Defence Procurement Agency

Annual Report and Accounts 2005/2006

HC 1164

DPA

Equipping the Armed Forces

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EQUIPPING THE ARMED FORCES

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FOREWORD

By the Chief Executive

I am very pleased to report to you that during the year 2005/2006 the Defence Procurement Agency succeeded, for the first time since its formation, in meeting all of the Key Targets set for it by Ministers.

The Agency has also for the first time delivered against the MoD's Public Service Agreement Targets – those set independently by HM Treasury for acquisition.

These are signal successes, not just for the Agency, but for the Department as a whole, because they could only be accomplished through the hard work of a great many people right across the acquisition community in MoD and industry.

They follow the Agency's achievement of five out of its six Key Targets last year – then our best ever performance – and demonstrate that improvements in performance are beginning to take hold.

It is now three years since I launched a 'Stocktake' of the Agency's work, followed by the corporate performance improvement programme 'DPA Forward'.

The successes that have flowed from this work, including the hugely improved partnership across MoD acquisition, will now be taken forward as part of the wide-ranging 'Defence Industrial Strategy' which will be the main driver for performance improvement across MoD through-life procurement in the years ahead.

Under 'Stocktake' and 'DPA Forward' new and rigorous processes have been introduced right across the Agency's project activity, to ensure that estimates of time, cost and performance that form the basis of the Department's major investment decisions are sound and take account of risks.

The Agency's governance and links with industry have been strengthened as part of a process of continuous improvement. Fresh emphasis has been given to the development of our people – so that they are properly and professionally prepared to meet the demands of the higher performance that will be required in the future.

Despite these many successes there is still much more to be done to embed the improved performance detailed in this year's Report and make it the new standard across all project activity. Some older projects, on which decisions were taken before all risks were fully understood, still carry major risks that need strong mitigation at Executive Board level.

During the year the Agency delivered more than £3.3Bn of military equipment to the Armed Forces – well above our target – along with 27 Urgent Operational Requirements (UORs) at an approved value of approximately £80m to meet the needs of Forces deployed on operations.

Key successes included the early delivery of both the Javelin anti-armour missile and Sonar 2087.

Other highlights included the delivery of 12 Typhoon combat aircraft; the launch of the Type 45 destroyer HMS *Daring;* delivery of more than 200 Storm Shadow cruise missiles and the achievement of full operational capability for the Brimstone anti-armour weapon.

All Agency staff can be proud of their performance as part of the wider team that makes up the acquisition community. Continued hard work, adaptability and a readiness to embrace change will be the keys to continued success as we carry through far-reaching changes announced under the 'Defence Industrial Strategy'.

Peter Spencer

Peter Spencer
Chief Executive
27th June 2006

Our Mission:

To equip the Armed Forces

The Defence Vision:

Defending the United Kindom and its interests

Strengthening international peace and stability

Defence Values for Acquisition:

By working together across all the Lines of Development, we will deliver the right equipment and services fit for the purpose required by the customer, at the right time and the right cost. In delivering this vision in acquisition, we all must:

- recognise that **people are the key to our success;** equip them with the right skills, experience and professional qualifications;
- recognise the **best can be the enemy of the very good;** distinguish between must have, desirable, and nice to have if affordable;
- identify **trade-offs between performance, time and cost;** cases for additional resources must offer realistic alternative solutions;
- **never assume additional resources** will be available; cost growth on one project can only mean less for others and for the front line;
- understand that **time matters;** slippage costs – through running on legacy equipment, extended project timescales, and damage to our reputation;
- think **incrementally;** seek out agile solutions with open architecture which permit 'plug and play'; allow space for **innovation** and the application of best practice;
- **quantify risk** and reduce it by placing it where it can be managed most effectively; stopping a project before Main Gate can be a sign of maturity;
- **recognise and respect the contribution made by industry;** seek to share objectives, risks and rewards while recognising that different drivers apply;
- value **openness and transparency;** share future plans and priorities wherever possible to encourage focused investment and avoid wasted effort;
- embed a **through-life culture** in all planning and decision making;
- value **objectivity** based on clear evidence rather than advocacy; ensure that we capture past experience and allow it to shape our future behaviour;
- realise that **success and failure matter;** we will hold people to account for their performance.

Members of the DPA Executive Board, along with Ministers and members of the Defence Management Board will play their part in working together for Defence by speeding up decision-taking, keeping the approval process simple and empowering teams to deliver.

Executive Summary

The accounts which follow cover the period 1 April 2005 to 31 March 2006 and have been prepared in accordance with a Treasury direction, dated 13th January 2006, in accordance with Section 7(2) of the Government Resources and Accounts Act 2000.

History and Background

The Agency was established on 1 April 1999 as an Executive Agency of the Ministry of Defence.

Performance Targets

Key Targets are set out in the Agency’s Corporate Business Plan and are agreed by Ministers. Details of the Agency's performance against these targets are set out on pages *16, 17 and 18.*

Principal Activities

The principal activities of the Agency are:

- providing a full project management function: undertaking studies and assessments of cost, time and risk to inform investment decisions, preparing specifications, placing and managing acquisition contracts, monitoring industry’s deliverables and managing integrated, multi-disciplinary project management teams;
- in conjunction with other Departmental areas with an acquisition role, developing and maintaining acquisition strategies and expertise and advising Ministers on these and related procurement matters;
- maintaining specialist expertise associated with its core functions, for example in the fields of commercial and technical standards, and disseminating guidance on those activities for which the Agency has, by agreement, taken the lead within the Department;
- within the capacity determined by its core tasks, supporting defence exports by assisting the Defence Export Services Organisation and industry on appropriate financial terms;
- improving communication and liaison between MoD, industry and other organisations by means of steadily improving business processes and the establishment of a shared information environment;
- working with suppliers to achieve best overall value for money and, subject to this, helping sustain a strong defence industrial base which can continue to meet the needs of UK defence policy;
- promoting international collaboration in defence procurement and associated activities, wherever such a course is compatible with broad Government policies and value for money aims.

Fixed Assets

The changes in fixed assets during the year are summarised in *notes 8, 9 and 10.*

Research and Development

Research and Development expenditure is incurred on the development of new fighting equipment and the improvement of existing fighting equipment.

The amount spent on Research is generally not capitalised and is shown in Other Operating Costs. *Refer note 5*. However where the conditions of the relevant accounting standard (FRS15) are satisfied and with the agreement of the DPA Finance Director about certainty, pre-Main Gate expenditure may be capitalised. Development Expenditure incurred during the year is included in Intangible Fixed Assets and shown in *note 8*.

Post Balance Sheet Events

On 1 April 2006 the Ministry of Defence transferred responsibility for accounting for fixed assets from the Defence Procurement Agency to other parts of the Ministry of Defence. Where the Agency retains the risks and rewards of ownership of these assets they will continue to be accounted for on the Agency's Balance Sheet in accordance with FRS 5 and SSAP 21. In other cases the costs of the use of these assets will be communicated to the Defence Procurement Agency by the asset owners and charged to the Operating Cost Statement. Consequently, these centrally accounted for assets will not be included on the Agency's Balance Sheet as they will be accounted for as operating leases under SSAP 21. There is no effect on the 2005/2006 accounts as a result of this change, and as a result no adjustments have been made to these financial statements.

Management

Members of the Executive Board during the year were:

Sir Peter Spencer	*Chief Executive*
David Gould	*Deputy Chief Executive*
Dr Iain Watson	*Director Information Superiority*
Major General Andrew Figgures	*Technical Director*
Jonathan Lyle	*Director Air & Weapon Systems*
Rear Admiral Ric Cheadle	*Director Land & Maritime*
Stan Porter	*Commercial & Supplier Relations Director*
David Noble	*Finance Director*
Professor Tom McGuffog	*Non–Executive Director*
Wendy Johnson	*Non–Executive Director*
Dr George Watkins	*Non–Executive Director*

The Chief Executive was appointed through open competition for a term of three years, (May 2003 - April 2006). The fixed term was extended by two years to April 2008. The Chief Executive's appointment and termination is in line with other senior MoD appointments.

Details of remuneration and any other significant interests of the members of the Management Board are given on pages 26 to 29.

Employee Policy

The DPA operates a policy of equal opportunity for all staff and potential recruits, regardless of gender, marital status, ethnic origin, religion, sexual orientation, disability or anything else unconnected with an individual's ability to do their job.

The MoD is part of the Principal Civil Service Pension Scheme (PCSPS) and the Armed Forces Pension Scheme (AFPS). Further details contained in *Note 1.16*

We are also a 'Family Friendly' employer. We have a 'Family Friendly' website on our intranet designed to bring together all relevant information, clarifying the various flexible working patterns, providing information for people with parental or other caring responsibilities, and encouraging networking amongst staff.

The Abbey Wood site has a large workplace nursery with 100 full time equivalent places, providing day care facilities for children aged between 3 months and 5 years, at very attractive rates.

Employee Involvement

The DPA is committed to excellent and regular working relations with the Trades Unions, through both the formal consultation and the Whitley processes, and more informal day-to-day liaison. In addition, the DPA continues to seek to maximise communication channels to employees in order to involve them in the decision-making processes of the Agency. Various methods, including regular in-house newsletters and bulletins, Chief of Defence Procurement's (CDP's) Business Improvement Seminars, cascade management briefings, Trades Union consultation and widespread training programmes are used to achieve this aim. The DPA systematically listens to its staff and conducts an annual staff survey, which contributes to its programme of continuous improvement.

Diversity

We continue to strive towards an environment in which all people are treated fairly and with respect through equality of opportunity, fairness and freedom from harassment, bullying, discrimination and stress, by valuing their differences and facilitating good work/life balance.

Development and Training

We place great importance on the development and training of our staff. We invest significantly in identifying individuals' knowledge and competences and matching them to the needs of the Agency. Training and development plans are used to identify present and future needs, design and promote learning opportunities and align individual and team objectives with Agency targets.

Defence Procurement Management Training (DPMT), the DPA funded centre for acquisition training has built on the success of previous years and provided 22,337 student days training in financial year 2005/2006. This figure comprises 21,587 days of classroom training and 750 days of e-learning. The substantial increase from last year can be attributed to an enhanced programme of off-site delivery of acquisition training; to meet the Departments emerging requirements and to satisfy DPMT's broadening and deepening objectives. A total of 2,492 delegate days of acquisition training were delivered under the wider markets initiative, of which 1,661 were delivered to BAE Systems for the Commercial Foundation Programme.

Development Partners

A key element of our 'DPA Forward' programme has been the establishment of a 'Development Partner' network, comprising senior experts in each of our primary functions, including project management, various technical specialisations, secretariat, commerce and finance. Development Partners have an important role to play in defining the size and shape of their functional areas, both now and in the future and in helping to ensure that the supply of functional skills matches demand. They also serve to provide guidance on career paths and anchors to those in their functional areas; to act as sponsors of Continuous Professional Development (CPD) and to inspire individuals to pursue development opportunities. CDP jointly with the Chief of Defence Logistics (CDL) re-launched the 'Development Partner' initiative across the DPA and the Defence Logistics Organisation in October 2005. This initiative feeds into the MoD HQ led work on implementing the professionalising Government agenda.

Health and Safety

The Agency is committed to full compliance with all legislation in respect of our staff and buildings and equipment delivered to the Armed Forces.

Investors in People

The Agency achieved IIP re-accreditation in July 2004. Our commitment to continue to meet or exceed the IIP standard is a key component of our drive for continuous improvement and a rolling programme of internal reviews will be conducted during 2006. DPA's plans for re-accreditation in 2007 will be influenced by MoD plans to seek Corporate Accreditation.

Payments to suppliers

The Agency aims to ensure that all invoices not in dispute are paid within 30 days or in accordance with contractual terms if otherwise agreed. For the financial year ended 31 March 2006, 99.99% of correctly presented bills were paid within 11 calendar days.

Environmental Policy

The Agency is committed to compliance with both the letter and spirit of the Environmental Protection Act and the Environment Act (which apply to all personnel, service and civilian) and with all other existing environmental legislation. Crown or Defence exemptions from legislation are only invoked when these are essential to operational effectiveness.

Political and Charitable Donations

The DPA does not make political or charitable donations.

Auditors

The Financial Statements for the Agency are audited by the Comptroller and Auditor General under section 7(2) of the Government Resources and Accounts Act 2000. A notional audit fee of £220,000 has been disclosed in respect of the statutory Audit Services. The auditors did not undertake any non-audit services. The Auditor's Certificate and Report on the Financial Statements is set out on *pages 36 & 37.*

Statement on disclosure to Auditors

As far as the Chief Executive is aware there is no relevent audit information of which the entity's auditors are unaware and he has taken all appropriate steps to make himself aware of any relevant audit information and to establish that the entity's auditors are aware of that information.

Overview of the year

Equipment Deliveries

The Agency delivered equipment and services valued at £3.3Bn during the course of the year. Highlights are listed below:

- 12 Typhoon combat aircraft and spares valued at around £900m were delivered to the RAF and 2 Merlin HM Mk1 submarine-hunting helicopters were delivered to the Royal Navy;
- 27 Urgent Operational Requirements were delivered to support the Armed Forces;
- More than 200 of the combat-proven Storm Shadow cruise missiles were delivered, and deliveries of ASRAAM short range air to air missiles for the RAF were completed;
- The Brimstone anti-armour weapon achieved full operational capability after demonstrating its capability in trials with the RAF. Several hundred of the weapons were delivered;
- Seawolf Block 2 naval air defence missiles were delivered to the fleet and, for land air defence, deliveries of High Velocity Missiles, command launcher units and Rapier missiles took place;
- The Javelin medium-range anti-armour missile was accepted into service four months ahead of schedule and missiles and command launcher units were delivered to the Army and Royal Marines;
- The advanced Sonar 2087 submarine hunting system was accepted into service five months ahead of schedule;
- Deliveries of night-vision equipment and SA80 Carbines continued and more than 9,000 Bowman radio units were delivered to the Armed Forces, with a value of £290m. The Combat, Infrastructure Platform BISA - a digital information handling element of Bowman – was accepted into service;
- Modernisation of Warrior and Scimitar armoured vehicles continued with further deliveries of the Battlegroup Thermal Imaging System. Deliveries of Viking protected vehicles to the Royal Marines continued and more than 500 light trucks and modified Land Rovers were accepted by MoD;
- More than 190 wheeled fuel and water tankers were delivered to the Armed Forces;
- The private finance initiative 'C' vehicles project – which covers engineering support equipment - entered service;
- Deliveries of the air mobile Cormorant Joint Rapid Reaction Force command system and the Joint Operational Command System – which links British forces and headquarters worldwide – took place;
- Further deliveries of world-leading surface ship and submarine torpedo defence systems were made;
- Land, sea and air platforms continued to be fitted with the sophisticated Successor Identification Friend or Foe equipment.

Projects obtaining Main Gate Approval

Projects obtaining Main Gate Approval, preparatory to moving from Assessment into the Demonstration and Manufacture Phase:

- A £1Bn programme was announced for the continued safe maintenance of British nuclear warheads for the remainder of their lives;
- A £750m contract was awarded for the upgrading of the Royal Navy's Merlin anti-submarine helicopter force;
- A £700m contract was placed for the Demonstration and Manufacture phase of the Watchkeeper advanced battlefield surveillance system;
- A £600m contract was awarded for a new Private Finance Initiative deal to provide plant and equipment for the Armed Forces;
- A contract valued in excess of £200m was placed for the advanced Falcon battlefield communications network;
- A £194m contract was placed for updated target acquisition and night-vision systems for the Apache attack helicopter;
- A £100m contract was placed for advanced computerised training systems to improve the combat effectiveness of existing major surface warships – and Type 45 destroyers;
- A £30m contract was placed for a first batch of Guided Multiple Launch Rocket Systems which will bring improvements in range and accuracy over existing systems;
- Type 23 Frigates are to receive one of the most advanced small-calibre gun systems in the world under a £15m contract.

Other Highlights

- Publication of the 'Defence Industrial Strategy' (December 2005) which sets the framework for the future development of the MoD's relationship with suppliers for the management of acquisition within the Department

Other significant achievements during the financial year included:

- Announcement of MoD's plan to spend £300m on developing the design of two new aircraft carriers to the point at which manufacturing can begin, expansion of the alliance which will deliver them to MoD and agreement with the French Ministry of Defence to co-operate on the project;
- The award of a series of risk-reduction contracts covering advanced technologies that may be used in Future Rapid Effects System armoured fighting vehicles;
- The first of a new class of powerful Type 45 air defence destroyers, HMS *Daring*, was launched;
- The Royal Fleet Auxiliary landing ship *Mounts Bay* started sea trials and sister ships *Cardigan Bay* and *Lyme Bay* were launched and named;
- MoD announced that the successful Skynet 5 satellite communications programme was to be given a longer service life through the addition of a third satellite;
- A Tornado F3 fighter test-fired an AIM120-C5 AMRAAM medium range air to air missile, which is on order to equip RAF fighters, and an RAF Typhoon successfully test fired an ASRAAM missile;
- A prototype of Terrier – a new combat engineer vehicle under development for the Army – was officially rolled out and trials of new Engineer Tank Systems vehicles, Titan and Trojan, took place;
- Work has started on HMS *Triumph*, the last of four Trafalgar class attack submarines to receive a major capability upgrade with advanced new combat systems.

Executive Board Team Excellence Awards

The performance of individual DPA Integrated Project Teams (IPTs) and Support Groups (SGs) is recognised annually through the Team Excellence Awards. Three IPTs were selected as winners for their achievements in the financial year and eight further IPTs and SGs were selected as runners up.

Joint first: Infantry Guided Weapons

The Infantry Guided Weapons (IGW) team achieved UK Javelin in-service date (ISD) within performance, time and cost parameters four months early. The success was due to the combined efforts of the wider team led by IGW IPT comprising Defence Ordnance Safety Group (DOSG), Defence Science and Technology Laboratory (DSTL), Land Guided Weapons IPT (LGW IPT) and the military user (Land Command and Commander in Chief (Fleet) / Royal Marines) represented by the Infantry Trials and Development Unit (ITDU).

The Army Customer is delighted with the new capability, with UK Javelin scoring 100% hits during the Live Firing Demonstrations in July 2005.

Joint first: Sonar 2087

The team's primary achievement this year has been achieving the ISD early against both the 50% and 90% confidence level milestones. This was completed despite a number of technical setbacks.

Although the IPT is small, the team includes many external contributors whose engagement has been essential to the achievement of ISD.

Third: Brimstone

The Brimstone Certificate of Safety Ordnance Munitions and Explosives (CSOME) was produced ahead of time to support the full operational capability (FOC) of Brimstone on 16 December 2005.

A diverse team of people worked together to provide complex information, manage stakeholder expectations and delivered the output to challenging timescales.

DPA Forward

Background

On taking up his post as Chief of Defence Procurement in May 2003, Sir Peter Spencer commissioned a wide-ranging review of how the DPA was performing. This review, which became know as 'Stocktake', identified that the principles on which 'Smart Acquisition' was founded were correct, and where they had been applied, projects succeeded. However, those principles had not been consistently applied.

The DPA introduced some immediate process and organisation changes arising from the 'Stocktake' in April 2004. We also identified around 150 other tasks to embed 'Smart Acquisition' more firmly into the DPA's culture, and to engage with colleagues in the broader MoD and with our suppliers on some aspects outside DPA's control.

In October 2004 DPA launched a single, overarching programme – 'DPA Forward' – to bring these different elements of work together. The emphasis of 'DPA Forward' is on greater consistency in implementing the principles of 'Smart Acquisition'.

The programme focuses on four key areas – Performance, People, Projects and Partnering. Each covers a series of specific initiatives with the overall aim of enabling the DPA to deliver effective military equipment capability to time and budget.

DPA Forward

The programme is divided into four major workstreams: Performance, People, Projects and Partnering. Each workstream in turn includes a series of more detailed initiatives that will identify and implement specific changes:

Performance – ***We will deliver on our promises.*** The 'DPA Forward' Performance workstream focuses on overseeing and co-ordinating work undertaken within the other three workstreams and ensuring that all activity is linked to improving the performance of the Agency. Specific initiatives within this workstream include:

- The DPA 'Operating Framework' – driving best practice by embedding defence values for acquisition throughout the organisation and by establishing a professional doctrine for how the department conducts it business.

People – ***We will have the right skills to do our job.*** Specific initiatives within the People workstream include:

- Workforce Development – creating an environment of professionalism and maintaining a workforce with a diverse range of knowledge, skills and experience in order to improve Agency performance.
- Workforce Incentivisation – continuing to enhance the way in which the achievements of teams and individuals are rewarded and to identify new ways to motivate and encourage staff to reach their full potential.

Projects – ***We will apply 'Smart Acquisition' principles across all our projects.*** Specific initiatives within this workstream include:

- Trade-offs – improving Agency performance on projects by taking full advantage of the opportunities inherent in trading project Performance, Time and Cost.

- Effective Project Control – ensuring that a 'gold standard' approach is applied to managing projects and a baseline is applied to ensure projects reach an appropriate state of maturity and are based on a sound business proposition before they go forward for approval.

Partnering – ***We will develop a robust understanding of supplier performance***. Specific initiatives within this workstream include:

- Key Supplier Management – embedding the use of KSM data and making it an integral part of IPT's decision-making processes. We are also seeking ways to bring coherence to the relationship between the MoD and its Prime Key Suppliers for mutual measurable benefit, consistent with the aims of the 'Defence Industrial Strategy' (DIS).

Peer Review

A formal office of Government Commerce (OGC) led Peer Review in November 2005 concluded that 'DPA Forward' had delivered significant improvements and that significant progress had, in particular, been made in the areas of DPA/DLO Joint Working, Project Review and Assurance, Key Supplier Management, More Effective Contracting and Performance Management. The review also recommended that more needed to be done in areas such as individual project governance, benefits measurement and programme communications. The programme was restructured in December 2005 to increase focus on these outstanding tasks and reflect the publication of the 'Defence Industrial Strategy'.

While there remains much work to do, we believe that the effects of the programme are beginning to be seen in the levels of performance against our Key Targets. The successful delivery of the programme cannot be achieved by the DPA alone. It requires the support of all stakeholders, including its suppliers. Further major change will be taken forward under the auspices of the 'Defence Industrial Strategy'.

Defence Industrial Strategy

Published in December 2005 the DIS White Paper set out a significant acquisition reform agenda, both across the MoD's supplier-base and internally within the Department, which is now being implemented. The DIS recognises that acquisition is evolving, and that the acquisition environment is becoming more complex and demanding. It aims to provide greater visibility of MoD's forward plans to inform the industry's own planning, explains how MoD will take into account broader industrial issues in taking its acquisition decisions and sets out how the Department, and industry, need to change in order to implement the DIS effectively. This change programme is built around
achieving:

- through-life relationships with industry;
- the delivery of integrated solutions;
- innovation, agility and flexibility;
- consistency in our approach; and,
- professional delivery skills.

In addition a high-level review has been launched to investigate the extent to which MoD's existing processes, structures, and organisations support or impede its ability to deliver lasting and transformational change and how they may need to be adjusted.

These change programmes are being driven by the Acquisition Policy Board, chaired by Minister (Defence Procurement), and will build on the significant progress achieved under initiatives such as 'Smart Acquisition', the Defence Logistics Transformation Programme and 'DPA Forward'. They are underpinned by the Defence Values for Acquisition (DVfA) which was published in October 2005 (see page 4). The DVfA define the behaviours necessary to deliver and maintain improvements in acquisition and work is underway to ensure that these behaviours are reflected in project and programme management and embedded throughout the Department, including in the decision-making and performance assessment processes.

Statement of Achievement Against Key Targets

We measure our achievement against Key Targets, which are the drivers for the achievement of the targets set by the Treasury through the Public Services Agreement. Our Key Targets set a significant challenge for the Agency, focusing upon the performance of all projects with procurement costs valued over £20m.

Key Targets 1, 2 and 3 cover our achievement on the three principal project measures of performance, time and cost. Key Target 1 measures our ability to deliver equipment to the customer at the required technical performance. It compares the number of approved Key Requirements against the number which are forecast to be, or have been, met. Key Targets 2 and 3 measure in-year average programme slippage and cost growth. The projects monitored for these Targets were all projects valued at greater than £20m, which had passed their main investment decision point (Main Gate), but not yet achieved their In-Service Date (ISD) as at 1 April 2005. These are agreed with the National Audit Office (NAO) and the Key Target results are validated by the NAO. Performance against the Key Targets is shown in the table on page 18.

Results

Key Target 1: Equipment Performance

Achieved – The target for achievement of projects' core requirements was 97%. We achieved 97%.

Key Target 2: Programme Slippage

Achieved – To achieve this target, average new slippage had not to exceed 1.0 months during the course of the financial year. Actual average new slippage recorded was 0.7 months, this equates to a total cumulative slippage of 30 months across the project population.

Key Target 3: Cost Growth

Achieved – To achieve the target, average new cost growth had not to exceed 0.6% during the course of the financial year. Actual cost grew by an average of 0.2%.

Key Target 4: Asset Deliveries

Achieved – This Key Target covers the achievement of forecast asset deliveries in-year. The Target required the Agency to deliver greater than 90%, by value, of its forecast Asset Deliveries for the year. This year the Agency delivered 107% of its forecast Asset Deliveries.

Key Target 5: Efficiency

Achieved – In 2004/05 the Agency introduced three measures covering its efficiency. The Key Target requires the Agency to stay within the boundary set by each of the three ratios set out below.

Measure i) Asset Turnover in months. The target level for this measure was set at less than 83 months, actual achievement in year was 72 months.

Measure ii) Assets Delivered per £ of Operating Cost. The target level for this measure was set at greater than £13.20, actual achievement in year was £15.23.

Measure iii) Assets Produced per £ of Operating Cost. The target level for this measure was set at greater than £23.16, actual achievement in year was £23.83.

Other measures

The achievement of a more detailed range of objectives is vital to our customers and other stakeholders. We therefore have targets and measures of performance in our Business Plan, which complement the Key Targets and ensure coverage of key supporting activities.

Key Target (KT)	02/03	03/04	04/05	05/06	06/07	07/08
	Targets, Outturns & Achievements	Targets				
KT1[1]						
Predicted achievement of Key User Requirements	97%	98%	97%	97%	97%	97%
Outturn	*99%*	*99%*	*99%*	*97%*		
PSA Target				97%	97%	97%
Outturn				*97%*		
KT2[1]						
Average in-year variation of forecast In-Service Date not to exceed (months)	0.4	0.5	0.9	1.0	0.9	0.8
Outturn	*7.2*	*2.4*	*0.9*	*0.7*		
PSA Target (DPA Stretch Target)				0.7	0.5	0.4
Outturn				*0.7*		
KT3[1]						
Average in-year variation of forecast cost not to exceed	0.0%	0.0%	0.5%	0.6%	0.5%	0.4%
Outturn	*5.4%*	*2.7%*	*-2.2%*	*0.2%*		
PSA Target (DPA Stretch Target)				0.4%	0.3%	0.2%
Outturn				*0.2%*		
KT4[2]						
Achievement of planned in-year asset deliveries			85%	>90%	93%	95%
Outturn			*100%*	*107%*		
KT5[2]						
Achievement of planned in-year efficiency measures						
Measure i): Asset turnover (Months)[3]			<70	<83	<52	To be
Outturn			*59*	*72*		*determined*
Measure ii): Assets delivered per £ of Operating Cost[3]			>£10.72	>£13.20	>15.44	To be
Outturn			*£14.36*	*£15.23*		*determined*
Measure iii): Assets delivered per £ of Operating Cost[3]			>£16.23	>£23.16	>18.01	To be
Outturn			*£19.13*	*£23.83*		*determined*

Notes:

1. Prior to April 2004 the Agency calculated results of Key Targets 1 to 3 against the 20 largest projects for which the major investment decision had been made ("Main Gate"). Key Target 2 and 3 variation compared 50% confidence forecasts against the 90% confidence forecast at Main Gate. From 1 April 2004 the Agency expanded the population of projects covered by Key Targets 1 to 3 to include all projects valued at over £20M ("Category A-C") for which the major investment decision had been made ("Main Gate") and which were not yet in service at the start of the financial year. Furthermore the calculation of Key Target 2 and 3 now compares the 50% confidence forecast against the 50% confidence forecast at the 1 April of the financial year.

2. Key Targets 4 and 5 were introduced in 2004/05.

3. Targets for Key Target 5 Measures i), ii) and iii) are set at the outset of the corresponding financial year.

Operating cost includes staff costs and certain other costs as agreed when the targets were set.

Report by the Comptroller and Auditor General on the Defence Procurement Agency's Statement of Performance Against 2005/2006 Key Performance Targets

The Chief Executive of the Defence Procurement Agency has asked me to validate performance against the 2005/2006 Key Targets.

Respective responsibility of the Defence Procurement Agency, the Chief Executive and the Auditor

The Defence Procurement Agency and Chief Executive are responsible for the measurement and reporting of the Agency's performance against the Key Targets.

I examine and conclude on whether the Agency has:

- Provided full details of performance against all the Defence Procurement Agency's Key Targets;
- Ensured that all performance information is reliable and fairly presented.

Basis of conclusion

The validation includes an examination, on a test basis, of evidence relevant to the amounts and disclosures of the outturns and achievements included within the Statement. It also includes an assessment of the significant judgements and methodologies made by the Defence Procurement Agency and Chief Executive in the Statement's preparation.

Conclusion

The Statement of Performance above includes all the Defence Procurement Agency's 2005/2006 Key Targets and it reliably and fairly presents the Agency's performance against Key Targets 1 to 5. I have no observations to make on this statement.

John Bourn
Comptroller and Auditor General
National Audit Office
157-197 Buckingham Palace Road
Victoria
London SW1W 9SP
29th June 2006

Financial Summary

Financial management information is utilised throughout the Agency and is key to producing our outputs and targets. The ‘DPA Forward’ initiative has reinforced the importance of financial scrutiny and assurance and we are using the financial systems to assist with providing these essential levels of confidence.

Improved processes and procedures continue to be developed jointly with the DLO and we have implemented the Department’s new planning, budgeting and financial systems during 2005/2006 to further complement the recently introduced accounting ORACLE software and replace existing applications. DPA together with the DLO are at the forefront of trialling and introducing these new systems which continue to progress the finance vision of integrated project management.

During the year progress has been made in embedding financial disciplines and awareness throughout the Agency concentrating particularly on the non-finance community – project team leaders and project and commercial managers. This will continue to be a key priority. Over 200 people have attended the ‘Resource Management for Resource Managers’ courses and more than 100 have undertaken a course on ‘Decision-Making in a Resource Environment’. In addition regular finance coaching and update sessions are provided.

The IPT Financial Controller is key to delivering high quality and consistent financial information, engaging with contractors and supporting the corporate financial aims of the Agency. We are continuing with plans to strengthen the finance function to ensure we have people with the right skills to fill these demanding roles. This is being done through external recruitment as well as internal development.

In addition to the MoD accountancy trainee scheme, DPA have externally recruited trainee accountants who are currently undertaking a concentrated and comprehensive managed training programme. A graduate trainee accountant scheme will be introduced in 2006.

Transfer of Nuclear Liabilities to the Nuclear Decommissioning Authority (NDA)

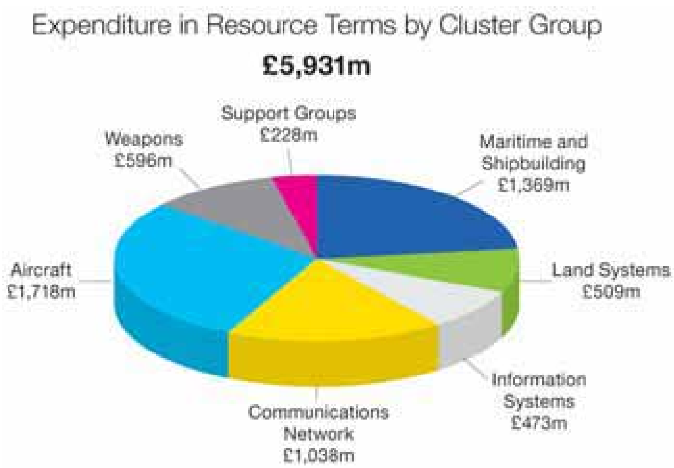
On 1 April 2005 the Nuclear Decommissioning Authority (NDA) took over the responsibility for the managing and cleaning of civil nuclear sites. As a result the MoD liabilities at 1 April 2005 relating to civil nuclear sites and the associated value of provisions and funding for decommissioning costs were transferred to the NDA.

The Agency Accounts 2004/2005 closing balances have been restated to reflect the DPA transfer value of £4.3Bn. *(Refer note 27).*

The Agency's Programme

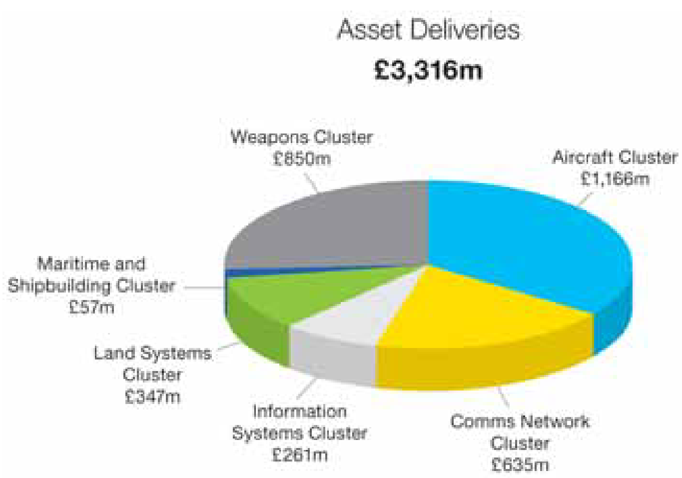
The Agency's programme has two parts:

- Equipment Procurement – purchase of new equipment systems and associated weapons, including some major upgrade programmes and system procurement expenses such as studies. Total expenditure for 2005/2006 was £5,931m. (2004/2005: £5,385m).
- Agency Operating costs and Nuclear Programmes – Expenditure in 2005/2006 was contained within the planned levels reported to Parliament through the Supply Estimates and within allocations set by the Department.



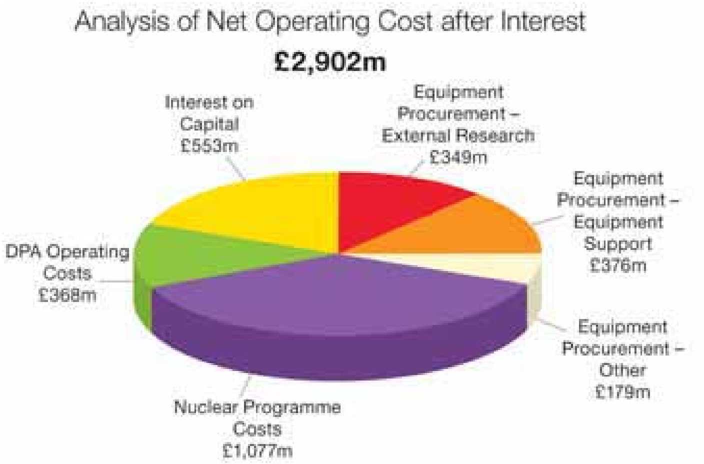
Asset Deliveries 2005/2006

Equipment delivered to Armed Forces customers amounted to £3,316m for the 2005/2006 financial year as shown below.



Operating Costs and Nuclear Programme

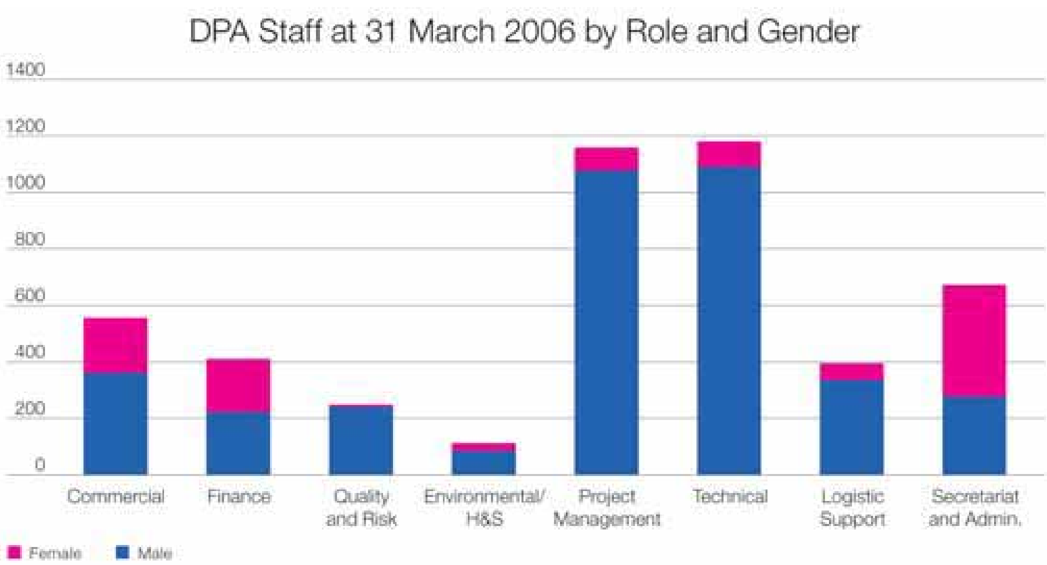
Operating costs of £2,902m in 2005/2006 consisted of £368m to run the Agency including staff costs of £177m (including provisions), £1,077m spent on the Nuclear Programme and £1,457m for Equipment Procurement and interest on capital.



People

As at 31 March 2006 the Agency employed 4,714 people made up of 704 Service Personnel, 3,882 Civilians and 128 Agency staff.

Total number of male:	3,678
Total number of female:	1,036
Total	4,714



Executive Board Members

Executive Board Members

1. Chief of Defence Procurement and Chief Executive

Sir Peter Spencer

Sir Peter served in the Royal Navy from 1965 until he retired in the rank of Vice-Admiral in January 2003. He has held a range of appointments including seven tours in acquisition. He was Director General Surface Ships and Controller of the Navy in the Procurement Executive from 1997, becoming Executive Director on the formation of the DPA on 1 April 1999. In January 2000 he was appointed 2nd Sea Lord and Commander in Chief, Naval Home Command, the appointment from which he retired. He rejoined the DPA as Chief Executive and Chief of Defence Procurement on 1 May 2003.

2. Deputy Chief Executive

David Gould

David Gould joined the Ministry of Defence in 1973. His responsibilities have covered NATO, Nuclear Plans and Operations and Royal Air Force Equipment and Logistics. He served as Under Secretary for Policy, Overseas and Defence Secretariat in the Cabinet Office, returning to the Ministry of Defence in 1995. He became Director General Finance and Business Plans for Defence Logistics in late 1999 and was appointed Deputy Chief Executive of the DPA in July 2000. He has responsibility for the Central Cluster of four Support Groups.

3. Director Land and Maritime

Rear Admiral Ric Cheadle

Ric Cheadle joined the Royal Navy in 1968, spending his early career in nuclear submarines. As a Commodore he was appointed Director of Nuclear Propulsion and in 2000 he became Naval Base Commander (Devonport). In 2002 as a Rear Admiral he served as the Chief-of-Staff to the 2nd Sea Lord prior to taking up his current appointment as Director Land and Maritime in 2003. He is Controller of the Navy, an appointment that carries membership of the Navy and Admiralty Boards and he is also Chair of the Defence Nuclear Safety and Ship Safety Boards.

4. Director Air & Weapon Systems

Jonathan Lyle

Jonathan Lyle is a Chartered Engineer and joined the Ministry of Defence in 1976 working initially as a project manager for Naval Systems. Between 1991 and 1996 he was seconded to the Cabinet Office and the Department of Trade and Industry returning to Defence Procurement in 1996 to manage a range of aircraft projects. He was appointed to his current role as Director Air & Weapon Systems in August 2004.

5. Director Information Superiority

Dr Iain Watson

Iain Watson joined the MoD in 1973 and worked in Anti-Submarine Warfare research. From 1989 he held a number of posts at Director level in Communications and Information Superiority (IS), becoming Director General Command and Information Systems in the Procurement Executive in 1997. Among the more important projects were Bowman, Skynet 4 and 5, ASTOR and Digitisation. He became BOWMAN IPT Leader on formation of the DPA and then spent two years on secondment to Thales Underwater Systems. He returned to the DPA in 2003 and is now Operations Director for Information Superiority.

6. Technical Director

Major General Andrew Figgures

Major General Andrew Figgures was commissioned into the Corps of Royal Electrical and Mechanical Engineers. He has served in a variety of command and staff appointments before establishing himself in the acquisition community, firstly as Director of Operational Requirements (Land), then on promotion to Major General as Capability Manager (Manoeuvre). He assumed his current role as Technical Director in the DPA in 2004. He sits on the DLO Board and is responsible to both CDP and CDL for Technical Assurance across the DPA and DLO. He is also Master General of the Ordnance and sits on the Army Board.

7. Finance Director

David Noble

David Noble joined the Agency on 1 July 2003, having previously held financial positions in Rolls-Royce plc. In April 2004 he was appointed Finance Director and assumed responsibility for the Finance Assurance Group. He is a member of the Chartered Institute of Management Accountants.

8. Commercial and Supplier Relations

Stan Porter

Stan Porter joined the MoD in 1963 and much of his service has been in commercial branches. In 1998 he became Director General Commercial. With the creation of the DPA in April 1999 he became XD5, while retaining his MoD corporate role as DG Commercial. In April 2004 he was appointed Commercial and Supplier Relations Director and assumed responsibility for the Commercial and Supplier Relations Group of five Support Groups. Stan Porter retired from the DPA Executive Board and Civil Service on 31 March 2006.

9. Non-Executive Director

Professor Tom McGuffog

Professor Tom McGuffog provides advice to CDP and the Executive Board, strongly based on what is best practice in commercial businesses. He was Director of Electronic Business with Nestlé UK until he retired. He has held various director roles in industry in Purchasing, Supply Chain, Transport and Distribution and Information Technology.

He is Chairman of UK Partners for Electronic Business and Vice-Chairman of the UK Simpler Trade Procedures Board. He is a visiting Professor at the University of Glasgow. He was appointed a Non-Executive Director on the DPA Executive Board in 1999.

10. Non-Executive Director

Wendy Barnes

Wendy Barnes is a Non-Executive Director in another Government Department and an independent consultant with a breadth of knowledge in customer service, marketing and change management.

She has extensive experience in developing and delivering several large scale change and product launch programmes. She was appointed a Non-Executive Director of the DPA Executive Board on 1 January 2005.

11. Non-Executive Director

Dr George Watkins

Dr George Watkins is a former Chairman and Managing Director of Conoco UK and was responsible for all oil and gas exploration and production activity in the UK, day-to-day operations and the development and implementation of business strategy. He holds several Non-Executive Directorships.

Other appointments have included Vice-President Exploration Production, North America for Conoco Inc and Director, Business Development with Conoco UK. He was appointed a Non-Executive Director of the DPA Executive Board on 1 January 2005.

Peter Spencer

Peter Spencer
Chief Executive
27th June 2006

Remuneration Report

Introduction

The DPA Agency accounts seek to comply with the disclosure practices applicable to companies in the private sector and as set out in the Greenbury code on corporate governance. The level of disclosure sought has recognised the differences between private sector directors and the directors that comprise the DPA Executive Board.

The DPA Executive Board is composed of Senior Civil Servants, senior officers of HM Forces and three Non-Executive Directors. Contracts of service including early termination for Senior Civil Servants and senior officers of HM Forces are in line with other senior MoD positions. There has been no significant award in respect of early termination made to past senior managers.

Unlike private sector directors, civil servants and officers do not determine their remuneration package. There is no Remuneration Committee; however, Senior Civil Service pay is determined by the Senior Salaries Review Board. In particular civil servants do not qualify for the large elements of variable pay which were of particular concern to the Greenbury Committee. Annual bonuses and awards are not linked to the achievements of key targets or any other corporate performance conditions. They are awarded under normal Civil Service conditions.

The Executive Board

Where appointments to the Board were made after the beginning of the financial year (1 April 2005), details are disclosed relating to their period of office only. Similarly, where Board members left before the financial year-end (31 March 2006), only details up to departure are disclosed.

Remuneration of DPA Executive Board during the year

(This section of Report is subject to audit)

The salary and pension entitlements of the most senior members of the DPA were as follows:

	Age 31 March 2006	Salary and benefits in kind for period of DPA appointment 2005–06	2004–05	Real increase in pension at pensionable age	Total accrued pension at 31 March 2006
		£000	£000	£000	£000
Sir Peter Spencer *Chief of Defence Procurement and Chief Executive*	58	135-140	125-130	0-2.5	5-10
David Gould *Deputy Chief Executive*	56	135-140	125-130	*2.5-5 plus 7.5-10 lump sum*	*50-55 plus 155-160 lump sum*
Dr Iain Watson *Director Information Superiority*	58	90-95	85-90	0-2.5 *plus 5-7.5 lump sum*	35-40 *plus 105-110 lump sum*
Maj Gen Andrew Figgures *Technical Director*	55	95-100	80-85	0-2.5 *plus 5-7.5 lump sum*	45-50 *plus 145-150 lump sum*
Jonathan Lyle *Director Air & Weapon Systems*	47	80-85	45-50	2.5-5	35-40
Rear Adm Ric Cheadle *Director Land & Maritime*	56	90-95	85-90	0-2.5 *plus 0-2.5 lump sum*	45-50 *plus 140-145 lump sum*
Stan Porter *Commercial & Supplier Relations Director*	61	110-115	100-105	2.5-5 *plus 10-12.5 lump sum*	50-55 *plus 150-155 lump sum*
David Noble *Finance Director*	50	105-110	100-105	0-2.5	5-10
Prof Tom McGuffog* *Non-Executive Director*	65	30-35*	15-20		
George Watkins* *Non-Executive Director*	62	15-20	0-5		
Wendy Barnes (formerly Johnson)* *Non-Executive Director*	49	20-25**	0-5		

* *This includes payments of £15k relating to fees for 2004/2005*
** *This includes payments of £3k relating to fees for 2004/2005*
* *Professor Tom McGuffog, Dr George Watkins and Wendy Barnes are employed on a fixed term contract renewable by agreement. They are not employed as civil servants and are not members of the Principal Civil Service Scheme (PCSPS).*

Benefits in kind for 2005/06

Benefits in kind were paid to the following Executive Board members:

Sir Peter Spencer	Chief Executive	–	£29.4k
David Gould	Deputy Chief Executive	–	£17.6k

Benefits in kind figures for civilian Board members represent the value obtained from the private use of official cars, and for Service members the value obtained from the use of Official Service Residence. The MoD has an arrangement with the HM Revenue and Customs where MoD pays the tax liability that would ordinarily be paid by the individual. The tax liability is therefore included in the figures disclosed to arrive at the full 'value' of the benefit to the individual.

Significant Interests

David Noble is a deferred pensioner of Rolls-Royce plc as a result of his 16 years service with the company prior to joining the MoD. All other Executive Board members have confirmed in writing that they individually have no company directorships or other significant interests held which may conflict with their management responsibilities.

Pension Benefits

The Executive Board members have Cash Equivalent Transfer Values (CETV), relating to the member's pension benefits accrued at the beginning and end of the reporting year through the Civil Service pension arrangements, as follows:

	CETV 31 Mar 06 or date left DPA Executive Board	CETV at 31 Mar 05 or date of appointment	Real increase in CETV after adjustment for inflation and changes in market investment factors
	£000	£000	£000
Sir Peter Spencer	75	56	33
David Gould	929	851	69
Dr Iain Watson	655	581	58
Maj Gen Andrew Figgures	998	967	50
Jonathan Lyle	399	346	39
Rear Adm Ric Cheadle	931	907	14
Stan Porter*	–	852	–
David Noble	64	40	25
Prof Tom McGuffog	–	–	–
Dr George Watkins	–	–	–
Wendy Barnes (formerly Johnson)	–	–	–

* Stan Porter retired on 31 March 2006: the CETV figures at this date are not available. Figures shown here are the latest available, as at 31 March 2005. Mr Porter retired on normal civil service pension terms, with no enhancement.

'Salary' includes gross salary, performance pay or bonuses, overtime, reserved rights to London weighting or London allowances, recruitment and retention allowances and any other allowance to the extent that it is subject to UK taxation.

'Accrued Pension' benefits are provided through either the (a) Principal Civil Service Pension Scheme for civilian Board members or (b) Armed Forces Pension Scheme for Service Board members.

(a) This is a statutory scheme that provides benefits on a 'final salary' basis at a maximum retirement age of 65. *Refer note 1.16*
(b) This is a statutory scheme that provides benefits on a 'final salary' basis at a normal retirement age of 55. *Refer note 1.16*

'Real Increase in Pension' and 'related lump sum at pensionable age' represents the increase in value of the Total Accrued Pension over the course of the year 2005/06. It is expressed in real terms after adjustment for inflation as illustrated. Accrued Pension at 31/3/06 less Accrued Pension at 31/3/05 adjusted for inflation gives real increase in pension.

Any pension funded by a Board member at their own expense, for example by way of Additional Voluntary Contributions, is excluded from the disclosed remuneration.
The CETV is not paid to the member. It is the amount that would be paid by the Civil Service defined benefit pension arrangements in the event that the member left the pension arrangement and transferred their Accrued Pension benefits to another pension arrangement approved by the HM Revenue and Customs.

The real increase in CETV reflects the increase in CETV effectively funded by the employer. It takes account of the increase in Accrued Pension due to inflation, contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market factors for the start and end of the period.

Peter Spencer
Chief Executive
27th June 2006

Statement of Accounts

Statement of Agency's and Chief Executive's Responsibilities

Under Section 7 of the Government Resources and Accounts Act 2000, the Treasury has directed the DPA to prepare a statement of accounts for the financial year in the form and on the basis set out in the Accounts Direction. The accounts are prepared on an accruals basis and must give a true and fair view of the Agency's state of affairs at the year end, and of its net operating cost, recognised gains and losses and cash flows for the financial year.

In preparing the accounts the Agency is required to:

- observe the Accounts Direction issued by the 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 the Financial Reporting Manual and applicable accounting standards have been followed;
- disclose and explain any material departures in the financial statements;
- prepare the financial statements on the 'going concern basis', unless it is inappropriate to presume that the Agency will continue in operation.

The Permanent Under Secretary of State (PUS), as the MoD's Principal Accounting Officer, has formally tasked the Chief Executive with responsibilities analogous to those of an Accounting Officer for the Agency. The Chief Executive's relevant responsibilities in this role, including his responsibility for the propriety and regularity of the public finances for which he is answerable and for the keeping of proper records, are set out in the Accounting Officer's Memorandum issued by the Treasury and published in 'Government Accounting'.

Statement on Internal Control

1. Scope of responsibility

As Accounting Officer and Chief Executive of the DPA, I have responsibility for maintaining a sound system of internal control that supports the achievement of the Agency's 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 'Government Accounting'.

I am accountable to the Minister for Defence Procurement. I report quarterly to the Defence Management Board on the performance of projects and against targets set for the DPA through the annual Service Delivery Agreement (SDA) that I agree with PUS and Chief of Defence Staff. Targets set for the DPA in the SDA are consistent with the Agency's Key Targets.

2. The purpose of the system of internal control

The system of internal control is designed to identify and to manage risk to a reasonable level rather than to eliminate all risk of failure to achieve policies, aims and objectives. It can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of the Agency's policies, aims and objectives, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically. The system of internal control has been in place in the Agency for the year ended 31 March 2006 and up to the date of approval of the annual report and accounts, and accords with Treasury guidance.

3. Capacity to manage and mitigate risk

The Executive Board continue to work towards embodying risk management and internal controls into DPA's business and management systems. The Executive Board's role in providing leadership to the risk management process has been demonstrated by its regular consideration of corporate risks in Board meetings. The Executive Board is accountable for reviewing and addressing any areas of weakness identified by the Audit committee, internal auditors and external auditors, in particular the NAO. A programme of risk awareness training is available to staff equipping them with the skills to manage risk effectively and meet business needs. Guidance is provided in documented and controlled procedures. DPA staff participate in a Risk Focus Group which brings together risk practitioners from each of the DPA and DLO clusters, and from across the Department to foster best practice.

4. The risk and control framework

We aim to capture risks from across the depth and breadth of the Agency and its stakeholder community. The Agency's approach to risk management addresses both **corporate risks** which are defined as having a probability and severity of impact that could adversely influence the achievement of one (or more) of the Agency's Key and Functional targets, and **project risks** that are specific to each individual project.

a) The **DPA Corporate Risk Management** process provides a controlled and documented framework for Agency staff to identify, categorise, and prioritise risks to Key and Functional targets in terms of probability and impact. The Executive Board assumes ownership of the risks and appoints risk controllers to manage all mitigation activities. To promote a better understanding of risk management in the context of the Agency's business the Executive Board has instituted a programme of risk management Master Classes for Risk Controllers, Integrated Project Team (IPT) Leaders and Support Group (SG) Leaders.

b) All DPA IPTs and SGs are encouraged to implement a recommended best practice **Project Risk Management** process, which is fully supported by detailed guidance, targeted training and appropriate tools. Project risks that threaten DPA Key and Functional targets are escalated to higher levels of management as part of the Corporate Risk Management process or through the periodic individual Project Review and Assurance events.

c) The DPA also has a strategy and policy for **Business Continuity** for the Agency which is reviewed on an annual basis and if there is a significant change of business conditions such as reorganisation. This is underpinned by detailed plans at IPT/SG Business Units level which identify key staff and other resources necessary for the continuation of business. A risk assessment has been carried out and is continually monitored.

d) A key component of the Agency's **financial assurance process** is the independence of the Financial Controller in each IPT and Support Group who has a direct reporting link to the Finance Director. The Business Analysts encourage best practice at Financial Controller level.

e) Additionally the Agency utilises a wide range of **Assurance Processes** covering the key areas of **Project Delivery; Technical, Commercial** and long-term **Support Solution Assurance.**

5. Review of effectiveness

As Accounting Officer, I have responsibility for reviewing the effectiveness of the system of internal control. In line with Departmental guidance I have established the following processes to maintain and review the effectiveness of the system of control:

a) An **Executive Board**, which meets monthly to manage the performance, plans and strategic direction of the Agency, comprising the Executive Directors of the Agency and three external, independent Non-Executive Directors. Following a review of Board effectiveness, the Executive Board has recently established a subsidiary Management Board, chaired by the Deputy Chief Executive, to concentrate on performance management, allowing the Executive Board to focus on building for the future and shaping the context for DPA operations.

b) A **Quarterly Corporate Risk Management report** is produced for the Management Board to monitor the status of each of the Corporate Risks and used in conjunction with monthly **project performance reports**. These reports link risk, and the steps taken to manage risk, to the achievement of the Agency's objectives. This enables the Management Board to ensure progress towards the achievement of Key and other Targets.

c) The appointment of an **Audit Committee** chaired by a Non-Executive Director. The Audit Committee meets quarterly to review the adequacy of the Agency's internal controls, risk management, and assurance processes and provides regular reports to the Executive Board highlighting issues and concerns.

d) A process of **Project Review and Assurance**: Operations Directors formally review the risks to performance, whole-life costs and to time on a regular basis and at each key project stage.

e) The DPA Management Board and Audit Committee review Business Continuity as part of Corporate Risk Management process and the Security and Business Continuity Stakeholder Group reviews the effectiveness of our plans.

f) Annual review by the Audit Committee of the 'Assurance Map' to identify various sources of assurance that underpin the system of internal control and targeting of assurance. This is consistent with the development of the Departmental Assurance Map.

g) From 1st January 2006 Earned Value Management has been mandated for Major Projects entering Demonstration Phase, as a means of monitoring progress against both project cost and build schedules. We expect the full benefits to be delivered in the longer term, although its introduction will strengthen our risk management approach and improve our relationship with industry.

h) Regular reports by Defence Internal Audit and by our internal assurance function, to standards defined in the Government Internal Audit Standards, which provide independent opinion on the system of internal control and recommendations for improvement.

My review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the executive managers within the Agency, who have responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports. I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the Board and Audit committee and a plan to address weaknesses and ensure continuous improvement of the system is in place.

6. Significant internal control weaknesses

It remains a matter of the highest priority for me and the Executive Board to continue to improve how our complex projects are managed. We have identified internal control weaknesses in the application of Earned Value Management, project cost estimating and risk management. We have several initiatives in hand to further develop our relationship with industry, the identification and management of risk, project cost estimating and more importantly, how we maintain this focus throughout the lifetime of the project to ensure through-life capability management in accordance with the principles of 'Smart Acquisition' and the 'Defence Industrial Strategy'.

Peter Spencer

Peter Spencer
Chief Executive
27th June 2006

The Certificate and Report of the Comptroller and Auditor General to the House of Commons

I certify that I have audited the Financial Statements of the Defence Procurement Agency for the year ended 31 March 2006 under the Government Resources and Accounts Act 2000. These comprise the Operating Cost Statement and Statement of Recognised Gains and Losses, the Balance Sheet, the Cashflow Statement and the related notes. These Financial Statements have been prepared under the accounting policies set out within them.

Respective responsibilities of the Agency, the Chief Executive and Auditor

The Agency and Chief Executive are responsible for preparing the Annual Report and Financial Statements in accordance with the Government Resources and Accounts Act 2000 and HM Treasury directions made there-under and for ensuring the regularity of financial transactions. These responsibilities are set out in the Statement of Accounting Officer's Responsibilities.

My responsibility is to audit the Financial Statements in accordance with relevant legal and regulatory requirements, and with International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the Financial Statements give a true and fair view and whether the Financial Statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with HM Treasury directions issued under the Government Resources and Accounts Act 2000. I also report whether 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. I also report to you if, in my opinion, the Annual Report is not consistent with the Financial Statements, if the Agency has not kept proper accounting records, if I have not received all the information and explanations I require for my audit or if information specified by relevent authorities regarding remuneration and other transactions are not disclosed.

I review whether the statement on *pages 32 to 35* reflects the Agency's compliance with HM Treasury's guidance on the Statement on Internal Control, and I report if it does not. I am not required to consider whether the Accounting Officer's Statements on Internal Control cover all risks and controls or to form an opinion on the effectiveness of the Agency's corporate governance procedures or its risk and control procedures.

I read the other information contained in the Annual Report and consider whether it is consistent with the audited Financial Statements. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the Financial Statements. My responsibilities do not extend to any other information.

Basis of audit opinion

I conducted my audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. My audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of financial transactions included in the Financial Statements and the part of the Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the Agency and Chief Executive in the preparation of the Financial Statements, and of whether the accounting policies are most appropriate to the Agency's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the Financial Statements and the part of the Remuneration Report to be audited are free from material misstatement, whether caused by fraud or error and that, 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. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the Financial Statements, and that part of the Remuneration Report to be audited.

Opinion

In my opinion:

- the Financial Statements give a true and fair view, in accordance with the Government Resources and Accounts Act 2000 and directions made there-under by HM Treasury, of the state of the Agency's affairs as at 31 March 2006 and of the net operating costs, recognised gains and losses and cashflows for the year then ended;
- the Financial Statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the HM Treasury directions issued under the Government Resources and Accounts Act 2000; and
- 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.

I have no observations to make on these Financial Statements.

John Bourn
Comptroller and Auditor General
National Audit Office
157-197 Buckingham Palace Road
Victoria
London SW1W 9SP
29th June 2006

The maintenance and integrity of the Ministry of Defence's website is the responsibility of the Accounting Officer; the work carried out by the auditors does not involve consideration of these matters and accordingly the auditors accept no responsibility for any changes that may have occured to the financial statements since they were initially presented on the website.

Operating Cost Statement

For the year ended 31 March 2006

	Note	2005/2006 £000	Restated (Note 27) 2004/2005 £000
Operating Costs			
Staff costs	2.2	176,804	190,841
Operating leases	5	82,238	82,139
Other operating costs	5	2,106,885	1,133,034
Finance lease charges			-
Gross operating costs		2,365,927	1,406,014
Operating income	6	(18,772)	(27,149)
Net operating cost before interest		**2,347,155**	**1,378,865**
Net interest payable/(receivable)		1,615	1,595
Cost of capital charge	7	553,229	648,716
Net operating cost after interest		**2,901,999**	**2,029,176**

The notes on pages 42 to 74 form part of these Financial Statements.

Statement of recognised gains and losses

For the year ended 31 March 2006

	Note	2005/2006 £000	2004/2005 £000
Net (gain)/loss on revaluation of fixed assets and stocks	18	(348,805)	(526,401)
Net gain on revaluation of donated assets	18	(1)	(2)
Transfer of donated assets	18	72	
Recognised (gains)/losses relating to the year		**(348,734)**	**(526,403)**
Prior year adjustment	27	(4,348,035)	
Recognised (gains)/losses since last Annual Report		**(4,696,769)**	

The results shown above are in respect of continuing activities.

The notes on pages 42 to 74 form part of these Financial Statements.

Balance Sheet

As at 31 March 2006

	Note	2005/2006 £000	Restated (Note 27) 2004/2005 £000
Fixed assets			
Intangible assets	8	6,578,833	5,676,213
Tangible fixed assets:			
Assets Under Construction	9	11,177,407	9,932,321
Other tangible assets	10	1,853,740	1,885,486
Investments	11	-	-
		19,609,980	17,494,020
Current assets			
Stocks and work-in-progress	12	2,635,220	2,610,291
Debtors	13	216,166	117,662
Cash at bank in hand	14	133,147	94,237
		2,984,533	2,822,190
Current Liabilities			
Creditors: amounts falling due within one year	15	(2,704,641)	(2,633,646)
Net current assets		279,892	188,544
Total assets less current liabilities		19,889,872	17,682,564
Creditors: amount falling due after more than one year	15	(173,218)	(85,794)
Provisions for liabilities and charges	17	(3,256,008)	(2,630,054)
Net assets		**16,460,646**	**14,966,716**
Taxpayers' equity			
General fund	19	14,224,711	13,005,506
Revaluation reserve	18	2,235,935	1,961,139
Donated assets reserve	18	0	71
		16,460,646	**14,966,716**

The notes on page 42 to 74 form part of these Financial Statements.

Peter Spencer

Peter Spencer
Chief Executive
27th June 2006

Cash Flow Statement

For the year ended 31 March 2006

	Note	2005/2006 £000	Restated (Note 27) 2004/2005 £000
Net cash flow from operating activities before interest	28	4,958,515	8,905,721
Net Capital expenditure	29	1,928,163	(2,371,181)
Net cash outflow before financing		6,886,678	6,534,540
Financing:			
– Payments from the Defence Resource Account		(6,934,735)	(6,547,030)
– Receipts into the Defence Resource Account		33,457	24,337
– Financing from other sources		(26,300)	–
– Returns on investment and servicing of finance		1,615	–
		(6,925,963)	(6,522,693)
Net financing from the Defence Resource Account	30	(6,925,963)	(6,522,693)
(Increase)/decrease in cash in hand and at bank in the period		**(39,285)**	**11,847**

Cash at bank includes overdrafts which are included in creditors.

The notes on page 42 to 74 form part of these Financial Statements.

Notes to the Agency Accounts

For the year ended 31 March 2006

1. Statement of Accounting Policies

1.1 Introduction

These Financial Statements have been prepared in accordance with the Resource Accounting Manual issued by HM Treasury, the Resource Accounting Policy Manual issued by the Ministry of Defence, and the Treasury Accounts Direction.

The principal accounting policies adopted by the Agency are summarised below. The policies set out the framework within which the Agency conducts financial management and have been applied consistently in dealing with items considered material to the Financial Statements.

1.2 Accounting Convention - Modified Historic Cost Accounting (MHCA)

The Financial Statements are prepared under the historical cost convention, modified to include the revaluation of intangible and tangible fixed assets, Assets Under Construction (AUC) and stocks. MHCA is applied to AUC when the value is over £25m and on Intangible Fixed Assets when the value is over £20m. The indices are produced by Defence Analytical Services Agency (DASA) and are common across the MoD.

1.3 Net Operating Costs

Costs are charged to the Operating Cost Statement in the period in which they are incurred and matched to any related recoveries.

1.4 Value Added Tax (VAT)

The Agency is not separately registered for Value Added Tax (VAT), which is accounted for centrally by the Ministry of Defence. Amounts included in the Operating Cost Statement and Balance Sheet are exclusive of VAT where it is recoverable from HM Revenue and Customs in respect of certain contracted out services as directed by the Treasury.

1.5 Intangible Fixed Assets

Intangible fixed assets are stated at actual contract cost, as adjusted for indexation. The total indexation value to date is £342m. Capitalised development costs are transferred to other parts of MoD at the same time as delivery of the first item of equipment. Development costs are capitalised where they contribute towards defining the specification of an asset type, e.g. class of ship or aircraft in accordance with the principles of SSAP 13. Amortisation commences when the asset type first enters service within the Department. If it is decided to withdraw a whole asset type early then any unamortised development costs are written off to the Operating Cost Statement, at the time of the decision, along with the underlying asset. Pure and applied research costs are charged to the Operating Cost Statement in the period in which they are incurred.

1.6 Tangible Fixed Assets

Tangible fixed assets are stated at their value to the Agency, with asset values and estimated economic lives being reviewed annually. Land and buildings are revalued by indexation in the periods between five yearly professional valuations, with other assets being subject to indexation. Indexation is produced using prescribed MoD indices. Single use military equipment, fighting equipment transport, plant machinery and vehicles, other transport and IT and Communication equipment are capitalised where the value is greater than £10,000.

A Quinquennial Review was undertaken during 2004/2005 by Defence Estates and carried out by the Valuation Office. 50% of MoD's Land and buildings were re-valued with the remaining 50% being addressed over the next two years. However, 100% of DPA's nuclear estate was re-valued whilst the Abbey Wood site was subject to a "desk-top" exercise using indexation.

The principal asset categories and their estimated useful economic lives are as follows:

	CATEGORY	YEARS
Land and Buildings	Land	Indefinite, not depreciated
	Buildings, dwellings (perm)	Useful economic life
	Buildings, non-dwellings (perm)	Useful economic life
	Buildings temporary	5 - 20
	Leasehold	Shorter of expected life and lease period
Single-use military equipment (including Guided Weapons, Missiles and Bombs		Effective operational life (on a pooled basis for GWMB)
Fighting Equipment transport		Effective operational life
Plant and Machinery		5 - 15
	Specialised Vehicles (includes non-fighting vessels and aircraft)	Effective operational life
	Specialist plant and machinery	Effective operational life
Other transport	Standard vehicles	3 - 5
IT and Communications Equipment	Computers	3 - 7
	Satellites	10
	Communications Equipment	Effective operational life
Non-Operational Heritage Assets		Indefinite, not normally depreciated
Assets under construction		Not depreciated
Capital Spares	Capital spares are items of repairable materiel retained for the purpose of replacing parts of an asset undergoing repair, refurbishment, maintenance, servicing, modification, enhancement or conversion.	Effective operational life (on a pooled basis, consistent with the effective operational life of the prime equipment supported)

Upon completion Assets Under Construction are transferred to other parts of the MoD for inclusion in their Balance Sheets.

1.7 Depreciation

Depreciation is calculated so as to write off the cost, or valuation, of tangible fixed assets, less their estimated residual values, on a straight line basis over their estimated useful economic lives.

1.8 Donated Assets

Donated tangible fixed assets are capitalised, within the principal asset category to which they relate, at their valuation on receipt; this value is credited to the Donated Asset Reserve. Subsequent revaluation and associated depreciation are also taken to this reserve.

1.9 Disposal of Tangible Fixed Assets

Assets declared for disposal and intended to be sold in bulk and where necessary subject to refurbishment prior to sale, are transferred to stock at the net recoverable amount. The remaining assets are eliminated from tangible fixed assets only on disposal to a third party and any surplus or deficit is shown in Other Operating Costs.

1.10 Operating Leases

Expenditure under operating leases is charged to the Operating Cost Statement in the period in which it is incurred. Operating Leases are detailed in *Note 21.*

1.11 Private Finance Initiative Transactions

Where the substance of the transaction is such that the risks and rewards of ownership remain with the Agency, the assets and liabilities remain on the Agency's Balance Sheet. Where the risks and rewards are transferred to the Private Sector the transaction is accounted for in the Operating Cost Statement through service charges in accordance with FRS5 and HM Treasury Guidance.

1.12 Investments

Investments represent holdings that the DPA intends to retain for the foreseeable future. Fixed asset investments are stated at market value where available, otherwise they are stated at cost.

1.13 Stocks

Stocks are stated at either current replacement cost or net realisable value. Current replacement cost applies to stocks expected to be used or sold in the ordinary course of business, and represents the cumulative revaluation of stock using latest cost of acquisition or indexation. Net realisable value applies to stocks that are not expected to be used or sold in the ordinary course of business, and have been identified for disposal. Where appropriate, provision is made for obsolete, surplus and defective stock. Provisions are also made to reduce the value of certain stock items over their estimated useful economic life. Current cost comprises purchase price and/or cost of conversion, and includes expenses incidental to acquisition, including irrecoverable VAT. Net realisable value is the estimated disposal sale value less the incidental costs chargeable to the sale.

1.14 Provisions for Liabilities and Charges

Provisions for liabilities and charges have been established to recognise a realistic and prudent estimate of the expenditure required to settle future legal or constructive obligations that exist at the Balance Sheet date where the amount and/or timing is uncertain. Provisions are charged to the Operating Cost Statement unless they have been capitalised as part of the underlying facility where the expenditure provides access to current and future economic benefits. In such cases the capitalised provision will be depreciated as a charge to the Operating Cost Statement over the remaining estimated useful economic life of the underlying asset. Where appropriate, provisions have been discounted to a current price base using HM Treasury's discount rate of 2.2% (2004/2005:3.5%). The discount for each material class of provision will be unwound over the remaining life of the asset class as an interest charge to the Operating Cost Statement. Provisions for restructuring and redundancy have been made only where the Agency has a detailed formal plan from which it cannot realistically withdraw. Provision made for early departure costs arising from retirement programmes and redundancies is charged to the Operating Cost Statement in the year in which the programmes are announced.

1.15 Reserves

The Revaluation Reserve reflects the unrealised element of the cumulative balance of indexation and revaluation adjustments on fixed assets and stocks (excluding donated assets and those financed by Government grants). The Donated Asset Reserve reflects the net book value of assets that have been donated to the Agency. The balance of taxpayers' equity is represented by the General Fund.

1.16 Pensions

Principal Civil Service Pension Scheme (PCSPS)

From 1 October 2002, civil servants may be in one of three statutory based 'final salary' defined benefit schemes (Classic, Premium and Classic Plus). New entrants after 1 October 2002 may choose between membership of Premium or joining a good quality "money purchase" stakeholder based arrangement with a significant employer contribution (Partnership Pension Account).

Classic Scheme

Benefits accrue at the rate of 1/80th of pensionable salary for each year of service. In addition a lump sum equivalent to three years' pension is payable on retirement. Members pay contributions of 1.5% of pensionable earnings. On death, pensions are payable to the surviving spouse at a rate of half the member's pension. On death in service, the scheme pays a lump sum benefit of twice pensionable pay and also provides a service enhancement on computing the spouse's pension. The enhancement depends on length of service and cannot exceed 10 years. Medical retirement is possible in the event of serious ill health. In this case, pensions are brought into payment immediately without actuarial reduction and with service enhanced as for widow(er) pensions.

Premium Scheme

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, but members may commute some of their pension to provide a lump sum up to a maximum of 3/80ths of final pensionable earnings for each year of service or 2.25 times pension if greater (the commutation rate is £12 of lump sum for each £1 of pension given up). For the purposes of pension disclosure note 2.2 assumes no commutation. Members pay contributions of 3.5% of pensionable earnings. On death, pensions are payable to the surviving spouse or eligible partner at a rate of 3/8ths the member's pension (before any commutation). On death in service, the scheme pays a lump sum benefit of three times pensionable earnings and also provides a service enhancement on computing the spouse's pension. The enhancement depends on the length of service and cannot exceed 10 years. Medical retirement is possible in the event of serious ill health. In this case, pensions are brought into payment immediately without actuarial reduction. Where the member's ill health is such that it permanently prevents them from undertaking any gainful employment, service is enhanced to what they would have accrued at age 60.

Classic Plus Scheme

This is essentially a variation of Premium, but with benefits in respect of service before 1 October 2002 calculated broadly as per Classic. Pensions payable under Classic, Premium and Classic Plus are increased in line with the Retail Prices Index.

Partnership Pension Account

This is a stakeholder type arrangement where the employer pays a basic contribution of between 3% and 12.5% (depending on the age of the member) into a stakeholder pension product. The employee does not have to contribute but where they do make contributions, these will be matched by the employer up to a limit of 3% (in addition to the employer's basic contribution). Employers also contribute a further 0.8% of pensionable salary to cover the cost of risk benefit cover (death in service and ill health retirement). The member may retire at any time between the ages of 50 and 75 and use the accumulated fund to purchase a pension. The member may choose to take up to 25% of the fund as a lump sum.

Armed Forces Pension Scheme (AFPS)

This is a statutory scheme that provides benefits on a 'final salary' basis at a normal retirement age of 55. Benefits accrue from the age of 21 up to a maximum of 34 years reckonable service (aged 55) at which the pension benefit will equate to 50% of final salary. In addition a lump sum equivalent to 3 years pension is payable on retirement. Pensions are linked to the Retail Prices Index. On death, pensions are payable to an entitled surviving spouse at the rate of half the member's pension. On death in service, the scheme pays a lump sum benefit of between 97% and 150% pensionable pay depending on length of service. Where the death is attributable to service causes, dependants' benefits may be significantly enhanced at the discretion of the Defence Council.

1.17 Benefits in kind

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

1.18 Capital Charge

A charge, reflecting the cost of capital utilised by the Agency, is included in the Operating Cost Statement. The charge is calculated using the HM Treasury standard rate on all assets and liabilities (except for donated assets, and balances held with the Office of Paymaster General (OPG) which are exempt from the charge). The rate charged by HM Treasury is 3.5%.

1.19 Foreign Exchange

Transactions denominated in foreign currency are translated into sterling using the MoD's General Accounting Rate (GAR) ruling at the date of each transaction. Monetary assets and liabilities are translated at the spot rate applicable at the Balance Sheet date and the exchange rate differences are reported in the Operating Cost Statement.

1.20 Notional Costs

Notional amounts are included in the Operating Cost Statement for charges in respect of services provided from other areas of the MoD. The amounts charged are calculated to reflect the full cost of providing the services to the Agency.

The Agency is not charged an audit fee by the National Audit Office. The audit fee represents a notional charge to the Operating Cost Statement based on the cost of the services provided.

1.21 Cash Flow

The management of liquid resources, which includes balances at commercial banks, is mainly due to balances on international collaborative projects. The level of balances is contingent upon the level of funding and the stage of the project.

2. Staff Numbers and Costs

2.1 The average number of full-time equivalent persons employed during 2005/2006 was as follows:

	2005/2006 Persons Employed	2004/2005 Persons Employed
Service		
Senior Management	30	36
Other Ranks	710	710
	740	**746**
Civilian		
Senior Management	530	478
Other Grades	3,292	3,287
Agency	128	40
	3,950	**3,805**
	4,690	**4,551**

2.2 The aggregate payroll costs, including allowances, for these persons were as follows:

	2005/2006 £000	2004/2005 £000
Salaries and Wages		
– Service	38,833	38,007
– Civilian	117,490	110,816
– Agency and Temporary Staff	6,362	3,481
Social Security costs	13,047	12,486
Other pension costs	31,930	25,014
Other Salary costs	–	–
Sub total	**207,662**	**189,804**
Redundancy and severance payments	(30,858)	1,037
Total payroll costs including Redundancy Payments	**176,804**	**190,841**

There was a net decrease in the provision for future redundancy and early retirement payments. Civilian early departure provision was reduced by £15m to reflect the change in method of calculation from forecast numbers to actual numbers in scheme. A further reduction of £16m was in respect of restructuring liabilities and charges.

3. Other Pension Costs

The PCSPS and the AFPS are non-funded multi-employer defined benefit schemes but the DPA is unable to identify its share of the underlying assets and liabilities. A full actuarial valuation was carried out at 31 March 2003 for the PCSPS and at 31 March 2005 for the AFPS. Details can be found in the resource accounts of these schemes that are published and laid before the House of Commons. The PCSPS is also available on the web at www.civilservice-pensions.gov.uk.

For 2005-2006, employers' contributions of £21.322m were payable (2004/2005: £14.850m) in respect of civilian staff at one of four rates in the range 16.2% to 24.6% of pensionable pay, based on salary bands. Rates will remain the same for the next year, subject to revalorisation of the salary bands. Employer contributions to the PCSPS are to be reviewed every four years following a full scheme valuation by the Government Actuary.

For Service personnel, employers' contributions of £10.607m (2004/2005: £10.164m) were made to the AFPS based on the rates of 34.3% of pensionable pay for Officers and 21.3% for other ranks, as determined by the Government Actuary. Employer contributions to the AFPS were reviewed during 2002/2003. The contribution rates reflect benefits as they are accrued, not when costs are actually incurred, and reflect past experience of the schemes.

Further details of the schemes are given in Notes 1.16.

4. Early Departure Costs

The Agency provides in full for the cost of meeting pensions up to normal retirement age in respect of early retirement programmes and redundancies announced in the current or previous years. Pensions payable after normal retirement age are met by the PCSPS for civilian personnel and the AFPS for service personnel. However, the additional element payable beyond the normal retirement age which derives from the enhancement of reckonable service continues to be met by the Agency. The Agency may, in certain circumstances, settle some or all of its liability in advance by making a payment to the Office of the Paymaster General account for the credit of the Civil Service Superannuation Vote. The amount provided is shown net of any such payments.

See also note 17 for provisions for future expenditures.

5. Other Operating Cost

	Note	2005/2006 £000	Restated (Note 27) 2004/2005 £000
Operating expenditure:			
– Hospitality and entertainment		98	172
– Movements, including staff travel costs		17,881	19,308
– Fuel		14,444	15,642
Stock consumption and valuation provisions		62,461	22,125
Accommodation management			
– Utilities		2,644	2,277
– Property management		12,889	11,540
– Accommodation charges		9,762	9,531
IT and Communications		11,340	15,987
Research and development expenditure		431,925	415,764
Equipment support and post design services		600,853	556,053
Education and Training		7,906	6,064
Professional Fees		14,073	15,328
Cost of training services provided		50,420	53,798
(Gain)/Loss on Exchange		(925)	1,644
Stock and project adjustments		(39,579)	22,683
Asset Write (on)/off		17,737	(39,822)
Other expenditure		1,897	5,584
Increase/(decrease) in nuclear decommissioning provisions	17	(118,070)	(290,219)
Increase/(decrease) in non-nuclear provision		(4,192)	19,401
Change to Treasury Discount Rate Effect on unwinding of provisions	17	776,611	0
Unwinding of nuclear decommissioning provision discount	17	71,672	94,721
Unwinding of non-nuclear provision discount	17	1,329	3,102
Auditors' remuneration	7	220	200
Charges from other parts of MoD	7	31,820	29,762
Depreciation and amortisation			
– Intangible assets	8	0	0
– Tangible fixed assets	10	120,638	101,077
– Impairment in value of fixed assets		11,922	51,805
– (Surplus)/Deficit on disposal of assets		0	0
Total Other Operating Costs before transfer		**2,107,776**	**1,143,527**
Communicated Costs to Lodger Units		(891)	(10,493)
Total Other Operating Costs after transfer		**2,106,885**	**1,133,034**
Operating Leases			
– Plant, Machinery and Vehicles (PMV)	21	24	102
– Other		82,214	82,037
Finance lease charges		–	–
Total Other Operating Costs (including Operating and Finance Leases)		**2,189,123**	**1,215,173**

6. Operating Income

	2005/2006 £000	Restated (Note 27) 2004/2005 £000
Operating income for 2005/2006 was received from external customers, Other Government Departments and Trading Funds – includes £1m rental receipts, £8.5m from NATO, £3.6m commercial exploitation levies and £2m liquidated damages	(18,772)	(27,149)
Total operating income	**(18, 772)**	**(27,149)**

7. Charges from other parts of MoD (Notional Costs)

Operating costs include non-cash items, and notional costs for services provided by other parts of the MoD:

	2005/2006 £000	Restated (Note 27) 2004/2005 £000
Charges from other parts of the MoD		
– MoD Central Overheads	5,588	5,399
– MoD Guarding/Policing	22,307	21,864
– Defence Storage and Distribution Agency	0	1
– Defence Bills Agency	759	665
– Defence Internal Audit	121	131
– Defence Codification	1,142	1,080
– Pay and Personnel Agency	788	0
– Defence Communications Fleet Tasking Agency	26	20
– Defence Postal and Courier Services	252	253
– Defence Transport and Movements Agency	837	349
Total Charges from other parts of MoD (Notional Costs)	31,820	29,762
NAO – Notional Fee for Audit Work (see note below)	220	200
Cost of Capital	553,229	648,716
Total Non-cash costs for services provided	**585,269**	**678,678**

The National Audit Office did not undertake any Non-Audit work during the year.

8. Intangible Fixed Assets

	2005/2006 £000	2004/2005 £000
Cost or Valuation		
At 1 April	5,676,213	9,307,442
Additions	1,449,588	1,451,832
Impairment losses		(709)
Transfers to other parts of the MoD	(533,127)	(5,618,596)
Revaluation	113,919	237,339
Net asset write-on	6,669	–
Disposals	–	–
Reclassifications	(134,429)	298,905
At 31 March	**6,578,833**	**5,676,213**
Amortisation		
At 1 April	–	–
Disposed of in year	–	–
At 31 March	**–**	**–**
NBV at 31 March	**6,578,833**	**5,676,213**

Development costs are transferred to other parts of the MoD for inclusion in their Balance Sheets with the first production delivery of related equipment.

Re-classifications are between asset categories in the following IPTs: Typhoon (£118m), Bowman, Torpedoes and General Support Vehicles.

9. Assets Under Construction

	2005/2006 £000	2004/2005 £000
Cost or Valuation		
At 1 April	9,932,321	9,501,260
Additions	3,934,282	3,270,070
Impairment losses	(4,155)	–
Transfers to other parts of the MoD	(2,926,689)	(2,450,390)
Revaluation	114,529	158,602
Net Asset write-on	31,089	
Disposals	–	–
Reclassification	96,030	(547,221)
At 31 March	**11,177,407**	**9,932,321**

Assets Under Construction (AUC) are transferred to other parts of the MoD for inclusion in their Balance Sheets as the related equipment is delivered.

Re-classifications are between asset categories in the following IPTs: Typhoon (£118m), Bowman, Torpedoes and General Support Vehicles.

Nuclear area – movement of completed assets from AUC to Fixed Assets Land and Buildings, Plant & Machinery and IT and Communications.

10. Other Tangible Fixed Assets

	Land and Buildings dwellings £000	Land and Buildings non-dwellings £000	Single-use military equipment £000	Plant & Machinery £000	Fighting Equipment transport £000	Other Transport £000	IT and Comms Equipment £000	Capital Spares £000	TOTAL £000
Cost or Valuation									
At 1 April 2005 Restated (Note 27)	518	697,071	8,357	2,089,695	220	4,313	40,265	48,861	2,889,300
Additions	–	25,381	–	192	–	–	1	–	25,574
Impairment losses	–	(5,123)	–	824	–	–	(7,228)	(1)	(11,528)
Disposals	(71)	(18,159)	–	(16,124)	–	(173)	(10,671)	–	(45,198)
Revaluation	25	21,518	–	38,559	–	58	–	1	60,161
Transfers to other parts of the MoD	(60)	–	(4,487)	(125)	351	3	(14)	2,147	(2,185)
Reclassifications	–	19,677	–	16,561	–	–	2,161	–	38,399
At 31 March 2006	**412**	**740,365**	**3,870**	**2,129,582**	**571**	**4,201**	**24,514**	**51,008**	**2,954,523**
Depreciation									
At 1 April 2005	(71)	(81,097)	(1,390)	(876,465)	(90)	(1,613)	(24,684)	(18,404)	(1,003,814)
Charged in year	(24)	(21,494)	(290)	(81,370)	(79)	(540)	(8,623)	(8,218)	(120,638)
Backlog depreciation	(3)	(1,272)	–	(4,826)	–	(15)	–	(1)	(6,117)
Impairment Losses	–	(759)	–	(64)	–	–	4,584	–	3,761
Disposals	7	517	–	10,111	–	82	14,594	–	25,311
Transfers to other parts of the MoD	15	–	596	107	(7)	–	–	3	714
Reclassifications									
At 31 March 2006	**(76)**	**(104,105)**	**(1,084)**	**(952,507)**	**(176)**	**(2,086)**	**(14,129)**	**(26,620)**	**(1,100,783)**
Net Book Value at 31 March 2006	**336**	**636,260**	**2,786**	**1,177,075**	**395**	**2,115**	**10,385**	**24,388**	**1,853,740**
NBV at 1 April 2005	**447**	**615,974**	**6,967**	**1,213,230**	**130**	**2,700**	**15,581**	**30,457**	**1,885,486**

Other Tangible Fixed Assets

10.1 Re-classifications include transfers from Assets Under Constructiuon (AUC) to Land & Buildings, Plant & Machinery and IT and Communications within the Nuclear area.

10.2 Donated assets are capitalised at their current valuation on receipt and are re-valued and depreciated on the same basis as purchased assets. Where donated assets are classed as Non-Operational Heritage assets they are deemed as having infinite life. In such cases no depreciation is charged.

Quinquennial Review

10.3 Land and buildings are re-valued every 5 years through the MoD's Quinquennial Review (QQR) of fixed assets and is managed through a rolling programme due to complete in 2007/2008. In the intervening years, the values of fixed assets are revised using indices provided by the Department. As part of the QQR, the Agency's nuclear estate was re-valued as at 1 April 2004 by the Valuation Office Agency (VOA). The VOA is a Government Agency independent of the MoD. Assets were valued on the basis of Existing Use or Depreciated Replacement Cost, as appropriate to the nature of the asset. The remainder of the Agency's estate was re-valued by the Defence Estates Agency using a 'desktop' revaluation exercise.

10.4 A desk-top revaluation for the Abbey Wood site was undertaken in April 2004: valuation was £51,480,700.

10.5 A professional valuation was carried out by the VOA at Dounreay and the Seismology Centre, Eskdalemuir in April 2004: valuation was £21,576,000.

10.6 For 2005/2006 Land and Buildings values were re-valued using predicted GDP deflators and inflation rates.

11. Investments

Investments, including ‘special shares’ are held in the following companies at 31 March 2006:

Investments	£1 Preferential shares
Atomic Weapons Establishment plc	1 share
Atomic Weapons Establishment Pensions Trustees Limited	1 share
BAE SYSTEMS Marine (Holdings) Limited	1 share

All shares held are unlisted and are valued at historical cost.

"Special shares" confer on the Secretary of State for Defence special rights regarding ownership, influence and control, including voting rights in certain circumstances, under individual Articles of Association of the relevant companies in which the shares are held. Further detailed information can be obtained from the companies’ individual Annual Report and Accounts which can be obtained from:

Atomic Weapons Establishment plc, AWE Aldermaston, Reading RG7 4PR
Atomic Weapons Establishment Pensions Trustees Limited, AWE Aldermaston, Reading RG7 4PR.
BAE SYSTEMS Marine (Holdings) Limited, Warwick House, PO Box 87, Farnborough Aerospace Centre, Farnborough, Hants, GU14 6YU.

12. Stocks and Work in Progress

	2005/2006 £000	2004/2005 £000
Raw materials and consumables	2,635,220	2,610,291
Total stocks and work in progress	**2,635,220**	**2,610,291**

13. Debtors

	2005/2006 £000	Restated (Note 27) 2004/2005 £000
Amounts falling due within one year		
Trade debtors	19,548	13,613
Deposits and advances	9,184	16,399
VAT		343
Other debtors	139,126	68,686
Prepayments and accrued income	48,560	27,181
Less Bad debts	(252)	(8,560)
Total debtors: amounts falling due within one year	216,166	117,662
Amounts falling due after one year		
Trade debtors	–	–
Prepayments and accrued income	–	–
Less bad debts	–	–
Total debtors: amounts falling due after one year	–	–
Total debtors	**216,166**	**117,662**

13(b) Intra-Government Balances

	Amounts falling due within one year	Amounts falling due after more than one year
Balances with Trading Funds		
Defence Science and Technology Laboratory (DSTL)	85,439	
Meteorological Office	1,432	
Hydrographic Office	3,332	
Sub-total: intra-government balances	90,203	–
Balances with Bodies external to government	125,963	–
Total debtors at 31 March 2006	**216,166**	**–**

14. Cash at Bank and In Hand

	2005/2006 £000	2004/2005 £000
As at 1 April	94,237	82,390
Net Cash Inflow/(Outflow):	38,910	11,847
As at 31 March	133,147	94,237
Balances at:		
Office of HM Paymaster General (OPG)	1,793	3,199
Commercial Banks and Cash in Hand	131,354	91,038
As at 31 March	**133,147**	**94,237**

Of the total balance, £24,278,085 is 'non-liquid cash'.

15. Creditors

	2005/2006 £000	Restated (Note 27) 2004/2005 £000
Amounts falling due within one year		
Trade creditors	207,753	271,465
Payments received on account	127	1,122
VAT	24,399	22,500
Other creditors	108,474	82,341
Accruals and deferred income	2,363,888	2,256,218
Total creditors due within one year	**2,704,641**	**2,633,646**
Amounts falling due after more than one year		
Other creditors	173,218	85,794
Capital element of finance leases	–	–
Total creditors due after one year	**173,218**	**85,794**

A re-assessment of the milestone payments on the Principal Anti-Air Missile System (PAAMS) project for the Type 45 destroyer has resulted in £82m of contract retentions (due in 2008) now classified as Creditors due after more then one year.

16. Intra-Government Balances

	Amounts falling due within one year	Amounts falling due after more than one year
Balances with other Central Government Bodies		
Cabinet Office	118,365	
Foreign and Commonwealth Office	375	
Balances with Local Authorities		
Forest of Dean District Council	9,634	–
Trafford Metropolitan Borough Council	24,681	–
Balances with Trading Funds		
Defence Science and Technology Laboratory (DSTL)	1,593,471	–
Defence Aviation Repair Agency (DARA)	101,325	–
Army Base Repair Organisation (ABRO)	7,323	–
Sub-total; intra-government balances	1,855,174	–
Balances with Bodies external to government	849,467	173,218
Total Creditors at 31 March 2006	**2,704,641**	**173,218**

17. Provisions for liabilities and charges

	Note	Nuclear decommissioning £000	Early retirement pensions commitments £000	Other £000	Total £000
At 1 April 2005 Restated	27	2,482,597	32,601	114,856	2,630,054
Utilisation of provisions		(40,338)	(6,256)	(48,444)	(95,038)
Change in Treasury Discount Rate		775,206	755	650	776,611
Unwinding of discount		71,672	937	392	73,001
Amounts capitalised		25,370	–	–	25,370
Transfer		–	–	–	–
Capitalised provision movements		–	–	–	–
Increase/(Decrease) in provisions		(118,070)	(15,095)	(20,825)	(153,990)
As at 31 March 2006		**3,196,437**	**12,942**	**46,629**	**3,256,008**

Major non-nuclear provisions relate to delay and dislocation claims and outstanding liabilities as a result of UK withdrawal from a collaborative project.

Nuclear Decommissioning

17.1 Nuclear decommissioning provisions relate principally to the cost of facility decommissioning and the treatment and storage of nuclear waste arising at MoD sites, operations of Royal Navy submarines and for the Departmental share of planning and constructing a national repository for the eventual disposal of that waste.

17.2 On the 1 April 2005, the Nuclear Decommissioning Authority (NDA), a newly formed organisation sponsored by the Department of Trade and Industry, took over the responsibility for certain nuclear decommissioning activities. As a result, the MoD liabilities at 1 April 2005 relating to civil nuclear sites and the associated value of provisions and funding for decommissioning costs were transferred to NDA. The liabilities for the decommissioning of other MoD sites and for the disposal of submarine waste have been retained by MoD. The MoD retains responsibility for the Automic Weapons Establishment (AWE).

17.3 The liabilities include the costs associated with decommissioning and care and maintenance of redundant facilities including submarines (the conditioning, retrieval and storage of contaminated materials), research and development, and the procurement of capital facilities to handle the various waste streams.

17.4 Calculation of the provision to cover the liabilities is based on schedules of information received by the MoD from major decommissioning contractors. These schedules are based on technical assessments of the processes and methods likely to be used in the future to carry out the work. Estimates are based on the latest technical knowledge and commercial information available, taking into account current legislation, regulations and Government policy. The amount and timing of each obligation are therefore sensitive to these factors. These sensitivities and their likely effect on the calculation and amount of the liabilities are reviewed on an annual basis.

17.5 The latest estimate of the undiscounted cost of dealing with the MoD's nuclear liabilities is £7,849,052,414 (2004/2005 £22,079,526,236) – (£8,057,105,236 excl NDA)

17.6 The estimate of £3,196,437,258 (2004/2005 £6,803,257,261) – (£2,482,597 excl NDA) at 31 March 2006 represents the liabilities discounted at 2.2% and expressed in 2005/2006 money values.

The estimated timescale over which the costs will need to be incured is as follows:

	31 March 2006 £000	1 April 2005 £000	1 April 2005 £000 excl NDA
Up to 3 years	309,098	1,272,152	316,240
From 4 – 10 years	710,779	1,599,902	595,857
Beyond 10 years	2,176,560	3,931,203	1,570,500
Total	**3,196,437**	**6,803,257**	**2,482,597**

17.7 Provisions have been made to cover the costs associated with the research, development and construction of the NIREX Deep Waste Repository (DWR). The provisions have been based on advice provided by NIREX. However, the policy for the disposal of intermediate and high level waste has yet to be clarified following the previous government's rejection, in May 1997, of planning consent for the proposed DWR. Pending the current government's consideration of a House of Lords Sub-Committee report on means of disposing of radioactive waste, the UK holders of such waste are working on the assumption that a repository will not be available earlier than 2040, with 2080 being the most likely date. This will necessitate the continued provision of interim storage.

17.8 During 2005/2006 a formal review has been undertaken of the AWE nuclear provision, incorporating an assessment of the risks and assumptions which underpin the provision calculations and the level of contingency within it. Progress made since 2000 against the original plans was also examined. The outcome of this review was the decision to retain the provision at its current level until the next quinquennial review (due 2007).

18. Reserves

		Revaluation Reserve		Donated Asset Reserve
	2005/2006 £000	2004/2005 £000	2005/2006 £000	2004/2005 £000
As at 1 April	1,961,139	2,481,101	71	69
Donated assets in year			–	–
arising on revaluation during the year (net)	348,805	526,401	1	2
Transfers to other parts of the MoD	(80,205)	(1,039,883)	–	–
Reclassifications	–	–	–	–
Transferred (to)/from General Fund	6,196	(6,480)	(72)	–
Donated Asset:				
Profit/(Loss) on disposal			–	–
Depreciation charged to OCS			–	–
Impairment charged to OCS			–	–
As at 31 March	**2,235,935**	**1,961,139**	**0**	**71**

The movement on the Donated Assets Reserve reflects the gifting of the Pattern Room, the world's largest working collection of military small arms, to the Royal Armouries on 1 September 2005.

19. Movements in the General Fund

	Note	2005/2006 £000	2005/2006 £000	2004/2005 £000	Restated (Note 27) 2004/2005 £000
General Fund at 1 April			13,005,506		10,974,395
Net Vote Expenditure			6,925,963		6,522,693
Net Operating cost for the year			(2,901,999)		(2,029,176)
Realised revaluation on disposal of assets	18		(6,196)		6,480
Revised revaluation on donated Asset	18		72		
Non-Cash Transactions:					
cost of capital	7	553,229		648,716	
cost communication		(891)		(10,493)	
auditors' remuneration	7	220		200	
notional costs	7	31,820	584,378	29,762	668,185
Net transactions with other parts of the MoD:					
transfer of intangibles	8	(533,127)		(5,618,596)	
transfer of AUC	9	(2,926,689)		(2,450,390)	
transfer of tangible fixed assets	10	(3,993)		(1,224)	
transfer of revaluation reserve	18	80,205		1,039,883	
transfer of investments	11	–		–	
retained transfer		–		–	
other transfers		591	(3,383,013)	(207,890)	(7,238,217)
Re-statement of General Fund	27				4,348,035
Re-statement of OCS	27				(246,889)
General fund at 31 March 2006			**14,224,711**		**13,005,506**

20. Capital Commitments

Capital commitments at 31 March 2006, for which no provision has been made in these Financial Statements, were as follows:

	2005/2006 £000	2004/2005 £000
Contracted but not provided for	17,811,804	19,492,477

21. Financial Commitments

	31 March 2006 £000	31 March 2005 £000
Lease Obligations The DPA was committed to making the following payments during the next year in respect of non-land and buildings operating leases:		
Expiry within one year	–	–
Expiring between two and five years	79,057	79,057
Expiring after five years	–	–

DPA has leased four Boeing C17s from the Boeing Corporation in the United States.

There are no lease commitments under finance leases with inception occurring after 31 March 2006.

22. Financial Instruments

The DPA has no borrowings and relies primarily on Parliamentary Supply for its cash requirements, and is therefore not exposed to liquidity risks. It also has no material deposits, and all material assets and liabilities are denominated in sterling, so it is not exposed to interest rate risk or currency risk. All our disclosures exclude short-term debtors and creditors.

FRS 13, Derivatives and Other Financial Instruments, requires disclosure of the role which financial instruments have had during the period in creating or changing the risks an entity faces in undertaking its activities. Because of the largely non-trading nature of its activities and the way in which Government Departments are financed, the Agency is not exposed to the degree of financial risk faced by business entities. Moreover, financial instruments play a much more limited role in creating or changing risk than would be typical of the listed companies to which FRS 13 mainly applies. Financial assets and liabilities are generated by day-to-day operational activities and are not held to change the risks facing the Department in undertaking its activities.

Liquidity risk

The Department's revenue and capital resource requirements are voted annually by Parliament and are therefore not exposed to significant liquidity risks.

Interest rate risk

A significant proportion of the Agency's financial assets and liabilities carry nil or fixed rates of interest. The exposure to interest risk is therefore not significant.

Foreign currency risk

The MoD enters into forward purchase contracts annually with the Bank of England to cover the majority of its foreign exchange requirements for the following year. Details of the outstanding foreign currency contracts will be contained in the Departmental Accounts.

23. Private Finance Initiative (PFI) Commitments

The payments made during the year in respect of on and off Balance Sheet PFI transactions were £118,969,770 (2004-2005: £92,865,199). There were no leased assets included within Fixed Assets in 2005-2006, or 2004-2005. Therefore there were no capital elements of finance leases and On Balance Sheet PFI rentals.

The payments which the DPA is committed to make during the year 2006-2007 are analysed below by timebands specifying the period in which the individual commitment expires:

	31 March 2006 £000	31 March 2005 £000
In the 1st Year	–	–
In the 2nd to the 5th Year	–	–
In the 6th to the 10th Year	–	–
In the 11th to the 15th Year	138,305	73,483
In the 16th to the 20th Year	–	–
In the 21st to the 25th Year	45,275	48,937
In the 26th to the 30th Year	–	–

The likely financial effects in future years on which DPA is committed are contingent upon specific contract terms, which will be dependent upon any actual volume implications of specific PFI deals. The above values are therefore based on the contracted levels of activity. The likelihood of future activity levels above these has not been factored in, as DPA transfer the equipment or services to other MoD organisations to operate, once in service.

The following information is provided for those schemes assessed as off Balance Sheet.

Project Description	Estimated Capital Value £000	Contract Start Date	Contract End Date
Attack Helicopter Training mission simulator: 3 field deployable simulators, ground crew, maintenance and armament training.	165,000	July 1998	September 2027
Skynet 5 Provision of military satellite communications services	1,140,000	October 2003	February 2018

24. Related Party Transactions

The Defence Procurement Agency is an agency of the Ministry of Defence which is regarded as a related party. During the year the Agency has had material transactions with the Department and other entities for which the Department is regarded as the parent.

In addition, the Agency had various material transactions with Other Government Departments (OGDs), other Central Government bodies, Public Corporations, NHS Trusts and local authorities as stated below.

MoD Training Funds:	
Defence Science and Technology Laboratory	£64m
Army Base Repair Organisation	£1m
Other Government Departments:	
Foreign & Commonwealth Office	£5m
United Kindom Atomic Energy Authority	£5m
Cabinet Office	£3m
Local Authorities:	
West Berkshire District Council	£5m
South Gloucestershire District Council	£4m

During the year, no Board member or key manager has undertaken any material transactions with the Agency.

As development and equipment is completed, it is delivered to the Armed Forces customer, at which point the asset transfers from the DPA Balance Sheet to that of the owner of the equipment in service.

25. Contingent Liabilities

The DPA has potential liabilities relating to the decommissioning of Astute submarine boats 1, 2 and 3 commencing in 2031/32, 2033/34, and 2034/35 respectively.

26. Post Balance Sheet Events

It is MoD's intention to create a new organisation from 1 April 2007, which will subsume the main functions of the Defence Procurement Agency. The status of the new organisation is yet to be determined and will be subject to consultation. The functions performed by the DPA will continue to be carried out by the MoD so there are no issues arising which affect the going concern. Consequently there are no adjustments required to the accounts.

On 1 April 2006, the Ministry of Defence transferred responsibility for accounting for fixed assets from the Defence Procurement Agency to other parts of the Ministry of Defence. Where the Agency retains the risks and rewards of ownership of these assets they will continue to be accounted for on the Agency's Balance Sheet in accordance with FRS 5 and SSAP 21. In other cases the costs of the use of these assets will be communicated to the Defence Procurement Agency by the asset owners and charged to the Operating Cost Statement. Consequently, these centrally accounted for assets will not be included on the Agency's Balance Sheet as they will be accounted for as operating leases under SSAP 21. There is no effect on the 2005/2006 accounts as a result of this change, and as a result no adjustments have been made to these Financial Statements.

27. Restatement of 2004/2005 Accounts

Balance Sheet

	Closing Balance 2004/2005 £000	Total Adjustment £000	Restated Closing Balance £000
Land and Buildings	641,680	(25,705)	615,975
Debtors	139,183	(21,521)	117,662
Creditors: amounts falling due within one year	(2,708,379)	74,733	(2,633,646)
Provisions	(6,950,582)	4,320,528	(2,630,054)
General Fund	(8,878,098)	**4,348,035**	(4,530,063)

Operating Cost Statement

	2004/2005 £000	Total Adjustment £000	Restated Balance £000
Increase/(decrease) in nuclear provisions	(185,434)	(104,785)	(290,219)
Unwinding of nuclear decommissioning discount	236,825	(142,104)	94,721
Adjustment for 2004/2005	51,391	**(246,889)**	(195,498)

'Total Adjustment' reflects the movement arising out of the transfer of responsibility for managing and cleaning of civil nuclear sites and the associated value of provisions and funding for decommissioning costs to the Nuclear Decommissioning Authority (NDA) on 1 April 2005.

28. Reconciliation of net operating cost before interest to net cash outflow from operating activities before interest

For the year ended 31 March 2006

	Note	2005/2006 £000	Restated (Note 27) 2004/2005 £000
Net operating cost before interest		2,347,155	1,378,865
Non-cash transactions			
– Depreciation and amortisation charges	10	(120,638)	(101,077)
– Permanent diminution in value of Fixed assets		(11,922)	(51,805)
– Stock provisions		(1,243)	10,102
– Stock write-off/on		(62,174)	(29,972)
– Auditors' remuneration	7	(220)	(200)
– Notional costs	7	(31,820)	(29,762)
– Communicated costs		891	10,493
– Surplus/(deficit) on disposal of fixed assets and investments	5	–	–
– Changes in provisions for liabilities and charges	17	153,989	165,707
– Unwinding of Provision Discounts	17	(849,612)	(97,823)
– Stock and project adjustments		39,579	(22,683)
– Write-off and write-on of assets		(17,737)	39,822
Adjustments for movements in working capital other than cash after adjustment for communicated costs			
– Increase/(decrease) in stocks/work in progress		(282,993)	(96,384)
– Increase/(decrease) in debtors		98,504	(45,401)
– (Increase)/decrease in creditors		(66,347)	167,077
Charged against provisions for liabilities and charges		93,241	354,139
Movement in Inter management group balances		3,669,862	7,254,623
Net cash (inflow)/outflow from operating activities before interest		**4,958,515**	**8,905,721**

29. Analysis of net capital expenditure and financial investment

For the year ended 31 March 2006

Acquisition of fixed assets	Note		2005/2006 £000	2004/2005 £000
Purchase of fixed assets				
– Intangibles		1,459,265		1,539,680
– AUC		3,852,298		3,116,967
– Other Fixed Assets	10	25,574		23,078
– Less capitalised provisions	17	(25,370)		(20,579)
Total purchase of fixed assets			**5,311,767**	**4,659,146**
Asset Transfers to Other Areas of the MoD				
– Intangibles	8	(533,127)		(5,618,596)
– AUC	9	(2,926,689)		(2,450,390)
– Other Fixed Assets		(3,993)		(1,224)
– Revaluation Reserves	18	80,205		1,039,883
			(3,383,604)	**(7,030,327)**
Other Transactions				
– Proceeds from disposal of fixed assets			–	–
Total other transfers			**(3,383,604)**	**(7,030,327)**
Net cash outflow/(inflow) from capital expenditure and financial investment			**1,928,163**	**(2,371,181)**

30. Determination of net cash requirement

For the year ended 31 March 2006

	Note	2005/2006 £000	Restated (Note 27) 2004/2005 £000
Vote expenditure appropriated in year	19	(6,925,963)	(6,522,693)
(Increase)/decrease in cash	14	(38,910)	11,847
Net cash requirement		**(6,964,873)**	**(6,510,846)**
Movement in Inter-Management-Group Balances			
Balance at 1 April		(7,123)	(8,420)
Movement in year	29	3,669,862	7,254,623
Balance at 31 March		**3,662,739**	**7,246,203**

Note: the movement between opening balance of (7,123) and closing balance prior year of 7,246,203 is due to the clear-down of the inter-management accounts at year-end.

31. Losses and special payments

A Losses Statement, details of Special Payments, Gifts, Loans and other notes as described in "Government Accounting" are required to be included in the financial statements. The purpose of the Losses Statement is to report all defined losses that have been brought to account during the year. In addition, any individual loss that exceeds £250,000 is noted separately.

The tables below give details of the payments made, and losses incurred, by the DPA as disclosed in the 2005/2006 Departmental Resource Accounts.

Losses Statement	**2005/2006 £000**
Total (205 cases)	**284,253**
Details (cases over £250,000)	
Constructive Losses	
This constructive loss arose from the UK Government decision not to proceed into the production for the medium range anti-tank guided weapons system (MR TRIGAT). Negotiations are continuing in connection with the LR TRIGAT project – estimated value of further write-off is £205m (see Advanced Notification)	**105,343**
A delay in the production of helicopter training course material resulted in a write-off	**8,369**
Loss due to a new building at AWE that was not fit for purpose and cannot be utilised in any other capacity (total loss £148m)	
a. a loss of £83m has been incurred in respect of plant and equipment within the building	**82,983**
b. a loss of £65m has been incurred following the impairment of the building	**64,672**

Special Payments (2 cases)

Ex gratia payments were made on account to British Nuclear Fuels plc and the United Kingdom Atomic Energy Authority towards the cost of treatment and disposal of nuclear waste and decommissioning plant at British Nuclear Fuels sites.

Total paid to 31 March 2005 is £1.503Bn. Final payments for 2005/2006 were passed to NDA as part of the transfer of responsibility for historic liabilities relating to the cleaning and decommissioning of civil nuclear sites.

HM Treasury agreed an ex gratia payment of up to £84.5m to Swan Hunter subject to completion of certain contractual conditions relating to the construction of two Landing Ship Dock (Auxiliary) LSD(A). Total paid to 31 March 2006 was £84.5m. Payments are now completed. The MoD originally placed a contrct for four LSD(A). There is a possible claim for £63.8m for delay and dislocation costs relating to the other two ships. (see Advanced Notification)	**84,500**
Gifts (1 case)	
MoD Pattern Room to the Royal Armouries Leeds. Details of the transfer were notified to the House of Commons in a Departmental Minute dated 14 June 2001. The effective date of transfer was September 2005.	**6,000**
Accounting and Bookkeeping Losses	
Clearance of obsolete balances for old, completed projects. Amounts written off.	**16,551**

Advanced Notification

Previously notified

This constructive loss arose from the UK Government decision not to proceed into production for the long-range TRIGAT anti-tank guided weapons systems (LR TRIGAT)	**205,000**
Slippage in the construction programme for two Landing Ship Docks (Auxiliary) caused delay in supplying design information and equipment to a contractor. This resulted in a claim on the MoD relating to the associated delay and dislocation costs.	**63,800**
The value of 8 Chinook Mk3 helicopters has been written down by £205m under prudent accounting practices while the MoD established a way forward for the programme. The write-down has arisen because, although the terms of the contract had been met, the helicopters do not currently meet operational requirements and cannot acquire Military Aircraft release.	**205,000**
The extended range ordnance modular charge system (ERO/MCS) was cancelled due to technical diffulties with the MCS that could not be resolved. This produced an estimated constructive loss. In 2003/2004 the loss was estimated at £34.5m.	**32,798**
A potential loss was reported last year following the termination of a contract for 4.5kW generators as a result of contractor non-performance. The loss did not materialise as all expenses were covered by call on a Financial Bond.	

Notified during the year

A potential claim against a contractor on the ASTOR programme has been abandoned resulting in a loss, but other benefits have been secured in compensation.	**28,000**
A potential loss arose as a result of the UK Government decision to reduce the number of Nimrod MRA4 being procured from 18 to 12.	**32,600**
A commercial compensation package agreed as a result of slippage to the delivery dates by the contractor and the unavailability of components for the COBRA programme has resulted in a potential write-off.	**548**
A constructive loss arose as a result of a settlement between the Agency and a manufacturer for the provision of Manportable Remote Control Vehicles (MRCVs).	**1,117**
Cancellation of the Alternative Launcher Drive system (ALDS) programme has resulted in a potential write-off.	**4,000**
An agreement breached with a contractor that required contracts for nuclear cores to be placed within a certain timeframe rendering MoD liable to pay default costs.	**562**
Special Payments	
Contractor is claiming extra costs resulting from the late delivery of unusable GPS chips in respect of the Storm Shadow missile programme, purchased via Foreign Military Sales (FMS). An earlier write-off of £1.763m was recorded in the 2004/2005 Accounts. However, the MoD is attempting to re-claim this extra cost from the supplier of the Government Furnished Equipment (GFE) via the US Courts.	**4,000**
There is a possible ex-gratia payment in settlement of the Armoured Vehicle Training Service (AVTS) PFI procurement strategy.	**2,900**
There is a possible extra contractual payment resulting from the late supply of GFE to the TITAN & TROJAN project.	**3,800**

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