government has investments in the Bank of England, Royal Bank of Scotland Group Plc, Lloyds Banking Group Plc, Northern Rock (Asset Management) Plc, Northern Rock Plc and Bradford & Bingley Plc, as shown below. Other than the Bank of England, these investments are managed by UK Financial Investments Limited (UKFI). Further information is available from HM Treasury's 2009-10 Accounts and UKFI's 2009-10 Annual Report and Accounts.

	Equity Investment £bn
Bank of England	4.2
Royal Bank of Scotland Group Plc	42.4
Lloyds Banking Group Plc	17.3
Northern Rock Plc	1.4
Northern Rock (Asset Management) Plc	-
Bradford & Bingley Plc	-
Total	65.3

Prepared on an unaudited consolidated basis

Note 8. Net public service pension liability

Each year a valuation of each pension scheme is performed on an accounting basis. This is performed in line with applicable accounting standards.

8.1 Analysis of Movements in the Liability

	Funded (net) £bn	Unfunded (gross) £bn	Total £bn
Net public service pension liability at 1 April 2009	(66.7)	(735.3)	(802.0)
Current service costs	(4.6)	(23.0)	(27.6)
Past service costs	-	(0.7)	(0.7)
Gains/(losses) on settlements and curtailments	(0.3)	-	(0.3)
Interest on scheme liabilities	(13.9)	(45.0)	(58.9)
Expected rate of return on funded schemes' assets	9.0	-	9.0
Actuarial gains/(losses)	(48.2)	(239.6)	(287.8)
Contributions by employer (Funded Schemes)	8.0	-	8.0
Benefits paid	-	26.8	26.8
Transfers in/(out)	-	0.2	0.2
Net public service pension liability at 31 March 2010	(116.7)	(1,016.6)	(1,133.3)

Prepared on an unaudited consolidated basis

Note that the funded pension scheme liability is shown on a net liability basis and the unfunded pension scheme liability is shown on a gross liability basis. The funded pension schemes will hold a range of assets including gilts as part of their investment portfolio. Gilts held by these pension schemes have not been eliminated.

'Current service costs' are the increase in the present value of the scheme liabilities arising from current members' service in the current period. 'Past service costs' are increases/decreases in the present value of the scheme liabilities related to employee service in prior periods arising in the current period as a result of the introduction, change, or improvement to retirement benefits. 'Interest on scheme liabilities' is the increase during the period in the present value of the scheme liabilities because the benefits are one period closer to settlement and is recognised in the Statement of Revenue and Expenditure. The interest cost is based on the discount rate, including inflation, calculated on the gross liability of the schemes (note that the funded scheme liability balance shown is net).

'Actuarial gains and losses' comprise of the effects of differences between the actuarial assumptions and what has actually occurred and the effects of changes in actuarial assumptions. They are accounted for through reserves as required by the Financial Reporting Manual (FReM). An actuarial loss of £287.8 billion has been recognised, of which £259.1 billion is due to changes in assumptions underlying the value of liabilities. This movement in 2009-10 reflects changes in the real yield of corporate bonds, as noted in paragraph 1.21 of the Commentary.

The 'Contributions by employer (funded pension schemes)' balance reflects the increase in scheme assets due to payments made into the scheme by the employer as a consequence of scheme requirements to fund any deficit of scheme assets compared to the total scheme liability. These contributions therefore exceed the current service costs. 'Benefits paid' on funded schemes do not show as a movement on the net liability as they are also included in the reduction in the scheme assets.

8.2 Analysis of the Liability by Type of Scheme

	£bn	Percentage of Liability
Unfunded schemes (gross)		
Teachers (UK)	(258.2)	23%
NHS (UK)	(329.8)	29%
Civil Service	(163.5)	14%
Armed Forces	(120.7)	11%
Police	(101.7)	9%
Firefighters	(21.1)	2%
Other unfunded	(21.6)	2%
	(1,016.6)	90%
Funded schemes (net)		
Local government	(100.4)	9%
Other funded	(16.3)	1%
	(116.7)	10%
Net public service pension liability	(1,133.3)	100%

Prepared on an unaudited consolidated basis

Note 9. Gilt edged securities

As at 31 March 2010, there were gilts of £803.8 billion of which £39.1 billion is due to be repaid within one year, and £764.7 billion is due to be repaid in excess of a year. This includes gilts held by public service pension schemes. Gilt-edged securities, or gilts, are UK Government sterling denominated listed bonds that are fixed rate or index-linked with the return linked to movements in the Retail Prices Index. As the Government's debt manager, the Debt Management Office sells gilts to the market to ensure sufficient funding is available to meet the Government's financial commitments. Further details on these operations can be found in the 2009-10 Debt and Reserves Management Report.

Note 10. Provisions

A provision is recognised when the following three criteria are met: there is a present obligation (either legal or constructive) as a result of a past event; it is probable that a transfer of economic benefits will be required to settle the obligation; and a reliable estimate can be made of the amount of the obligation. The amount recognised as a provision is the best estimate of the expenditure required to settle the present obligation at the reporting date, discounted where appropriate. The year on year changes to the discount rate are charged through the Statement of Revenue and Expenditure.

	Nuclear decommiss-ioning	Clinical negligence	Other types of provision	Total
	£bn	£bn	£bn	£bn
At 1 April 2009	(59.3)	(14.0)	(59.8)	(133.1)
Provisions arising during the year	(0.7)	(3.7)	(7.3)	(11.7)
Provisions utilised during the year	2.4	0.9	8.6	11.9
Unwinding of discount	(2.7)	-	(0.6)	(3.3)
Provisions not required written back	(0.2)	1.0	30.5	31.3
Transfers in-year	(0.1)	-	-	(0.1)
At 31 March 2010	(60.6)	(15.8)	(28.6)	(105.0)
Expected timing of discounted cash flows:				
Within one year	(2.4)	(2.1)	(11.0)	(15.5)
Between 1 and 5 years	(10.2)	(4.6)	(7.4)	(22.2)
Between 5 and 10 years	(10.2)	(9.1)	(2.9)	(22.2)
Between 10 and 50 years	(23.7)	-	(7.1)	(30.8)
Between 50 and 75 years	(3.2)	-	(0.1)	(3.3)
Thereafter	(10.9)	-	(0.1)	(11.0)
Total Future payments	(60.6)	(15.8)	(28.6)	(105.0)

Prepared on an unaudited consolidated basis

Note that the provision for nuclear decommissioning was subject to an Emphasis of Matter on uncertainties in the provision by the Comptroller & Auditor General. Further information is set out in the 2009-10 accounts of the Nuclear Decommissioning Authority.

Note 11. Commitments under PFI contracts

The net book value of PFI assets included in the Statement of Financial Position was £30.8 billion as at 31 March 2010. The assets were accounted for in a manner consistent with other assets of that type. The PFI liability for the present value of capital amounts payable included in the Statement of Financial Position was £29.9 billion.

Interest on the liability and expenditure on services provided under PFI transactions are recognised in the Statement of Revenue and Expenditure as they accrue. Charges payable under the PFI contract can be apportioned between three elements: an element for services; an element for interest on the liability and an element to repay the initial liability.

Future obligations in relation to those PFI contracts which are recognised on the Statement of Financial Position are shown below. The amount of future obligations includes obligations to pay life cycle replacement costs. It does not include service charges which will be payable in relation to these PFI contracts.

Obligations for future periods arise in the following periods:	£bn
No later than one year	3.3
Later than one year and not later than five years	13.5
Later than five years	52.2
	69.0
Less finance charges allocated to future periods	(33.2)
Present value of future obligations	35.8
Total number of PFI contracts	609

Prepared on an unaudited consolidated basis

The total number of PFI contracts recognised on the Statement of Financial Position and the gross present value obligations by segment is:

	Number of contracts	Value £bn
Central government	243	14.0
NHS trusts	129	20.8
Subtotal of central government	372	34.8
Local authorities	226	33.3
Public corporations	11	0.9
Total	609	69.0

Prepared on an unaudited consolidated basis

Details on PFI contracts are available in the individual accounts of WGA entities. Further detail of PFI projects with central government support is available on the HM Treasury website at www.hm-treasury.gov.uk/ppp_index.htm. The website includes data provided by central government departments at the time of the Budget 2011 in March 2011.

Note 12. Contingent assets and liabilities

A contingent liability is a possible obligation arising from past events whose existence will be confirmed only by uncertain future events or present obligation arising from past events that are not recognised because either an outflow of economic benefit is not probable or the amount of the obligation cannot be reliably measured. A contingent asset is a possible asset whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity. Where the time value of money is material, the contingent liabilities and assets are stated at discounted amounts. Some contingent liabilities are quantifiable but many are not as the quantum of the liability can either not be determined with reasonable certainty or to quantify it would jeopardise their outcome.

Note 12.1 Contingent assets

The Government has quantifiable contingent assets discloseable under IAS 37 of £4.6 billion. The most significant component is a contingent asset in relation to nuclear decommissioning of £3.9 billion, reflecting the Government's estimate of assets held by the Nuclear Liabilities Fund to meet its nuclear decommissioning liabilities.

Note 12.2 Contingent liabilities

Total quantifiable contingent liabilities discloseable under IAS 37, reported by category, are as follows:

	£bn
Financial stability interventions	174.7
Export guarantees and insurance policies	9.0
Clinical negligence	7.5
Taxes subject to challenge	5.5
Supporting international organisations	1.9
Other	8.2
Total quantifiable contingent liabilities	206.8

Prepared on an unaudited consolidated basis

Details of all contingent liabilities are available in the individual accounts of WGA entities.

Government departments also report to Parliament remote contingent liabilities, where the risk of crystallisation is too remote to be disclosable under accounting standards, but as guarantees, indemnities and letters of comfort, they create an exposure to financial risk. The full potential costs of the quantifiable remote contingent liabilities, which are largely guarantees and indemnities in place to support the financial sector, are as follows:

	1 April 2009	Increase/ additions	Liabilities crystallised	Obligation expired	31 March 2010
	£bn	£bn	£bn	£bn	£bn
Guarantees	359.5	34.8	-	(148.3)	**246.0**
Indemnities	637.8	60.3	-	(312.1)	**386.0**
Letters of comfort	4.0	-	-	-	**4.0**
TOTAL	1,001.3	95.1	-	(460.4)	636.0

Prepared on an unaudited consolidated basis

Details of all remote contingent liabilities are available in the accounts of Government departments.

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