HM Treasury

Whole of Government Accounts:

year ended 31 March 2016

HC 254

July 2017

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1 Overview and performance analysis

Overview

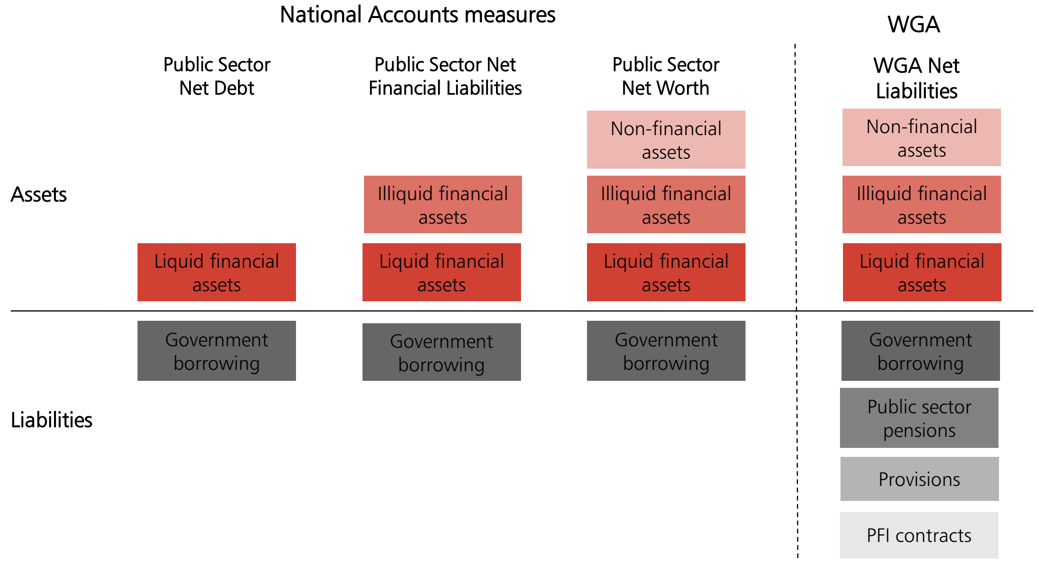
1.1 The Whole of Government Accounts (WGA) are financial statements prepared in accordance with International Financial Reporting Standards (IFRS). WGA reports on the financial performance and position of the UK public sector through a statement of income and expenditure, a statement of financial position (or balance sheet), a statement of cash flows and a statement of other recognised gains and losses, together with associated notes providing additional detail and analysis.

1.2 WGA consolidates the audited accounts of over 6,000 organisations across the UK public sector including central government departments, local authorities, devolved administrations, the NHS, academy schools and public corporations. It is a uniquely comprehensive product as it is the only set of consolidated public sector accounts in the world that includes both central and local government.

1.3 The amounts reported in WGA are different from those reported in the National Accounts, the statistical reporting framework used by the government for budgeting, reporting and financial analysis.

1.4 Chart 1.A illustrates the scope of National Accounts measures for financial position and the balance sheet position reported in WGA. As WGA includes assets and liabilities not reported within the National Accounts, it provides a more complete picture of the government's financial position. By incorporating long-term liabilities, such as the pension entitlements of public sector employees or liabilities incurred under public-finance initiative (PFI) contracts, WGA provides more information about the future consequences of decisions already taken and financial commitments already entered into.

Chart 1.A: Comparison of National Accounts and WGA measures

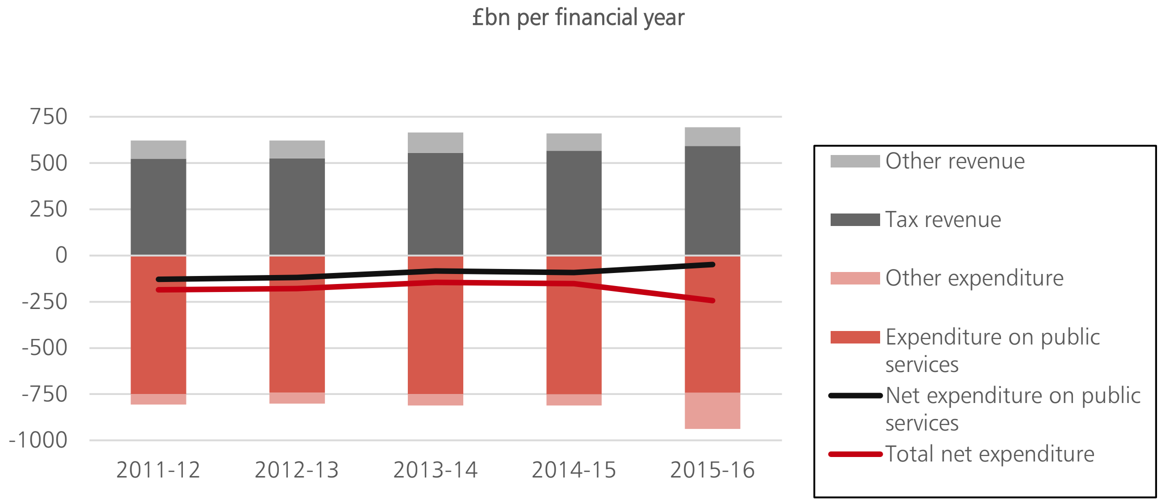


1.5 In looking at the fiscal picture, there are a number of different statistical measures available which each provide a different perspective of the health of the government's balance sheet. Public Sector Net Debt (PSND) comprises government borrowings less liquid financial assets (such as bank deposits and foreign exchange reserves). PSND excluding the public sector banks is the government's preferred measure of fiscal health as it is consistent with the internationally agreed National Accounts framework. Public Sector Net Financial Liabilities expands on PSND to include all financial assets, such as loans, derivatives and equity investments. The most comprehensive measure within National Accounts is Public Sector Net Worth which compares the government's debt with all of its assets, including physical assets which are used to deliver services such as infrastructure, offices, hospitals and schools.

1.6 When considering the affordability of long-term liabilities the government additionally considers the future cash flows and how sustainable they are, often expressed as a percentage of GDP. Further information on the profile and affordability of long-term liabilities, including provisions and public sector pensions, is included in the Performance Analysis and in the Office for Budget Responsibility fiscal sustainability reports.

The public sector income and expenditure

Chart 1.B: Income and expenditure trends



1.7 Over the last 5 years expenditure on public services as recorded in WGA has remained flat at around £746 billion. This is because increased expenditure on social protection and health has been offset by lower levels of impairments, for example on the government's shareholding in Royal Bank of Scotland, and by lower levels of new provisions (as opposed to valuation changes for existing liabilities).

1.8 Over the same period revenue has increased from £621.5 billion to £693.9 billion, primarily as a result of an increase in tax revenue of £69 billion. This means that net expenditure on public services in WGA has decreased by 62% from £128.5 billion to £48.3 billion, mirroring reductions in the current budget deficit from £81.1 billion to £40.1 billion.

1.9 WGA also includes expenditure for financing government's long-term liabilities which are not included in National Accounts. The change in the discount rate used to value future provision payouts in today's prices, led to an additional expense of £125.2 billion in this year's WGA and an increase to overall net expenditure.

1.10 WGA discloses expenditure in the categories as required by the accounting standards, for example staff costs. An alternative breakdown of public expenditure would be to split expenditure based on the services that are being delivered, such as health or transport.

1.11 The main data source for the alternative breakdown of public expenditure by objective or outcome is the Public Expenditure Statistical Analyses (PESA).[1] PESA is the yearly HM Treasury publication of information on government spending and it aligns with public spending in the National Accounts (i.e. the expenditure element of the current budget deficit). It brings together recent outturn data, estimates for the latest year, and spending plans for the rest of the current spending review period.

[1] https://www.gov.uk/government/statistics/public-expenditure-statistical-analyses-2016

Table 1.A: Public services expenditure breakdown

Function	2015-16 £bn	% of total	2014-15 £bn	2013-14 £bn	2012-13 £bn	2011-12 £bn
Social protection	264.2	38%	260.9	254.0	253.4	244.8
Health	138.7	20%	134.1	129.4	124.3	121.3
Education	84.0	12%	85.7	85.3	84.2	86.5
Defence	36.6	5%	36.7	36.4	36.3	38.7
Public order and safety	30.2	4%	29.6	29.6	31.3	32.1
Transport	28.1[2]	4%	20.3	19.1	18.5	19.4
Other economic affairs	17.0	3%	17.9	18.9	16.5	17.4
Environment protection	11.6	2%	11.6	11.2	10.7	10.5
Housing and community amenities	10.0	1%	10.2	9.8	10.0	10.2
Recreation, culture and religion	11.4	2%	12.4	11.4	12.7	12.5
General public services	22.0	3%	22.1	21.1	19.0	19.2
Debt interest	36.7	5%	36.5	39.7	40.4	44.5
EU transactions	7.7	1%	6.2	7.2	6.7	4.3
Public services expenditure per PESA	**698.2**	100%	684.2	673.1	664.0	661.4
Add: Depreciation and impairment	42.7		45.4	51.1	51.1	64.4
Add: Increase in provisions	9.2		26.0	18.3	21.6	15.5
Accounting adjustments	(7.9)		(4.3)	6.4	4.2	8.7
WGA expenditure on public services	**742.2**		751.3	748.9	740.9	750.0

Source: Public Expenditure Statistical Analyses 2016, Table 4.2

1.12 PESA is prepared on a different basis than WGA, therefore figures do not align precisely. PESA shows that expenditure on public services has increased over the last 5 years, driven by increases in expenditure on social protection and health.

1.13 The largest element of expenditure on public services is social protection. This incorporates social security benefits (the largest element of expenditure within WGA) and broader expenditure on social protection such as social care. This expenditure is captured through staff costs, purchase of goods and services and other lines within WGA based on the type of expenditure incurred to deliver social protection.

[2] Increase in expenditure on Transport is due to Network Rail being included in PESA for the first time in 2015-16

The public sector balance sheet

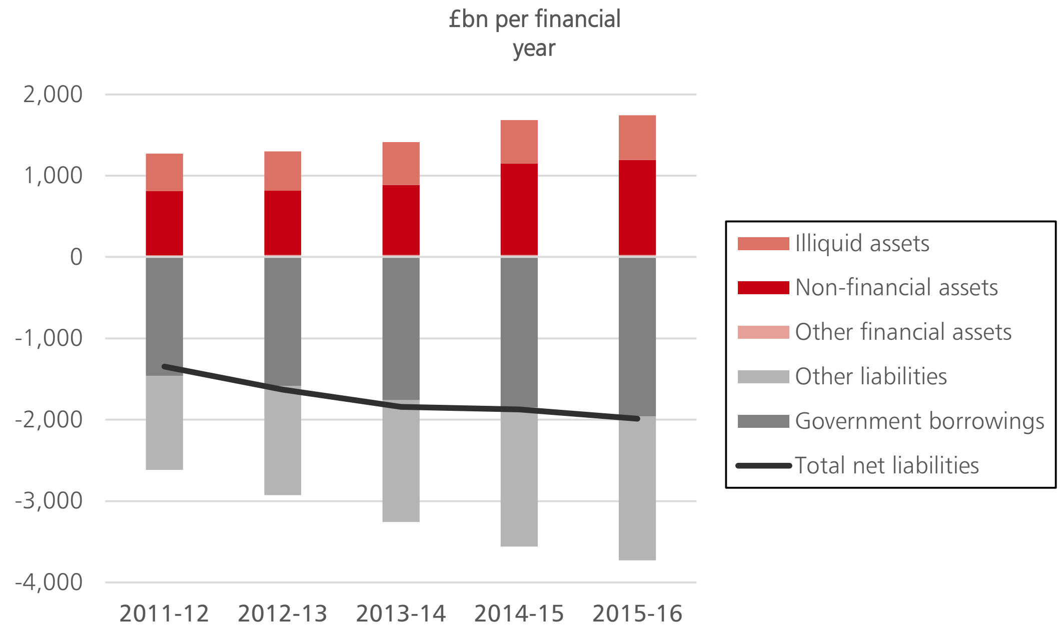
1.14 The public sector balance sheet has expanded significantly over the last 5 years. In part, this is due to government borrowing increasing to fund in-year deficits and capital investment. This is reflected in the increase in PSND excluding public sector banks from £1.2 trillion in March 2011 (76% of GDP) to £1.6 trillion in March 2016 (84% of GDP).

1.15 Similarly other liabilities have increased from £1.2 trillion to £1.8 trillion leading to an overall increase in liabilities of around 42%. The largest increase in other liabilities took place in 2015-16 as a result of a change in the discount rate used to value long-term provisions. This discount rate change alone increased provisions by £125.2 billion. 2015-16 was the first time since WGA has been prepared that this long-term discount rate has changed and it decreased significantly from 2.2% to negative 0.8%, reflecting decreases in government's borrowing costs over the last 10 or so years. The change in discount rate has a very significant impact on how future cash flows are converted to today's prices, most notably for the nuclear decommissioning provision due to its size and long-term nature.

1.16 The long term nature of some of the government's liabilities mean that even small changes to the discount rates can have a large impact on the liabilities. In the current year this is particularly noticeable in the effect that the change in the long term discount rate had on the provision for nuclear decommissioning and the provision for clinical negligence. In 2016-17 the discount rate used for the public sector pension scheme liability will decrease significantly, which will cause a material increase in the valuation of the pension liability. Over the last 5 years there has also been an increase in financial assets (£478.3 billion to £573.4 billion) and non-financial assets (£792.3 billion to £1,169 billion). Assets have increased at a slower rate than liabilities, in part due to the government intentionally not retaining assets when there is not a strong rationale to do so. For the most part, liabilities will be funded from future taxation rather than assets built up in advance.

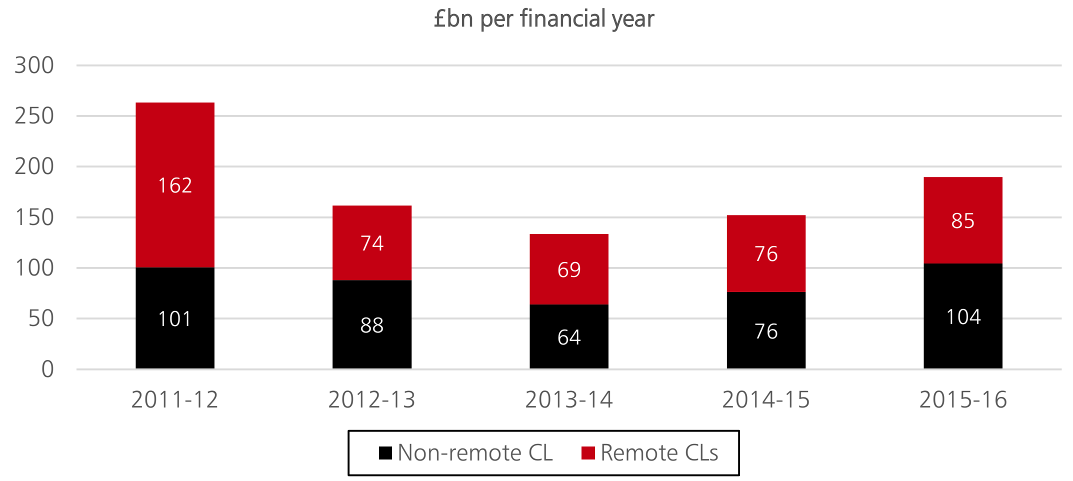
1.17 Overall there has been an increase in risk due to the increase in the government's liabilities over the last 5 years which is discussed in further detail in the Performance Analysis section.

Chart 1.C: Asset and liability trends



Contingent liabilities

Chart 1.D: Quantifiable Contingent Liabilities (CLs): Non-remote and remote



1.18 The public sector's exposure to quantifiable contingent liabilities has reduced overall, as guarantees issued to support the financial sector at the time of the financial crisis have subsequently expired. However, certain contingent liabilities, most notably relating to tax and clinical negligence, have increased over the same period and further details are provided in the Performance Analysis.

1.19 In addition to the quantifiable contingent liabilities mentioned above, the government had entered into a number of contingent liabilities where the size of the liability could either not be determined with reasonable certainty or to quantify it would jeopardise the outcome of any legal proceedings. The details of the most significant non-quantifiable contingent liabilities are included in notes 29 and 30 to the financial statements.

Further information available

1.20 In addition to WGA, further information is published by HM Treasury and others on the public finances as viewed using the National Accounts framework:

- Public Expenditure Statistical Analyses (PESA) provides backwards and forwards looking analyses of public expenditure. It includes an analysis of public expenditure by country and region. The information in PESA can therefore be used to understand the profile of spend across government
- Annex A to WGA reconciles WGA outturn figures to Public Sector Net Debt and the current budget deficit. It also explains the differences between WGA and National Accounts frameworks
- the OBR's Fiscal Sustainability Report sets out long-term projections for spending, revenue and financial transactions, and assesses whether they imply a sustainable path for public sector debt[3]

[3] http://budgetresponsibility.org.uk/fsr/fiscal-sustainability-report-january-2017/

Performance analysis

Key findings from the 2015-16 WGA

1.21 In summary, the 2015-16 WGA shows:

- revenue increased by 5%, from £659.9 billion to £693.9 billion, primarily due to an increase in taxation revenue
- total expenditure on public services decreased by 1%, falling from £751.3 billion to £742.2 billion; small increases to social security benefits, staff costs and interest costs on government borrowings were more than offset by lower levels of new provisions
- net expenditure on public services decreased by 47%, from £91.4 billion to £48.3 billion
- the cost of financing government's long term liabilities resulted in an additional expense of £187.4 billion compared to £65.1 billion in 2014-15. Of this, £125.2 billion is due to a change in the discount rate used to produce a current valuation of provisions. A further £52.1 billion relates to the increase in the present value of the pensions liability as a result of the benefits being one year closer to settlement and the discount therefore unwinding over time
- total assets increased by 4%, from £1,683.3 billion to £1,742.4 billion, due to investment in land and buildings, the government increasing its holdings of foreign currency reserves and an increase in the value of student loans as a result of both an increase in the volume of lending and a lower impairment amount
- total liabilities increased by 5%, from £3,558.5 billion to £3,728.4 billion, driven by increases in provisions and a rise in the level of government borrowing required to fund the fiscal deficit
- despite total liabilities increasing, the public section pension liability decreased by 5%, from £1,493.3 billion to £1,424.7 billion, as a result of a small increase in the discount rate and demographic changes being less significant than originally expected by scheme actuaries. The benefit of this reduced liability has been recognised in Other Comprehensive Income and doesn't affect net expenditure
- the overall result is that the net liability position of the balance sheet has increased by 6%, from £1,875.2 billion to £1,986.0 billion

1.22 The rest of this performance analysis provides an overview of the government's income, expenditure, assets and liabilities. Further detail is also available in the notes to the account as set out overleaf.

Income

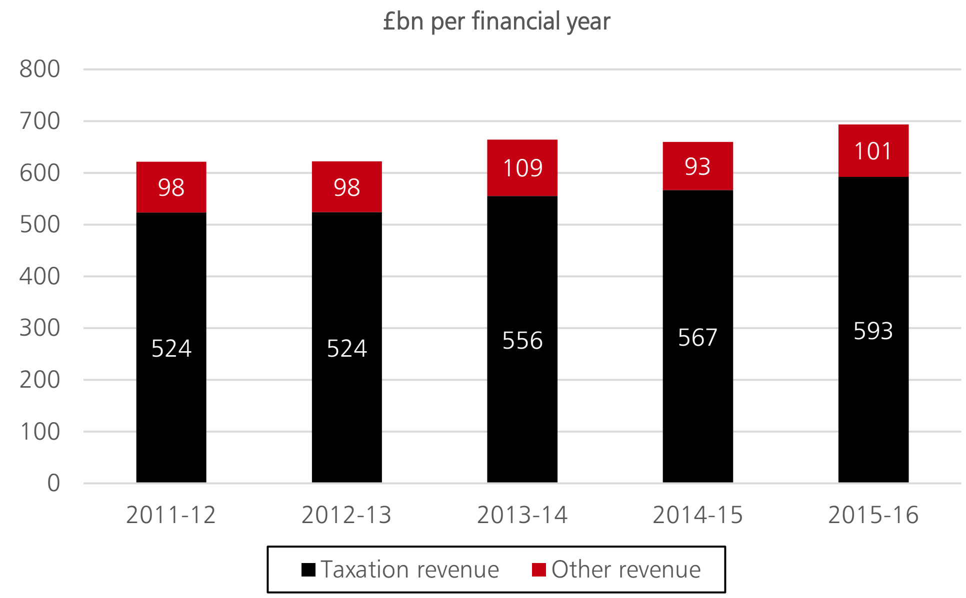
What does government receive from taxes and other income?

The primary source of revenue is **taxation**, making up 85% of total public sector income

		2015-16 £bn	2014-15 £bn
Taxation revenue	Note 4	592.6	566.7
Other revenue	Note 5	101.3	93.2
Total public services revenue		**693.9**	659.9

1.23 Over the last 5 years there has been an increase in the total revenue from public services which is analysed in further detail below.

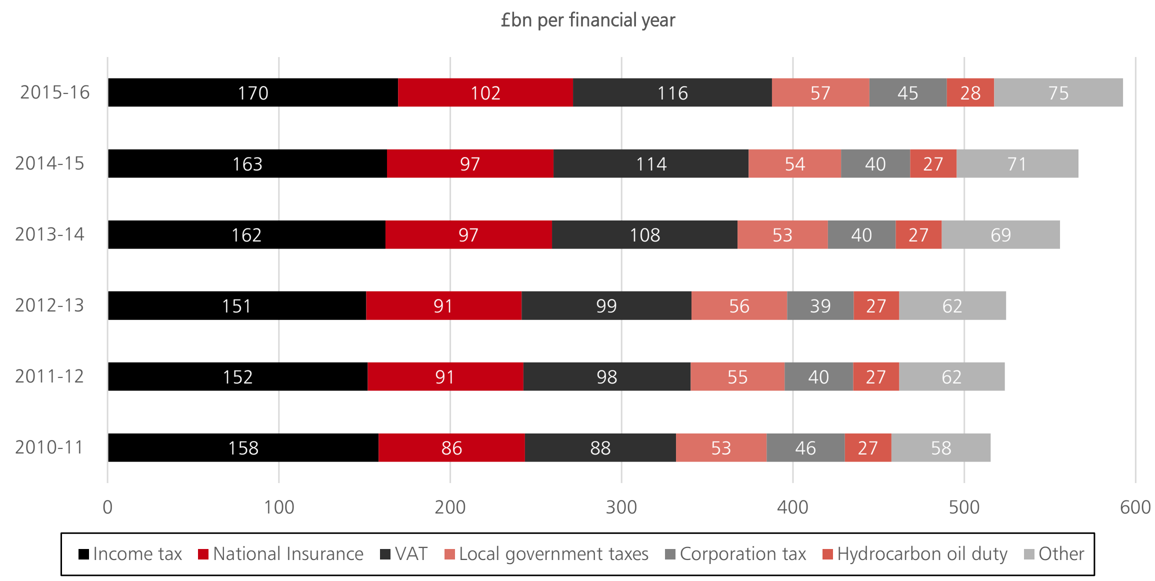
Chart 1.E: Income trend



Tax revenue

1.24 The forecasted tax receipts for 2015-16 as set out in the 2015 Summer Budget were £628.9 billion and the outturn reported by the OBR was £630 billion. This is higher than the taxation reported in WGA. The WGA balance is lower as National Insurance Contributions, VAT and business rates paid by the public sector are eliminated and certain levies are included within other revenue. The chart and text below is therefore based on the eliminated balance.

Chart 1.F: Breakdown of tax revenue by type



1.25 Taxation revenue increased by 5% compared to the prior year, primarily due to an increase in the overall level of activity in the economy:

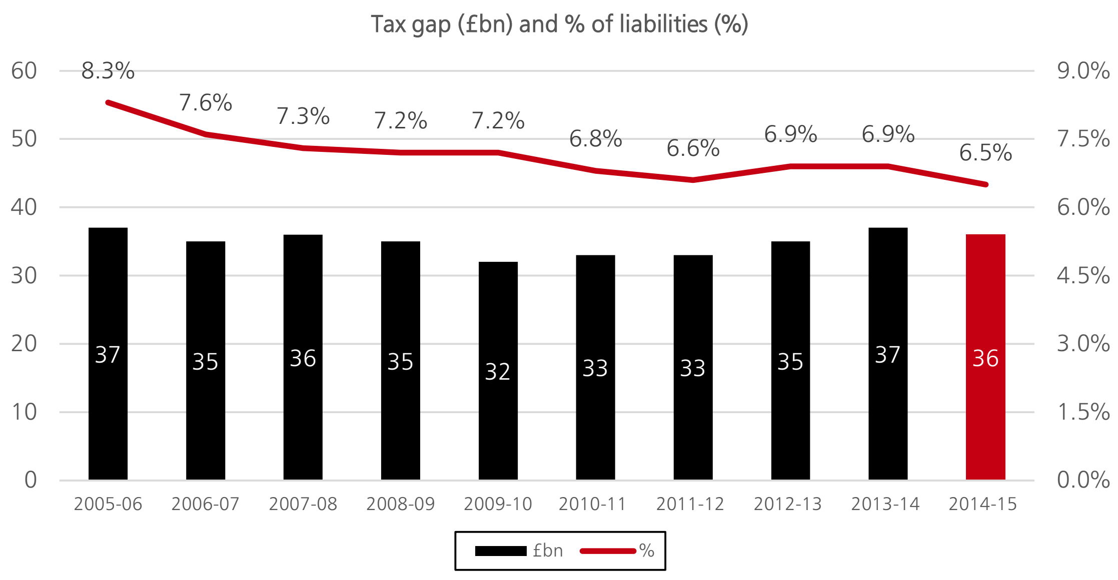
- Income tax (29% of tax revenue), and National Insurance Contributions (17% of tax revenue) increased by 4% and 5% respectively, due to higher levels of employment and higher wages
- Value Added Tax (VAT) (20% of tax revenue) increased by 2%, due to increases in receipts for the automotive, business services and utilities sectors as well as higher household spending
- Corporation Tax (8% of tax revenue) increased by 12%
- hydrocarbon oils (5% of tax revenue) increased by 2%, due to the reduction of pump prices increasing the amounts purchased
- Council Tax and National Non-Domestic Rates (10% of tax revenue) increased by 5% and 6% respectively.

1.26 A number of other taxes, including stamp taxes, alcohol and tobacco duties, Capital Gains Tax, Inheritance Tax and Air Passenger Duty, accounted for the remaining 11%.

The tax gap and compliance revenues

1.27 The tax gap is the difference between the amount of tax that should in theory be collected by HMRC against what is actually collected. HMRC publish an estimate of the tax gap each year. For 2014-15, the latest year that data is available, the tax gap is estimated to be at £36 billion which is 6.5% of theoretical tax liabilities.

Chart 1.G: Tax gap and percentage of theoretical tax liabilities 2005-06 to 2014-15



1.28 There is an overall downward trend in the tax gap from 8.3% in 2005-06 to 6.5% in 2014-15. The tax gap estimate of £36 billion is £11 billion lower than it would have been if the percentage tax gap level had remained at the 2005-06 level.

Other revenue

1.29 Note 5 of the accounts sets out the government's sources of revenue, other than taxation. Overall, other revenue increased by 9% compared to the prior year. This is primarily as a result of increases in the net profit on sale of assets. The most significant sources of other revenue are:

- sale of goods and services totalling £35.5 billion, for example charges made by local authorities for social care or planning and development
- fees, levies and charges totalling £12.8 billion, for example those set by the NHS for dental and prescription services
- net profit on sale of assets totalling £6.3 billion, mainly arising from the sale of shares in the Lloyds Banking group and RBS

Expenditure

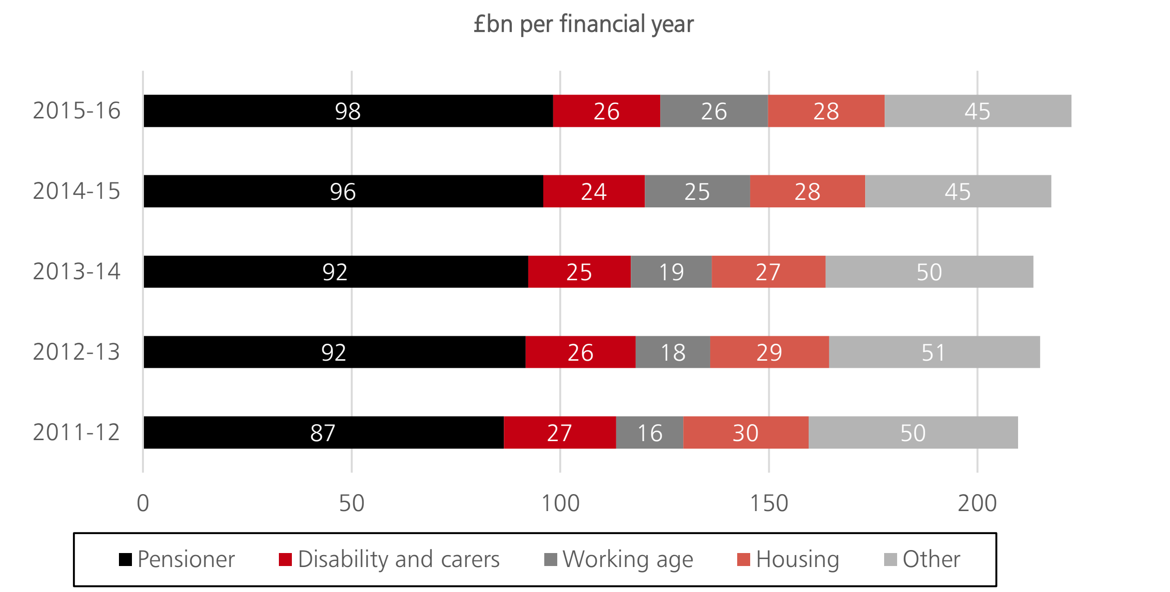
What does government spend on providing services and running costs?

The most significant elements of expenditure were **social security benefit payments**, **goods and services** purchased to meet operational requirements, and the **cost of employing staff** in the public sector.

		2015-16 £bn	2014-15 £bn
Social security benefits	Note 6	222.5	217.7
Staff costs	Note 7	193.3	185.5
Purchase of goods and services	Note 8	192.1	191.7
Other operating expenditure	Notes 9 and 10	96.8	102.8
Interest costs on government borrowing	Note 11	28.3	27.6
Increase in provisions	Note 22	9.2	26.0
Total expenditure on public services		**742.2**	751.3

Social security benefits

Chart 1.H: Breakdown of social security benefits



1.30 Government spending on social security benefits increased by 2% compared with 2014-15. The effect of lower unemployment was offset by higher spending on people with disabilities and health conditions as well as higher spending on the state retirement pension.

1.31 Increases in pensioner benefit spending reflect both demographic trends and the government's policy of increasing state pensions every year by the highest of price inflation, earnings growth, or 2.5% (the 'triple lock').

1.32 The rising prevalence of mental health conditions and learning difficulties, particularly at younger ages, has been an important driver of the rising disability benefits caseload and the rising proportion of incapacity benefit claimants that are being placed in the support group of Employment and Support Allowance (which is more expensive to the exchequer than the alternative work-related activity group).

1.33 The two largest areas of spending – employment and support allowance and its predecessor incapacity benefit and the personal independence payment and its predecessor disability living allowance – are the subject of ongoing reforms. The impact on spending of both sets of reforms has proved difficult to forecast, with each yielding smaller savings than were originally intended.

1.34 The overall increase in social security benefit spending in 2015-16 was consistent with the longer term trend on benefit expenditure as set out in the chart above. There has been a £12.8 billion (6%) increase in benefit expenditure over the past 5 years.

1.35 At Summer Budget 2015 and subsequent fiscal events, further reforms to the welfare system were announced. The most recent Welfare Trends Report projects that between 2015-16 and 2020-21, overall spending on welfare will as a result have fallen by 2.3% in real terms (relative to CPI inflation forecasts).[4]

Staff costs

1.36 Staff costs comprises expenditure on salaries and wages of £149.6 billion (2014-15: £148.5 billion) and expenditure on pensions of £43.7 billion (2014-15: £37.0 billion).

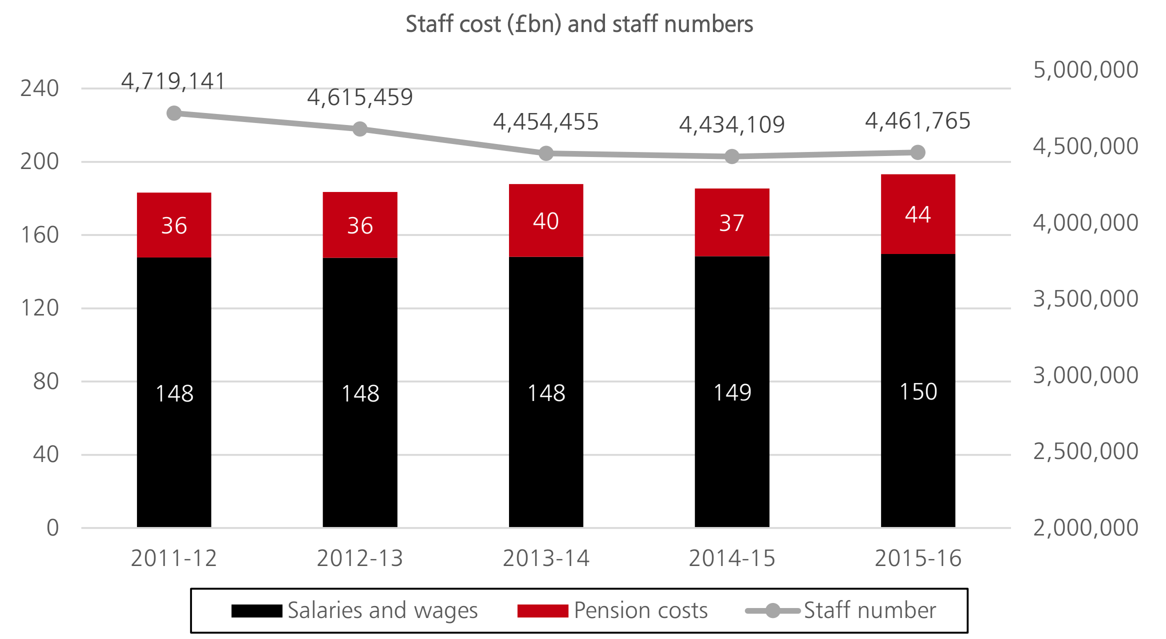
1.37 Salaries and wages have shown a slight increase of 1% or £1.1 billion in comparison to 2014-15. Of this, £0.6 billion relates to the first time inclusion of Further Education colleges in Northern Ireland and Scotland.

1.38 The increase in pension costs was primarily due to an increase in current service costs (net of employees' contributions) for public sector pensions of £4.1 billion and an increase in expenditure on external pension schemes of £1.5 billion. The current service cost is an estimate made by scheme actuaries of the benefit earned by employees in the year and it is used to determine standard contribution rates for each scheme. In 2015-16 these standard contribution rates increased for a number of schemes, including NHS, Armed Forces and local government, resulting in higher levels of employer expenditure. For example the standard contribution rate for the NHS Pension Scheme changed from 32.7% in 2014-15 to 36.0% in 2015-16. Further details on the applicable standard contribution rates can be found in the annual reports of the pension schemes. This has been the first valuation following the pension reforms.

1.39 The government continued to set public sector pay awards at an average of 1% in 2015-16. As a result of this salaries and wages have remained relatively stable over the last 5 years. There has been an increase in pension costs and these are discussed in further detail in the public sector pensions section of this chapter.

[4] http://budgetresponsibility.org.uk/wtr/welfare-trends-report-october-2016/

Chart 1.I: Staff cost and staff numbers trend



1.40 Further details on staff costs and numbers are included in the Remuneration and Staff Report in Chapter 4.

Purchase of goods and services

1.41 Purchases of goods and services remained fairly constant compared to the prior year, increasing by £0.4 billion or 0.2%. One of the challenges with WGA is getting a more in-depth breakdown of this balance as the level of detail provided by bodies included in the consolidation is very variable. Along with the timing of the account, this is a key area for development in future years. This year's WGA includes a segmental analysis of purchase of goods and services in note 3 to the accounts and an analysis of total expenditure on public services by objective or outcome in the Overview to this chapter.

Interest costs on government borrowing

1.42 The cost of servicing government debt increased by £0.7 billion or 3%, whilst at the same time the stock of government debt increased by 7% from £1,174.5 billion to £1,260.6 billion. The effective interest rate in 2015-16 was 2.3%, which is slightly higher than the 2014-15 rate of 2.2%.

1.43 Debt interest costs as a share of total receipts fell from 4.2% in 2014-15 to 4.1% in 2015-16. The interest costs exclude interest that is paid on debt held by the Bank of England as part of its quantitative easing programme. This reduces interest costs recognised in WGA by around a third.

Financing long-term liabilities

What does government pay to finance its long-term liabilities?

The government recognises expenditure when estimating the value of liabilities which will be paid in the future.

		2015-16 £bn	2014-15 £bn
Provision financing costs	Note 11	127.9	1.9
Pension financing costs	Note 11	52.1	56.6
Other finance expense	Note 11	7.4	6.6
Total financing costs of long-term liabilities		**187.4**	65.1

Valuing long-term liabilities

1.44 Some of the government's operations result in liabilities that are very long-term and will involve cash outflows over decades to come. For example, the costs of carrying out nuclear decommissioning and the costs of public sector pensions. The amount that will be paid out to settle these liabilities is uncertain, yet WGA must present a single number in the accounts as a best estimate. Estimating the amount that will be paid out involves a number of assumptions, the most significant of which are described in the critical accounting policies in note 2 to the accounts.

The effect of the discount rate

1.45 The discount rate for pensions is updated annually by scheme actuaries. In 2015-16 the rate increased slightly from 1.3% to 1.37% reflecting increased yields on corporate bonds. This increase contributed approximately £48.0 billion of the £123.0 billion revaluation gain on pensions. This decrease in liability has been recognised on the balance sheet and in Other Comprehensive Income, but not net expenditure.

1.46 The more significant impact of financing pensions in WGA is the effect of unwinding the discount each year as the future stream of payouts gets a year closer. For provisions, this effect is relatively modest and results in around £2.5 billion of expenditure each year. For pensions the effect is much more significant and resulted in £52.1 billion of expenditure in 2015-16 and £56.6 billion in 2014-15.

1.47 In 2015-16, the long-term provisions discount rate was updated by HM Treasury for the first time since 2003-04 and decreased from 2.2% to negative 0.8%. This increased the value of the existing provisions in today's prices by £125.2 billion without impacting the amount that the government actually expects to pay to settle its provisions.

1.48 Box 1.A on the following page provides more information on discount rates while the Liabilities section of the Performance Analysis provides further information on the affordability of long term liabilities.

Box 1.A: Discount rates

What is discounting?

Government accounting follows International Financial Reporting Standards (IFRS).

In general IFRS tries to measure assets and liabilities at exit values, which is the price at which the asset could be sold or a liability could be settled at today. To estimate this, expected future cash flows that will be earned from assets or paid out to meet liabilities are discounted to reflect the time value of money for investors.

Future cash flows are discounted because cash received today can be used to buy low risk assets that earn a return and mature when the money is needed for payment. The discount rates used are adjusted for inflation.

Any changes to the discount rate affect the value of assets and liabilities on the balance sheet even though the estimates of future cash flows are unchanged.

How are discount rates determined?

Public sector pensions

IFRS requires that pension liabilities are discounted based on the yields of high quality corporate bonds. For unfunded schemes the discount rate is set by HM Treasury using an index of corporate bond yields, with an adjustment to reflect that pensions are uprated by the Consumer Prices Index (CPI) and not the Retail Prices Index (RPI). For funded schemes the discount rate is determined by the actuaries for individual schemes using a market rate for high quality corporate bonds.

Provisions

Provisions are discounted at a risk free rate, which is taken to mean the return on government gilts adjusted for inflation. Three rates are set by HM Treasury to reflect different maturities - short, medium and long term. Short and medium term rates are updated annually. The long term rate was updated for the first time in 2015-16 following the Spending Review.

Student loans

Future cash flows are discounted at the government's long term cost of borrowing. The rate is updated at each Spending Review.

How have discount rates changed over the last year?

The applicable discount rates are set out below. With the exception of local government rates for pensions they have all been adjusted for inflation:

	Central government %		Local government %	
Section	2015-16	2014-15	**2015-16**	**2014-15**
Public sector pensions	**1.37**	1.3	**2.7 - 4.0 nominal**	3.0 – 4.4 nominal
Provisions:				
Short term	**-1.55**	-1.50	**-1.55**	-1.50
Medium term	**-1.00**	-1.05	**-1.00**	-1.05
Long term	**-0.80**	2.20	**-0.80**	2.20
Student loans	**0.70**	2.20	-	-

What do the changes mean for net expenditure?

Public sector pensions

The small increase in the discount rate has the effect of reducing the pension's liability and contributes to the gain on revaluation which is recognised in Other Comprehensive Income.

The only effect on net expenditure is an expense for unwinding the discount as all future cash flows are one year closer to payment. In 2015-16 this discount rate unwind resulted in an expense of £52.1 billion.

Provisions

The decrease in the long-term discount rate resulted in the value of future payouts in today's prices increasing by £125.2 billion. This has been recognised within net expenditure.

Student loans

The decrease in the long-term discount rate resulted in the value of future receipts in today's prices increasing. This has been recognised as a reversal to impairments that were previously recognised against expenditure on public services of £2.9 billion at the Department for Business, Innovation and Skills (BIS).

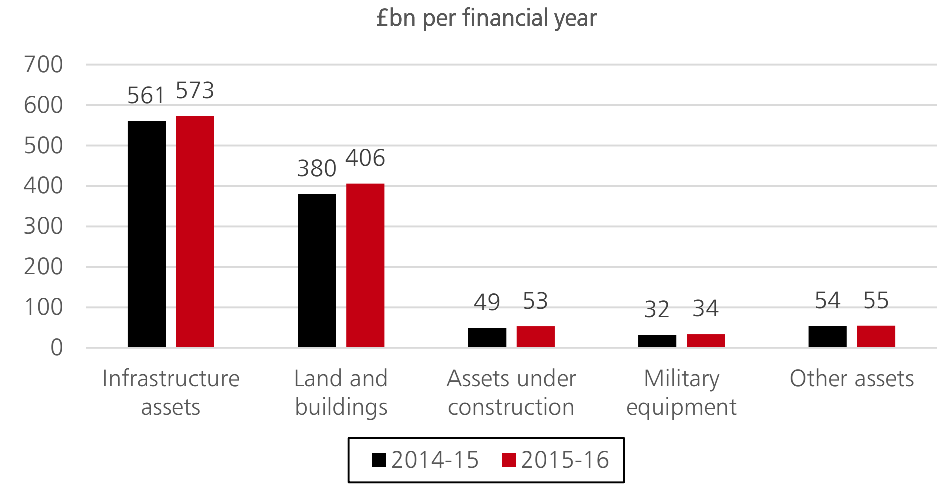
Assets

What are the most significant assets owned and controlled by government?
The most significant assets owned and controlled by government are **property, plant and equipment** (which includes land and buildings, infrastructure and military equipment), **financial assets** (which includes the investment in the public sector banks) and **trade receivables.**

		2015-16 £bn	2014-15 £bn
Property, plant and equipment	Note 12	1,120.2	1,075.8
Other financial assets	Note 16	373.0	365.5
Trade and other receivables	Note 15	154.7	145.9
Other assets	Notes 13, 14, 17, 18 (incl. gold and assets held for sale)	94.5	96.1
Total assets		1,742.4	1,683.3

Property, plant and equipment

Chart 1.J: Types of property, plant and equipment



1.50 Overall, the value of government's property, plant and equipment increased by £44.4billion or 4% in 2015-16. The most significant components of the government's property, plant and equipment are infrastructure assets and land and buildings which are reviewed in more detail below.

Infrastructure assets

1.51 The value of the government's infrastructure assets increased in value by 2% for the 2015-16 year. Table 1.B Breakdown of infrastructure ownership provides a further breakdown of the government's infrastructure assets. The most significant movements related to Scottish Water's estimate of the value of its infrastructure assets as a result of updates to geographical mapping of the type and location of assets held.

1.52 Central government and public corporations value their infrastructure assets at depreciated replacement cost. Local government on the other hand, values their assets, of which highways infrastructure is the most significant, based on historical cost. The differences in valuation method means that local authority infrastructure assets are likely to be understated by at least

£257.5 billion and therefore the local government share of infrastructure appears disproportionately small. Further information on the differences in valuation are included in the critical accounting policies in note 2 to the accounts.

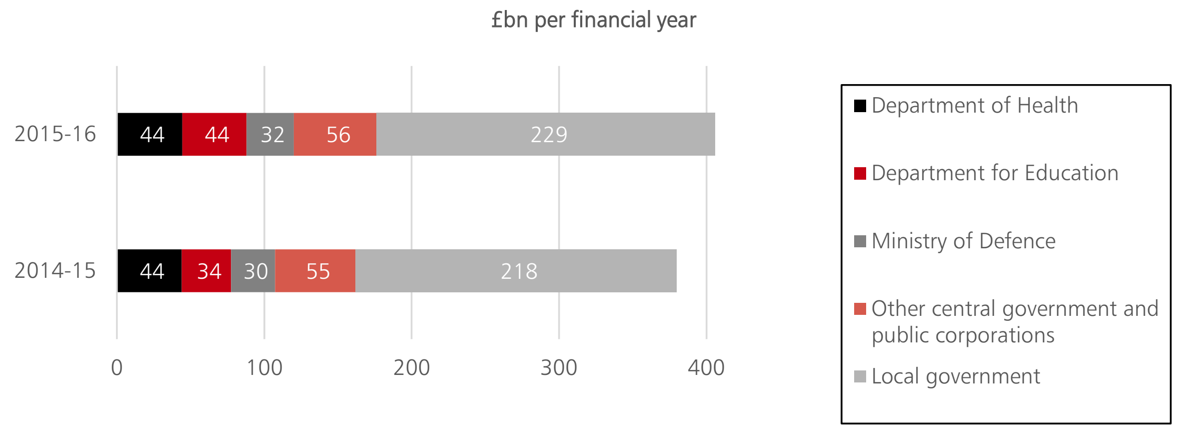
Table 1.B: Breakdown of infrastructure assets

Held by	**2015-16 £bn**	2014-15 £bn
Network Rail	280.1	278.1
Department for Transport	113.3	115.2
Scottish Water	52.2	41.8
Northern Ireland Department for Regional Development	24.5	27.0
Scottish Government	17.1	17.0
Welsh Government	14.8	15.2
Other	5.5	4.8
Total central government and public corporations	507.5	499.1
Transport for London	18.2	17.7
Highways infrastructure and other local government assets	46.9	44.4
Total local government	65.1	62.1
Total infrastructure assets	572.6	561.2

Land and buildings

1.53 The value of land, buildings and dwellings owned by government has increased by 7% compared to 2014-15. This movement is driven by a number of entities undertaking a periodic revaluation of assets as well as building additions across the whole of English local government.

Chart 1.K: Breakdown of government's estate



1.54 The government is establishing a new executive agency to own and manage government property, allowing it to better identify opportunities to obtain the best value for money for taxpayers. This new body will implement a commercially-driven approach to asset management and drive better strategic oversight and management of the estate. It is expected to commence operations in 2017-18.

1.55 The Cabinet Office are also leading a programme to rationalise the government's office estate from 800 buildings to fewer than 200 by 2023. As part of this, the government is set to move around 5,700 full time civil and public servants from offices in Whitehall to East London by the end of 2018.

Trade and other receivables

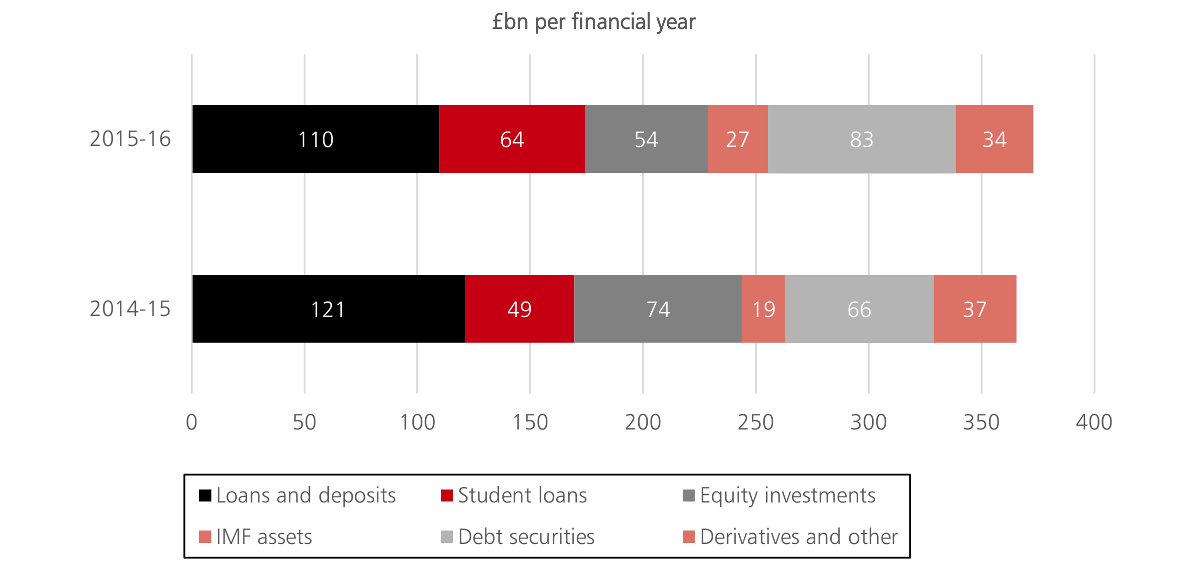
1.56 Trade and other receivables increased by £8.8 billion or 6% to £154.7 billion. Of this £5.9 billion relates to an increase in taxes and duties which are not yet due for payment. The increase is broadly in line with the increase in tax revenue for 2015-16. In addition, the provision for impairment of overdue taxes and duties decreased by £1.4 billion due to improved collection rates. Further information on the government's approach to debt management is included in the fraud, error and debt section of this performance analysis.

Other financial assets

1.57 As the chart below shows, the government holds a range of financial assets. Some are held as part of the government's normal operations to manage cash and foreign exchange risks. Others were acquired to support particular policy objectives. For example, student loans are provided to support access to education and loans and equity investments were acquired during the financial crisis to support financial stability.

1.58 The government's policy is to sell assets where it is value for money to do so and where there is no policy reason to continue to own them. Selling assets gives headroom for the government to invest in other policies with greater economic or social returns and reduces fiscal pressures. To support this policy, the government has set up UK Government Investments as a new centre of excellence in corporate finance and corporate governance, bringing together the functions of the Shareholder Executive and UK Financial Investments under a single holding company.

Chart 1.L: Types of other financial assets



Loans and deposits

1.59 Loans and deposits decreased by £11.3 billion (9%) in 2015-16, mainly due to the reduction in the UKAR mortgage loans. As a result of portfolio sales and redemptions the total UKAR mortgage loan assets decreased to £35.5 billion from £52.6 billion in 2014-15.

Debt securities

1.60 The government increased its holdings of foreign currency reserves during the year leading to an increase of £17.1 billion (26%) in debt securities.

Student loans

1.61 The carrying value of student loans held by government increased by £15.9 billion or 33% in 2015-16. Of this, £10.2 billion is attributable to net new lending as a result of higher student numbers. A further £3.7 billion is due to reversed loan impairments. Loan impairments were reversed as result of a change in HM Treasury's long term discount rate (see Box 1.A Discount Rates) and as a result of changes to the repayment threshold for post-2012 loans.

1.62 The value of student loans held by government at 31 March 2016 reflects an estimate of the present cost of subsidising interest on loans over the life of the loan (interest subsidy impairment) and an estimate of the future cost of policy write offs as not all of the loans issued will be recoverable due to the repayment terms offered (policy write off impairment). The carrying value of England only student loans, which makes up almost 90% of all student loans, was 75% of the face value of these loans. Further information on the valuation of student loans is included in note 2 to the accounts on critical accounting policies.

1.63 In February 2017 the government announced the process to start selling part of the English student loan book has begun. The sale of the student book is a part of the government's aim to sell publicly-owned assets in a way that secures good value for money for taxpayers and reduce fiscal pressures.

1.64 The sale will cover a selection of loans which entered repayment between 2002 and 2006 and it is expected to be the first of a planned 4-year programme of sales of loans issued before 2012, which is expected to return £12 billion to the Exchequer.

Equity investments

1.65 The value of the government's shares in Lloyds and RBS reduced by £21.0 billion (48%) due to share sales totalling £10.4 billion and revaluations and impairments totalling £10.6 billion.

1.66 The government remains committed to returning these assets, taken on in the financial crisis, to the private sector in a way that will maximise value for money for the taxpayer. During the 2016 financial year, the government disposed of £7.1 billion of shares in Lloyds and £2.1 billion of shares in RBS, reducing government's shareholding down to 9% and 72% respectively. Subsequent to 31 March 2016, the government has completely disposed of its shareholding in Lloyds.

Liabilities

What liabilities does government have?

Government borrowing comprises long-term borrowing in the form of gilt-edged securities (gilts), National Savings and Investments (NS&I products) and short-term borrowing in the form of Treasury bills.

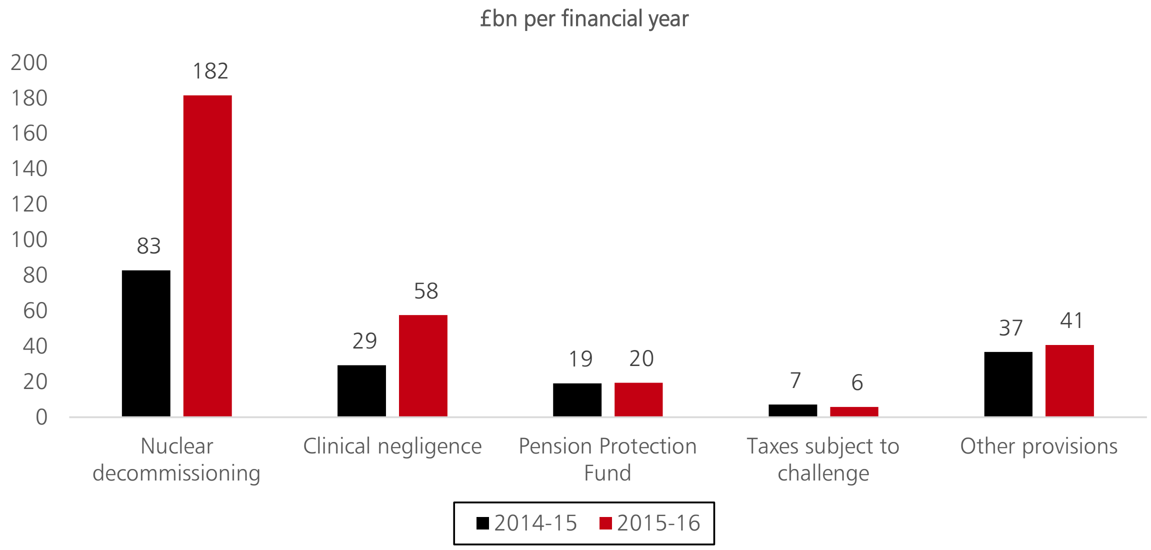
The government also has **public sector pension liabilities** and **provisions** which will be paid out in future years.

		2015-16 £bn	2014-15 £bn
Public sector pension schemes	Note 24	1,424.7	1,493.3
Government borrowings	Note 20	1,260.6	1,174.5
Other financial liabilities	Note 21	557.4	542.5
Provisions	Note 22	305.5	175.3
Trade and other payables	Note 19	180.2	172.9
Total liabilities		**3,728.4**	3,558.5

Provisions

1.67 The changes in the discount rate (see Box 1.A Discount rates) for long term provisions has led to a £125.2 billion increase in the value of the government's provisions. The effect is most significant on the two largest types of provisions, which are the provision for nuclear decommissioning and the provision for clinical negligence. The net increase in the value of provisions excluding the effect of the discount rate change was only £2.7 billion.

Chart 1.M: Movement in types of provisions

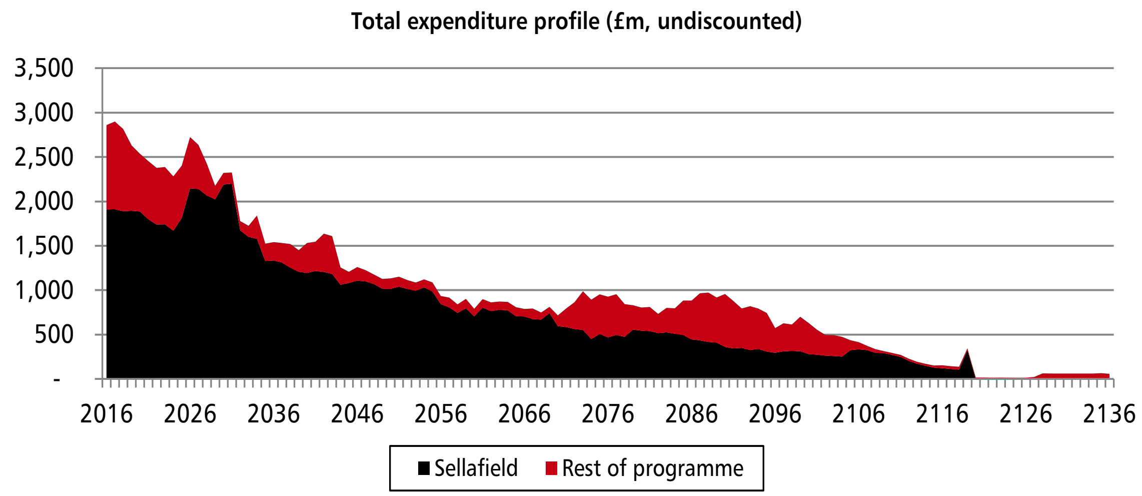


Nuclear decommissioning

1.68 The provision for nuclear decommissioning increased by £98.8 billion, from £82.9 billion in 2014-15 to £181.7 billion in 2015-16. The discount rate change accounted for £94.8 billion of the £98.8 billion increase in the value of the nuclear decommissioning provision. The discount rate change has a large effect on this provision because payouts are expected to occur over a long time period.

1.69 The chart below illustrates the expected profile of payouts by the Nuclear Decommissioning Authority which total £117.0 billion before discounting and £162.0 billion after discounting, and makes up the largest portion of the total provision of £181.7 billion. The remaining nuclear decommissioning provision of £19.7 billion is held by other bodies, including the Nuclear Liabilities Fund and the Ministry of Defence.

Chart 1.N: Nuclear decommissioning provision: expenditure profile for future years on NDA provision



1.70 The largest element of the government's nuclear decommissioning liability relates to Sellafield which comprises £117.4 billion of the £181.7 billion nuclear decommissioning provision. From 1 April 2016, the ownership of the organisation responsible for managing and operating Sellafield on behalf of the Nuclear Decommissioning Authority transferred from the private sector to the public sector. This new model enables better planning for the uncertainty that is inherent in handling such a complex site and provides benefits for managing long-term outcomes which extend beyond 2120. The aim is to increase the pace of progress, improve performance, including making use of partnerships with the private sector, and ensure a continued focus on the long-term clean-up mission.

Clinical negligence

1.71 The discount rate change accounted for £25.4 billion of the £28.3 billion increase in the value of the clinical negligence provision. Claims arising from another year of activity and changes in the assumptions used to calculate the provision increased the provision accounted for the remaining £2.9 billion increase.

1.72 The NHS Litigation Authority (now NHS Resolution) manages clinical and non-clinical claims against the NHS in England and in 2015-16 they recorded a 4.6% decrease in the number of new clinical claims reported compared to the prior year (2015-16: 10,965 claims, 2014-15: 11,497). In addition 4,172 non clinical claims were received compared to 4,806 in 2014-15.

Although the volume of new claims has decreased, the overall value of claims and corresponding provision has increased. The highest value of clinical claims received in 2015-16 was from the speciality area of obstetrics, continuing a year-on-year trend.

1.73 The NHS is taking action to reduce the incidence of harm and clinical negligence, for example through improved professional standards. 2015-16 was also the first full year of implementation of the Statutory Duty of Candour which requires NHS and independent health providers to give accurate, truthful and prompt information when mistakes are made and treatment does not go to plan, including apologising to the patient and offering further support.

1.74 Although claims volumes have decreased for two years in a row, it is likely that the overall cost of clinical negligence will continue to increase in the short-term. In February 2017 the Lord Chancellor announced a change to personal injury compensation payments. When individuals accept lump sum compensation payments for clinical negligence, the actual amount they receive is adjusted according to the interest they can expect to earn by investing it. The Lord Chancellor's announcement lowered this return from 2.5% to minus 0.75%, based on returns on the lowest risk investments, typically Index Linked Gilts.

1.75 Clinical negligence provisions increase each year as a consequence of a government decision to retain and manage these obligations rather than making one-off cash settlements, with each year seeing an addition to the provision from new claims in excess of the settlement of old claims, many of which will be settled over a period of several decades.

Pension Protection Fund

1.76 The Pension Protection Fund (PPF) provision relates to liabilities to pay compensation to members and claims from pension schemes. The PPF retains the assets of the pension plans it rescues and generates investment growth to support the obligations it acquires. At 31 March 2016, it had net investments of £23.4 billion, nearly £4.0 billion in excess of its liabilities.

Public sector pension schemes

1.77 At £1,424.7 billion, the largest liability in the 2015-16 WGA is the liability in respect of public sector pension schemes. This has decreased by £68.6 billion (5%) over 2015-16, reversing a previous trend of this liability increasing each year since 2010-11.

Discount rate changes

1.78 The main cause of the change in this liability each year is the annual change to the discount rate used to measure the liability - the "discount rate net of the consumer price index (CPI)". This discount rate is used because the value placed on the liability each year is based upon commitments from the schemes to make future benefit payments, which are generally indexed with CPI, discounted back to today's terms.

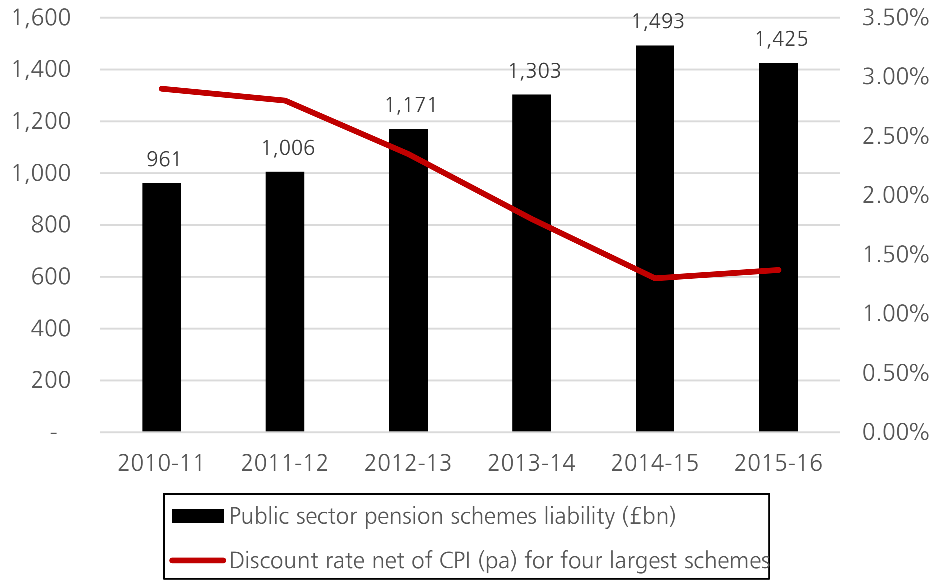
1.79 This discount rate generally has a significant impact on the liability because many of the benefit payments the schemes expect to make fall decades into the future, and so a small change in the (per annum) discount rate has a large impact on the liability.

1.80 As prescribed by the relevant accounting standards, the discount rate changes each year reflecting changes in the real yield on corporate bonds. An increase in the discount rate lowers the liability because future benefit payments are discounted by a higher amount.

1.81 Over three quarters of the public sector pension schemes liability relates to 4 of the largest (unfunded) schemes - those for the armed forces, civil service, teachers and the NHS. The chart below illustrates how the trend in the discount rate for these schemes compares with the trend in the public sector pension schemes liability over recent years. It shows that a small increase in the discount rate over 2015-16 corresponds with a small drop in the liability. Over the previous 4 years, from 2011 to 2015, three larger reductions in the discount rate correspond to three larger increases in the liability. Similarly over 2010-11 a small reduction in the discount rate matched a small increase in the liability.

1.82 The discount rate for the year 2016-17 has been set at 0.24% pa (a large drop from 1.37% pa) with individual entities currently preparing their 2016-17 resource accounts. We therefore anticipate an increase of around £300 billion in the reported public sector pension scheme liability when the 2016-17 WGA is published next year solely as a result of this change in the rate used to estimate a current value for the long-term liability.

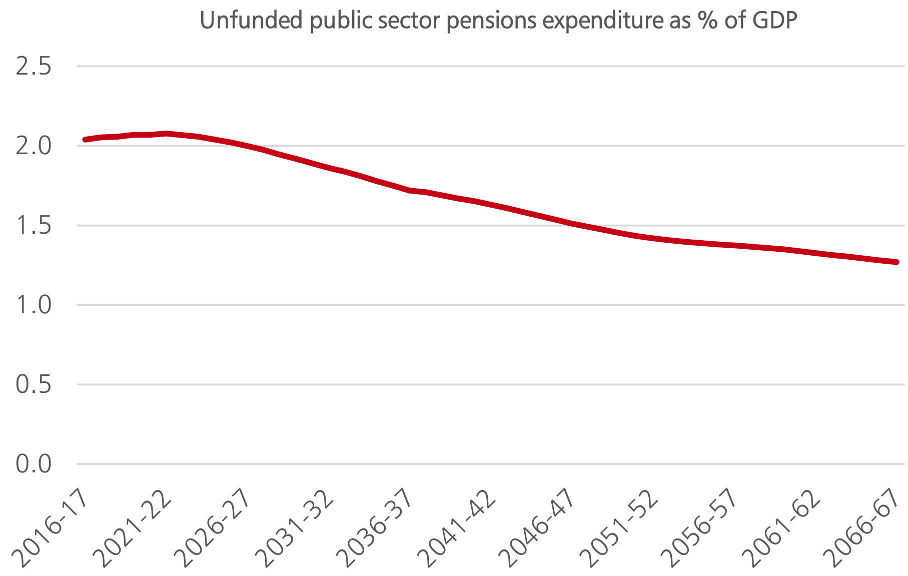
Chart 1.O: Discount rate trend



Affordability of public sector pensions and pension reforms

1.83 While annual changes in the discount rate drive changes in the balance sheet valuation of the public sector pension liability, setting aside future CPI growth, the discount rate has no bearing on the future benefits payable. The government therefore focuses on other measures to assess the overall fiscal implications, and manage the fiscal risks associated with, the public sector pension schemes. For example, when monitoring the fiscal implications of the schemes the government considers the Office for Budget Responsibility's (OBR) long term projections of public sector pension scheme expenditure published in their Fiscal Sustainability Reports (FSRs). The chart below shows the most recent such projection made in the January 2017 FSR:

Chart 1.P: Expenditure



1.84 This chart shows that spending on unfunded public service pensions is projected to fall gradually from around 2% of GDP to below 1.5% of GDP over the next fifty years. There are various reasons for this fall – including the impact of both historic and recent reforms.

1.85 In recent years, to address the fiscal pressures that will result from an ageing population, to rebalance taxpayer and member contributions and to ensure that the schemes are sustainable, the government has implemented a package of public sector pension scheme reforms to reduce their costs. These reforms included ending final salary pension schemes, aligning normal pension age with the state pension age; increasing member contribution rates and changing indexation arrangements from the retail price index (RPI) to the consumer price index (CPI).

1.86 These reforms built on the more historic reforms implemented midway through the 2000s, the effects of which will also emerge over future decades. With the exception of the police, firefighters and armed forces these reforms generally increased normal pension ages from 60 to 65. These reforms also changed the way benefits accrue and introduced retirement lump sum options to bring more consistency across all the schemes.

1.87 To manage the fiscal risks associated with the public sector pension schemes, alongside the reforms, the government introduced a mechanism to cap the cost of each of the reformed pension schemes. This mechanism is embedded within the regular valuations of the schemes (used to set the schemes' employer contribution rates) which take place on a 4 year cycle (or three year for the local government pension schemes). [5] Unlike the discount rate used in WGA, these valuations use a more stable discount rate linked to the OBR's expected rate of long term GDP growth, which is reviewed every 5 years.

1.88 The caps were set when the first valuations of the reformed pension schemes were carried out alongside the introduction of the reformed pension schemes. The mechanism requires the costs of these schemes to be assessed against the caps at the next, and each subsequent, valuation. The current valuations (effective date 2016) are currently underway with outcomes of the first tests against the caps anticipated before 2019. If tests indicate costs (ignoring discounting effects) have increased/decreased then members will have to pay more/less, or

[5] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/289366/public_service_pensions_actuarial_valuations_130314.pdf

future benefit accruals will be reduced/increased thereby ensuring that the costs to taxpayers remain as envisaged when the reformed schemes were established.

1.89 The alignment of the schemes' normal pension ages with the state pension age, coupled with the link between state pension age and life expectancy also helps manage the fiscal risks these schemes bring - specifically the risk of increasing costs through increasing life expectancy.

Other factors impacting public sector pensions

1.90 In addition to the increase in the discount rate, two other factors contributed to the decrease in the pension liability in 2015-16. The first of these was a change to short-term assumptions, largely due to extending the period during which pay restraint is assumed. This contributed around £20 billion to the decrease. The second was a change to mortality assumptions whereby the rate of future improvements is expected to be slower. This contributed around £23 billion to the decrease.

Government borrowing

1.91 The total nominal value of central government wholesale debt (excluding government holdings) in end-March 2016 was £1,260.6 billion, up from £1,174.5 billion end-March 2015. The market value weighted average maturity of the portfolio increased slightly in 2015-16, from 16.4 years to 16.6 years.

1.92 When setting strategy for government borrowing, a number of risks are taken into account. These include interest rate risks, refinancing risk, inflation risk, liquidity risk and execution risk. Extending the maturity of government debt is part of an expressed objective to mitigate refinancing risk. Details of the government's debt management strategy and financing plans for 2015-16 were set out in the 'Debt and reserves management report 2015-16', HM Treasury, March 2015, available at https://www.gov.uk/government/publications/debt-and-reserves-management-report-2015-to-2016.

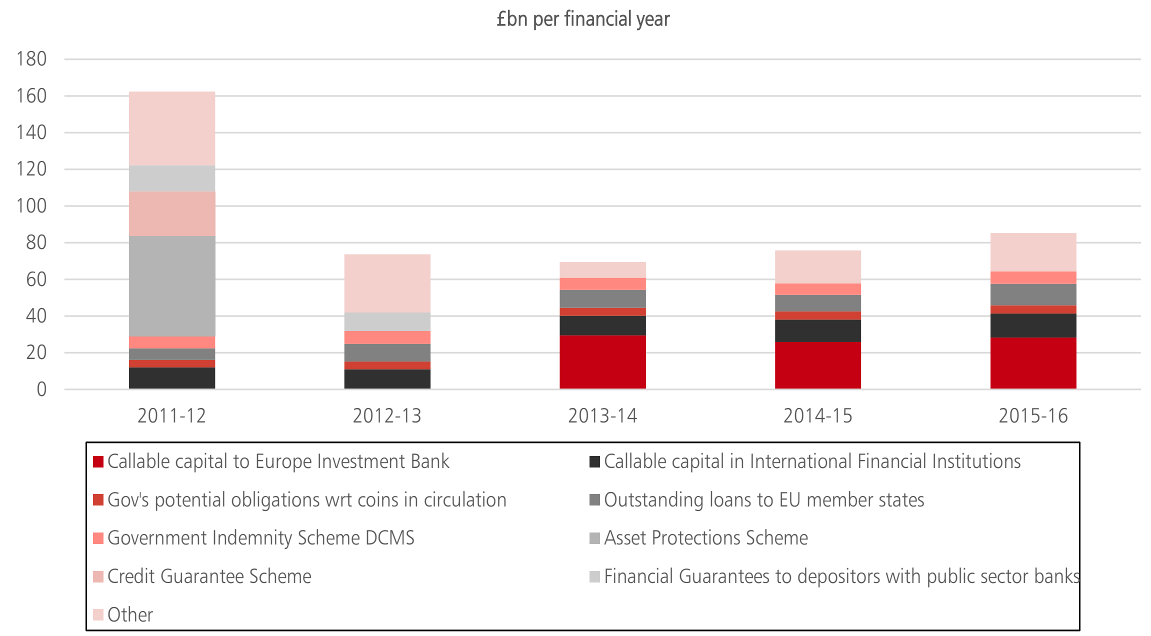
Other key matters

Contingent liabilities

1.93 In the past 5 years total quantifiable contingent liabilities (remote and non-remote) have fallen from £263.2 billion in 2011-12 to £189.6 billion in 2015-16, driven by a fall of £77.1 billion in the remote contingent liabilities. However, the same period has seen a rise of £3.5 billion in the non-remote contingent liabilities, which are more likely to crystallise.

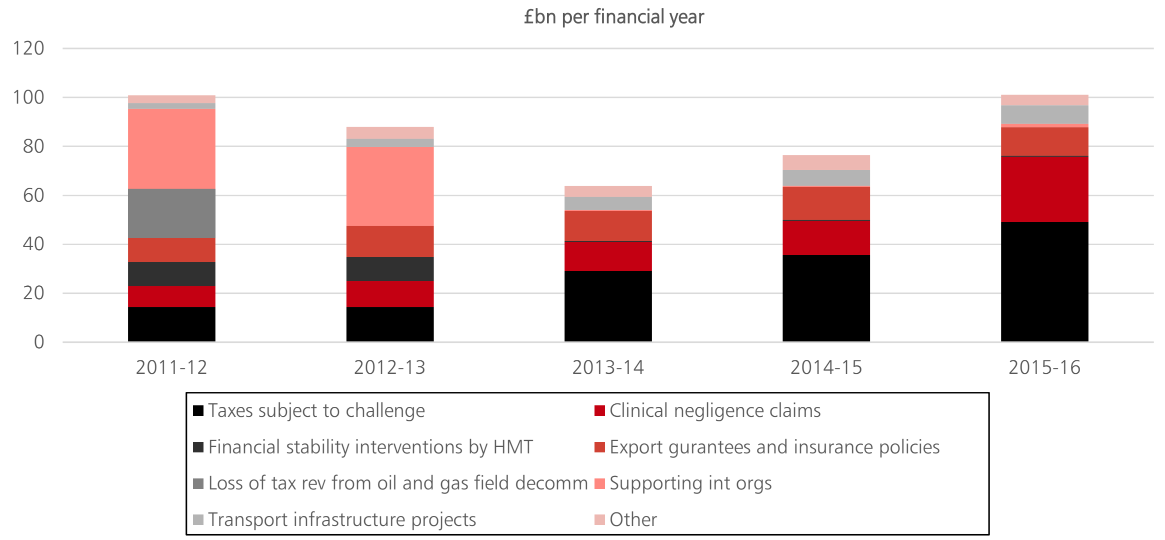
1.94 The £77.1 billion (47%) fall in remote contingent liabilities of over this period is mainly the result of the closure of financial stability schemes set up during the global financial crisis, such as the credit guarantee scheme and asset protection scheme, as can be seen in the chart below.

Chart 1.Q: Remote contingent liabilities by type



1.95 Increases in the non-remote quantifiable contingent liabilities were mainly due to increases in the categories of clinical negligence and taxes subject to challenge, resulting in a £3.5 billion (3%) increase over the last five years, as can be seen in the chart below.

Chart 1.R: Non-remote contingent liabilities by type



1.96 Where the time value of money is material, contingent liabilities which are required to be disclosed under the terms of the accounting standards are stated at discounted amounts. The change in the long term discount rate (see Box 1.A Discount rate) has been the main contributing factor in the 91% increase in the clinical negligence contingent liabilities.

1.97 The increase of 38% in the value of the contingent liabilities on taxes subject to challenge is due to the revision and reclassification of estimates for cases currently in litigation, taking into account court decisions during the year and interest that would be payable on final settlements.

1.98 In addition to the quantifiable contingent liabilities, the government has entered into a number of contingent liabilities where the size of the liability could either not be determined with reasonable certainty or to quantify it would jeopardise the outcome of any legal proceedings. The details of the most significant non-quantifiable contingent liabilities are included in notes 29 and 30 the financial statements in Chapter 5.

1.99 HM Treasury is looking to enhance and strengthen its approach in relation to the scrutiny and management of all contingent liabilities. The department has introduced stricter controls for approving new contingent liabilities. These include a rigorous review of alternatives options, the duration and size of the government's exposure, what could cause the contingent liability to crystallise, whether this would be affordable, and what governance arrangements will be in place to manage the risks associated with the contingent liability.

Fraud, error and debt

Fraud and error in the Welfare system

1.100 Significant areas of fraud and error expense within central government relate to overpayments of welfare benefits, pensions and personal tax credits administered by the Department for Work and Pensions (DWP) and HM Revenue and Customs (HMRC). Both DWP and HMRC saw a rise in levels of fraud and error in their last measurement exercises. This follows a number of years where the levels of fraud and error had been reducing.

Table 1.C: Reported rates of fraud and error

		2015-16	2014-15	2013-14	2012-13	2011-12
DWP	Overpayments as a percentage of benefit payments	1.9%	1.8%	2.1%	2.1%	2.1%
	Net overpayments after recoveries have been offset	1.2%	1.2%	1.5%	1.6%	1.6%
HMRC	Fraud and error as a percentage of finalised personal tax credits entitlement	5.5%	4.8%	4.7 %	5.3%	7.3%

1.101 Within DWP, the value of overpayments in 2015-16 was £3.3 billion, where around £1.0 billion of overpaid benefit was recovered by the department and local authorities during the same period. Universal Credit is forecast to bring through a reduction in fraud and error across welfare. DWP has a long-term fraud, error and debt strategy and has also set out their strategy for reducing fraud and error for each benefit. They are focusing on Housing Benefit and Pension Credit, which account for over 50% of the money lost as well as new welfare benefits including Universal Credit and Personal Independence Payments. Further details on DWP's strategy are included in the Accountability Report of DWP's 2015-16 Annual Report and Accounts.[6]

1.102 Fraud and error for 2015-16 in HMRC-administered tax credits was 5.5% of expenditure or £1.6 billion (2014-15: 4.8% of expenditure or £1.4 billion). This is against the challenging backdrop of the end of tax credits and the transition of staff and customers to Universal Credit. HMRC will continue to develop insight into the different error and fraud risk groups, using a range of data sources to select the right cases for action, and delivering large-scale checks on those cases where HMRC believe the award could be wrong.

Management of debt owed to government

1.103 Government's trade and other receivables totalled £154.7 billion as at 31 March 2017 and a more detailed breakdown of this balance can be found in note 15 to the financial statements. The majority of debt is paid on time and at the reporting date an estimated £24

[6] https://www.gov.uk/government/publications/dwp-annual-report-and-accounts-2015-to-2016

billion was overdue. Around 99% of overdue debt is held by HMRC, DWP and the Ministry of Justice. Debt owed to these departments includes overdue tax liabilities, benefit or tax credit overpayments, outstanding fines and court confiscation orders.

1.104 The government has taken steps in response to the recommendations made in the National Audit Office report, 'Managing debt owed to central government', published in February 2014. Each department now has its own debt management strategy and collects data on a consistent basis in order to facilitate comparison between departments and over time.

1.105 The government is also developing a cross-government debt management strategy to set out a more consistent and strategic approach to debt management. One example of this is the transfer of tax credit debt from HMRC to DWP for claimants who have moved to Universal Credit.

Events since 31 March 2016

1.106 Since the accounts of the individual entities that form WGA were prepared, there have been a number of events that could have a bearing on the Statement of Financial Position as at 31 March 2016. These events are shown in note 32 to the accounts.

Julian Kelly
Accounting Officer

7 July 2017

2 Statement of Accounting Officer's responsibilities

2.1 Under section 9 of the Government Resources and Accounts Act 2000 (the GRAA), HM Treasury is required to prepare, for each financial year, a consolidated set of accounts for a group of entities, each of which appears to HM Treasury:

- to exercise functions of a public nature
- to be entirely or substantially funded from public money

2.2 The account is prepared on an accruals basis and in accordance with the GRAA and the 2015-16 Government Financial Reporting Manual (FReM) which applies EU adopted International Financial Reporting Standards (IFRS) as adapted or interpreted for the public sector. The accounts must give a true and fair view of the whole of government's finances.

2.3 In preparing the accounts, the Accounting Officer is required to comply with the requirements of the FReM, and in particular to:

- observe the relevant accounting and disclosure requirements and apply suitable accounting policies on a consistent basis
- make judgements and estimates on a reasonable basis, including those judgements involved in consolidating accounting information provided by different sectors
- state whether applicable accounting standards, as set out in the FReM, have been followed, and disclose and explain any material departures in the accounts
- prepare the accounts on a going concern basis

2.4 In addition to these responsibilities, and specifically with regard to Whole of Government Accounts (WGA), the Accounting Officer is responsible for:

- drawing up WGA in accordance with the GRAA
- ensuring that WGA complies with the FReM and generally accepted accounting practice
- agreeing the process of producing WGA and for ensuring that relevant data are collected and accurately and appropriately processed
- ensuring that there is an appropriate control environment for the production of WGA

2.5 The responsibilities of an Accounting Officer are set out in Managing Public Money published by HM Treasury and include the need for efficiency, economy, effectiveness, and prudence in the administration of public resources to deliver value for money.[1]

2.6 The WGA Accounting Officer is responsible for signing the WGA Governance Statement. When signing the Governance Statement, the WGA Accounting Officer places reliance on the assurances made for each individual entity by the Accounting Officer or their equivalent, as documented through the Governance Statement for those bodies.

[1] http://www.hm-treasury.gov.uk/psr_mpm_index.htm

3 Governance statement

Scope of Accounting Officer's responsibility

3.1 As Accounting Officer, I am responsible for maintaining a governance framework to support the efficient and effective production and audit of the Whole of Government Accounts (WGA). The framework is designed to minimise the risks to the process of preparing and publishing the consolidated accounts. The accounts of individual entities consolidated within WGA are subject to their own governance frameworks including Accounting Officer or equivalent controls.

3.2 The framework is intended to manage risk to a reasonable level rather than to eliminate all risk of failure to the consolidation and preparation process. It provides reasonable, but not absolute, assurance of effectiveness. The governance framework is based on an ongoing process, designed to identify and prioritise the risks, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently.

3.3 Publication of WGA is managed within HM Treasury's overall risk management framework, which is set out in the department's annual report and accounts. The Deputy Director for Government Financial Reporting is responsible on a day-to-day basis for managing risk and for ensuring that the activities necessary for the production of these accounts are properly planned, resourced and performed.

3.4 In producing WGA, I must rely on the accounting officer (or equivalent) of each entity to manage their own risks. In some instances, the risks from underlying accounts may have a significant impact on the WGA consolidation and preparation process. The major risks identified from the underlying accounts are set out in paragraphs 3.14 to 3.16 below. The key risks in the preparation of WGA include:

- inaccuracies in entities' WGA returns, resulting in materially misstated balances
- failure to provide data or delays in the submission of WGA returns
- non-elimination of intra-group transaction streams and balances, resulting in materially misstated figures in the accounts

3.5 HM Treasury has put in place a risk management framework to manage the key risks to the WGA consolidation and preparation process. This includes maintenance and regular review of a risk register to assist in identifying and implementing mitigating actions. HM Treasury also maintains a control and validation framework to define the controls over the preparation of the accounts and to monitor the effectiveness and completeness of the controls in place.

3.6 The WGA governance framework has been in place for the year ended 31 March 2016 which this account reports on and the full period of account preparation up to the date of approval. The governance accords with HM Treasury guidance, including the 'Corporate Governance in Central Government: Code of Good Practice', to the extent that it is deemed relevant and practical. The control and validation framework was provided to the HM Treasury Group Audit Committee who confirmed it provided a good basis of assurance.

The WGA governance framework

3.7 I receive support and assurance on the management of risks in a number of ways:

- the **HM Treasury Group Audit Committee**, chaired by a non-executive member and supported by the Treasury's internal audit function, reviews the department's approach to internal control and provides independent advice, with oversight of financial reporting and risk management activities associated with WGA. The effectiveness of the audit committee is assessed in the HM Treasury Annual Report and Accounts
- as well as the internal framework of governance and risk management, the WGA is subject to external audit provided by the **Comptroller & Auditor General**, supported by staff from the National Audit Office. The Comptroller & Auditor General is independent, and reports his findings on the accounts to Parliament. More information about the respective responsibility of the auditor and preparer can be found in the Comptroller & Auditor General's audit certificate. The Comptroller & Auditor General and his staff have access to all HM Treasury papers and attend HM Treasury's Audit Committee

3.8 In April 2017 I disbanded the WGA Advisory Group. The group had previously provided me with advice on issues relating to the accounts and provided great support in championing WGA. Although the group will no longer meet on a regular basis, I will still look to draw on the skills and experience of the wider finance community, for example through technical working groups for particular issues. At the same time I have sought input and advice from the Financial Reporting and Advisory Board on the strategy for WGA and how to improve the presentation of the account.

Improvements in preparing WGA

3.9 Part of the challenge of producing such a comprehensive consolidation as WGA is the time it takes to receive audited returns covering over 6,000 organisations and to consolidate these returns into an accurate and understandable format. The Treasury's short-term target is to publish WGA within 12 months of the year-end. Longer-term, the ambition is to publish the account earlier and there are already initiatives in place to support this, for example the deadline for local authorities to produce their audited accounts will be moving forward by two months from 2017-18.

3.10 WGA is based on International Financial Reporting Standards (IFRS), the method of accounting used internationally by the private sector. WGA is independently audited by the National Audit Office. As can be expected from a consolidation of this scale, WGA has received audit qualifications each year since it was first produced. The Treasury is making steady progress in removing them. This year the qualification on inconsistent accounting policies has improved as a result of an updated valuation of Network Rail's railway asset and the qualification on the elimination of intra-government transactions and balances has been fully removed.

How WGA is being used

3.11 This is the seventh year of WGA and it is being increasingly used to support decision making and manage risks more effectively. Some examples are:

- the Office for Budget Responsibility (OBR) independently reports on the future sustainability of the public finances in its annual Fiscal Sustainability Report, drawing on the data published in WGA
- the Treasury uses WGA data to monitor balance sheet risks and contingent liabilities
- the Treasury uses WGA data for analysing operating expenditure across government departments and identifying opportunities for savings, for example by informing the government's property strategy

3.12 Publication of WGA also supports the government transparency agenda to make more public data available. In their recent evaluation of the UK, the International Monetary Fund highlighted the strength of the UK's reporting, concluding that WGA and the government's other fiscal reports place the UK at the forefront of fiscal reporting practices worldwide. [1] WGA is independently audited giving both Parliament and the outside world greater confidence in the figures, and supports effective scrutiny by Parliament through the Public Accounts Committee.

Review of effectiveness

3.13 The 2015-16 WGA has been qualified as a result of qualifications in the underlying accounts and as a result of issues relating to the boundary and accounting policies applied by the Treasury when carrying out the WGA consolidation.

(a) Addressing significant governance issues in underlying accounts

3.14 The underlying accounts and WGA data submissions show significant governance issues in a small number of entities that have resulted in audit qualifications. These weaknesses are the responsibility of the relevant accounting officer (or equivalent) and cannot be managed by the WGA Accounting Officer. Internal control weaknesses that led to qualifications (other than regularity) are also considered for their impact on WGA.

3.15 Those qualifications that are material to WGA are summarised below:

- The Department for Education received an adverse opinion on their 2015-16 accounts. The principal reason behind the adverse opinion was the academy year end of August and the increasing divergence between this data and the estimations used by the department to convert to a March year end. In addition, a material and pervasive level of error was identified in the opening balances and prior period comparatives included in the group account. From 2016-17 onwards the Department and HM Treasury will be trialling a new methodology that may be more suitable for WGA
- the Ministry of Defence has not applied IFRIC 4 'Determining whether an Arrangement Contains a Lease' to all of its contracts. It is believed that a limited number of significant, largely single source contracts, particularly strategic procurement arrangements with key contractors, would meet the IFRIC 4 definition of containing a lease if they were reviewed against IFRIC 4; and that some of these leases would meet the definition of a finance lease per IAS 17 'Leases'. The impact on the financial statements of not applying IFRIC 4 is that contractors' assets held

[1] https://www.imf.org/en/Publications/CR/Issues/2016/12/31/United-Kingdom-Fiscal-Transparency-Evaluation-44395

under finance leases and the associated liabilities have been excluded from the Statement of Financial Position. Consequently, the Comptroller & Auditor-General qualified his opinion on the accounts of the Ministry of Defence on the basis that a material value of leased assets and liabilities were omitted from its Statement of Financial Position

- both DWP and HMRC's accounts received qualified audit opinions due to the level of fraud and error being material to the overall audit opinion on the regularity of the accounts

3.16 In addition to the qualifications above, the Comptroller & Auditor General disclosed an emphasis of matter without qualifying his opinion in relation to the following items:

- the Department of Health 2015-16 accounts included an emphasis of matter relating to the uncertainties inherent in the claims provision for the clinical negligence scheme for NHS Trusts and the Nuclear Decommissioning Authority accounts included an emphasis of matter statement on the uncertainty inherent in the valuation of the provision for nuclear decommissioning. Given the long-term nature of these liabilities and the number and nature of the assumptions on which the estimate is based, a considerable degree of uncertainty remains over their valuation

- the Department for Business, Innovation and Skills accounts included an emphasis of matter relating to the uncertainty inherent in the valuation of student loans. This was due to the long term nature of the recovery of the loans, the number and volatility in the assumptions underpinning their valuation in the accounts

(b) Addressing significant governance issues in the WGA consolidation process

3.17 The qualifications which arise from the consolidation process are those relating to the boundary and accounting policies. The boundary qualification will remain as long as the Royal Bank of Scotland (RBS) is in public ownership. The qualification on inconsistent accounting policies mainly relates to different methods used in valuing infrastructure assets. The 2015-16 WGA includes a depreciated replacement cost valuation of the railway asset for the first time which represents significant progress. The largest difference remaining is the valuation of the local authority road network. The Treasury is working with the body which sets accounting standards for local authorities on a plan to obtain this information. Further details on both of these qualifications are included in the critical accounting policies in note 2 to the accounts.

3.18 Up until 2014-15, WGA was qualified because the balances and transactions between consolidated bodies were not eliminated in full. In last year's account, improvements to the eliminations process meant that the year-end intra-group balances were materially correct for the first time and the qualification was limited to intra-group income and expenditure streams. This year the Treasury undertook further analysis to demonstrate that all intra-group transactions were materially correct which has led to the successful removal of this qualification.

3.19 Further improvements will be made as experience of producing and using WGA grows. These will focus on improving the accuracy of the data collected at the local level to minimise the corrective work in the centre. Plans are being developed to increase the speed of account production to within 9 months of the year end.

3.20 I have assessed the WGA compliance with the Corporate Governance in Central Government Departments Code of Good Practice. I believe that we comply with the provisions of the Code that are relevant to my responsibilities to prepare WGA.

3.21 I am satisfied that effective remedial action is being taken to address the remaining control issues and that action taken so far is beginning to yield positive results. However, some improvements may take several years to implement fully. In part, this is because lessons are being learned after the accounts of the previous year have been completed. I have procedures in place to monitor the progress being made to tackle these weaknesses.

(c) Assurance in making this judgement

3.22 I have considered the evidence that supports this governance statement and I am assured that the Treasury has a strong framework of controls to support the production of WGA.

HM Treasury's role in managing financial risk

3.23 In addition to the WGA governance framework, HM Treasury also has a role in managing the government's financial risk more widely, although this is outside the responsibility of the WGA Accounting Officer. Financial risk is managed in a number of ways, including:

- **the Managing Public Money framework** – provides departments with guidance and sets out requirements on how to handle public funds properly
- Spending Reviews – the process through which spending is allocated to areas of government activity including public services, social security, and administration costs, according to the government's priorities. Spending Reviews set firm and fixed spending budgets over several years for each department
- **the budget and estimates process for central government departments** - the government uses the annual budgeting system to plan and control public expenditure. The Treasury presents estimates of budgetary plans to Parliament to obtain the statutory authority to consume resources and spend cash. The budgetary system has two main objectives:
  - to support the achievement of macro-economic stability by ensuring that public expenditure is controlled in support of the government's fiscal framework
  - to provide good incentives for departments to manage spending well so as to provide high quality public services that offer value for money for the taxpayer
- the Treasury sets the **financial reporting framework** for central government and works with the other relevant authorities such as CIPFA Local Authority (Scotland) Accounts Advisory Committee (LASAAC) for financial reporting across government and the Financial Reporting Advisory Board, to set best practice accounting standards
- **the Treasury spending teams** provide strategic challenge to, and monitoring of, departments' spending on an ongoing basis
- the **Treasury's Fiscal Group** is responsible for ensuring the sustainability of the public finances over the short, medium and long term, including management of key financial assets and liabilities on the public sector balance sheet

Information and data handling

3.24 In preparing WGA, HM Treasury does not collect any personal data from WGA entities. WGA data collected from WGA entities are held on HM Treasury's Online System for Central Accounting and Reporting (OSCAR) database. Data is published on http://www.data.gov.uk as part of a scheduled release of OSCAR data.

Disclosure of information to auditors

3.25 As Accounting Officer, I confirm that there is no relevant audit information of which the National Audit Office is unaware. I have taken all the necessary steps to make myself aware of any relevant audit information and to establish that the National Audit Office is aware of that information.

3.26 I confirm that this annual report and accounts 2015-16 is, as a whole, fair, balanced and easy to understand. I take personal responsibility for the annual report and accounts, including the judgements required for determining that it is fair, balanced and easy to understand.

Julian Kelly
Accounting Officer

7 July 2017

4 Remuneration and staff report

Remuneration report

4.1 Remuneration reports produced by Whole of Government Accounts (WGA) entities contain information about senior employees' salaries, bonuses, benefits in kind and pension entitlement, but a similar report for WGA would require publishing details of senior employees for over 6,000 entities. This remuneration report therefore does not follow the same format as the remuneration reports of WGA entities. Instead it sets out the government's policy on public sector pay, summarises the remuneration arrangements of the main public sector workforces and includes some statistics on pay across the public sector.

Government policy on public sector pay

4.2 The 1% pay award is an average that applies to an organisation or workforce, rather than each individual. This means that organisations are free to distribute the award among staff based on their own requirements. Employers may decide to allocate more to specific parts of its workforce provided the average increase in the annual award for the organisation's total pay remit is in line with the pay policy. The pay restraint policy applies to the Pay Review Body workforces and the Civil Service and associated bodies. The government does not control pay in public corporations or local government. The Local Government Association announced that the majority of employees will receive an uplift of 1% in April 2016 and April 2017.

Remuneration in main public sector workforces

Pay review bodies

4.3 For much of the public sector, pay awards are set by the government after receiving advice from the independent pay review bodies. Each year the review bodies take evidence from interested parties, including government departments and trade unions, carry out their own independent research, and then formulate recommendations on the remuneration of their particular workforce. The government then decides whether to accept, reject or stage the pay awards recommended by the review bodies.

4.4 The pay review bodies are:

- National Health Service (NHS) Pay Review Body – covering all NHS staff, excluding doctors, dentists and very senior managers
- Review Body on Doctors' and Dentists' Remuneration – covering hospital doctors and dentists, public and community health doctors, ophthalmic medical practitioners, general medical practitioners, general dental practitioners, and community dental and dental public health staff
- School Teachers' Review Body – covering school teachers in England and Wales
- Armed Forces' Pay Review Body – covering members of the Naval, Military and Air Forces of the Crown up to and including the rank of Brigadier (one star) or equivalent

- Prison Service Pay Review Body – covering prison staff in England, Wales and Northern Ireland and includes governors and other operational managers, principal and senior officer grades, and prison officer and support grades
- Senior Salaries Review Body – covering senior civil servants, members of the judiciary, senior officers in the armed forces, senior police, very senior managers in the NHS and police and crime commissioners
- the National Crime Agency (NCA) Remuneration Review Body – covering all NCA officers in the UK
- Police Remuneration Review Body – covering police officers in England and Wales

4.5 Pay for those working in NHS Foundation Trusts and academy schools is a matter for those organisations. However, in practice, the majority of these organisations choose to follow the relevant Pay Review Body recommendation.

Civil service pay policy

4.6 Pay policy for civil servants below the Senior Civil Service is delegated to departments, within overall parameters set by HM Treasury. Each year, the Treasury publishes pay guidance which sets out these parameters, and it is then for departments to agree their individual settlement with the trade unions, within those parameters.[1] These arrangements also cover many non-departmental public bodies where staff are not civil servants.

The devolved administrations

4.7 Where civil servants work for the devolved administrations, pay is a matter for these administrations. Reports on pay related matters affecting the devolved bodies may be sent to the First Ministers of the Scottish Parliament and The National Assembly for Wales, and the Presiding Officer of the Northern Ireland Assembly. Where civil servants work in UK departments, but are based in the devolved countries, and in instances such as the armed forces, pay is a matter for the UK government.

Local government[2]

4.8 Pay for local government workers is a matter for local government to determine. In practice, the pay and conditions for the vast majority of the local government workforce is set by the National Joint Council (NJC) for local government services. The NJC is a negotiating body comprising trade unions and employers. It sets a national pay scale, but it is for individual authorities to decide where to place employees on that scale or whether to opt out completely from that pay framework.

[1] https://www.gov.uk/government/publications/civil-service-pay-guidance-2015-to-2016/civil-service-pay-guidance-2015-to-2016

[2] Details of local government pay in England and Wales are available from the Local Government Association (LGA), which publishes an annual local government earnings survey on its website: www.local.gov.uk. An overview of English local government pay and workforce figures is published annually by the Department for Communities and Local Government in their report 'Local Government Financial Statistics England' available on its website: https://www.gov.uk/government/organisations/department-for-communities-and-local-government. Details of remuneration by local authority are available in their individual accounts and online.

Staff report

Staff costs (audited)

Table 4.A: Staff costs

	Permanently employed staff £bn	Others £bn	2015-16 Total £bn	2014-15 Total restated £bn
Salaries and wages	138.4	11.2	149.6	148.5
Pension scheme costs: current service costs (net of employees' contributions)	40.2	-	40.2	36.1
Pension scheme costs: past service costs	1.4	-	1.4	0.6
Pension scheme costs: losses on settlements and curtailments	(0.4)	-	(0.4)	(0.7)
Expenditure on external pension schemes	2.5	-	2.5	1.0
Total staff costs	182.1	11.2	193.3	185.5

4.9 Salaries and wages increased by £1.1 billion to £149.6 billion in 2015-16. Expenditure on NHS salaries and wages increased by £1.5 billion as a result of an increase in staff numbers, which has been offset by decreases in salaries and wages in other sectors. Scottish and Northern Ireland Further Education Colleges were included in WGA for the first time in 2015-16 leading to the inclusion of £0.6 billion of salaries and wages for which the comparative figures have not been restated.

4.10 'Others' included the cost of ministers, special advisers, temporary and contract staff. The cost of the salaries of ministers was £5.9 million (2014-15: £5.7 million) and the cost of special advisers was £8.9 million (2014-15: £10.2 million). The ministerial salary only includes the additional element on top of the basic salary of an MP.

4.11 Pension scheme costs increased by £5.2 billion in 2015-16 to £41.2 billion. These costs included expenses such as current service costs, past service costs, enhancements, gains/losses on settlements and curtailments. Further details are included in note 24 to the accounts.

4.12 Expenditure on external schemes increased by £1.5 billion in 2015-16 and this was mainly due to an increase of £1.1 billion at the Ministry of Defence where the range of employer basic contributions increased from 1 October 2015.

Median earnings

4.13 Median earnings across the public sector for the financial year 2015-16 for all employees are shown below.

Table 4.B: Median earnings

	Median earnings 2015-16 £	Median earnings 2014-15 £	Median earnings 2013-14 £
Central government civil service[3]	25,350	24,980	24,730
Local government[4]	-	20,194	19,582
Public sector[5]	25,002	24,686	24,294
Private sector[6]	22,500	21,703	21,293

Average number of persons employed

Table 4.C: Average number of full-time equivalent (FTE) persons employed during the year

	Permanently employed staff	Others	2015-16 Total	2014-15 Total
Central government (including health)	2,475,646	185,330	2,660,976	2,586,098
Local government	1,630,966	58,888	1,689,854	1,732,578
Non-financial public corporations	86,355	21,839	108,194	112,892
Financial public corporations	2,741	-	2,741	2,541
Total	**4,195,708**	**266,057**	**4,461,765**	4,434,109

Table 4.D: Central government breakdown

	2015-16 Total	2014-15 Total
Health sector	1,380,598	1,351,459
Academy schools	367,129	339,990
Northern Ireland and Scottish FE colleges	14,635	-
Other	898,614	894,649
Total central government (including health)	**2,660,976**	2,586,098

4.14 As shown in the tables above, within the central government staff numbers, health sector staff increased from 1,351,459 (2014-15) to 1,380,598 (2015-16); academy school staff increased from 339,990 (2014-15) to 367,129 (2015-16) of which some were previously included in local government staff numbers; the rest of central government increased from 894,649 (2014-15) to 913,249 (2015-16) due mainly to the inclusion of 14,635 staff in Northern Ireland and Scottish Further Education (FE) colleges for the first time in 2015-16 for which comparative figures have not been restated.

4.15 'Others' included 124 ministers (2014-15: 117) and 122 special advisers (2014-15: 151) working in central government.

[3] ONS Statistical Bulletin, Civil Service Statistics, 2016, 2015 and 2014 (www.ons.gov.uk)
[4] Local Government Earnings Survey, Summary 2013-14 and 2014-15 (http://www.local.gov.uk); data for 2015-16 has not yet been released
[5] Table 13.7a, Annual Survey of Hours and Earnings, 2016 (Provisional), 2015 (Revised) and 2014 (Revised), ONS (www.ons.gov.uk)
[6] Table 13.7a, Annual Survey of Hours and Earnings, 2016 (Provisional), 2015 (Revised) and 2014 (Revised), ONS (www.ons.gov.uk)

Civil Service and other compensation schemes - exit packages

Table 4.E: Exit package cost band 2015-16

	Number of compulsory redundancies	Number of other departures agreed	Total number of exit packages by cost band	Total Cost £bn
<£10,000	2,455	4,382	6,837	0.1
£10,000-£50,000	12,478	35,435	47,913	0.9
£50,000-£100,000[7]	781	4,658	5,439	0.3
>£100,000	297	1,490	1,787	0.2
Total	**16,011**	**45,965**	**61,976**	**1.5**

Table 4.F: Exit package cost band 2014-15

	Number of compulsory redundancies	Number of other departures agreed	Total number of exit packages by cost band	Total Cost £bn
<£10,000	2,068	3,754	5,822	0.1
£10,000-£50,000	13,349	37,812	51,161	0.9
£50,000-£100,000[7]	917	3,909	4,826	0.3
>£100,000	508	1,391	1,899	0.2
Total	16,842	46,866	63,708	1.5

4.16 The majority of these payments are made within the terms and conditions of exit schemes under the relevant remuneration framework. The government has committed to introducing two measures on public sector compensation: a cap on all public sector exit payments at £95,000; and a 'clawback' of redundancy compensation when a highly-paid individual returns to the public sector shortly after receiving an exit payment.

Julian Kelly
Accounting Officer

7 July 2017

[7] Local government packages of £40,000-60,000 are included in the band £50,000-100,000 as the local authority specific accounting requirements have different bands.

5 Financial statements

Statement of Revenue and Expenditure

For the year ended 31 March 2016

	Note	2015-16 £bn	2014-15 restated £bn
Taxation revenue	4	(592.6)	(566.7)
Other revenue	5	(101.3)	(93.2)
Total public services revenue		**(693.9)**	(659.9)
Social security benefits	6	222.5	217.7
Staff costs	7	193.3	185.5
Purchase of goods and services	8	192.1	191.7
Grants and subsidies	9	54.1	57.4
Depreciation and impairment	10	42.7	45.4
Interest costs on government borrowing	11	28.3	27.6
Increase in provisions	22	9.2	26.0
Total expenditure on public services		**742.2**	751.3
Net expenditure on public services		**48.3**	91.4
Financing costs of long-term liabilities, including discounting	11	187.4	65.1
Revaluation of financial assets and liabilities		8.1	(4.5)
Net expenditure for the year		**243.8**	152.0

Statement of Comprehensive Income and Expenditure

For the year ended 31 March 2016

	2015-16 £bn	2014-15 £bn
Net expenditure for the year	243.8	152.0
Other comprehensive income and expenditure:		
Net (gain)/loss on:		
Revaluation of property, plant and equipment	(31.0)	(22.2)
Revaluation of intangible assets	(0.3)	(0.6)
Revaluation of available for sale financial assets	0.4	(3.9)
Revaluation of pension scheme liabilities	(123.0)	134.7
Other comprehensive income and expenditure	**(153.9)**	108.0
Total comprehensive expenditure for the year	**89.9**	260.0

Statement of Financial Position

As at 31 March 2016

	Note	2015-16 £bn	2014-15 restated £bn
Non-current assets			
Property, plant and equipment	*12*	1,120.2	1,075.8
Investment property	*13*	15.8	14.9
Intangible assets	*14*	33.0	32.4
Trade and other receivables	*15*	14.4	12.7
Other financial assets	*16*	208.8	216.6
		1,392.2	1,352.4
Current assets			
Inventories	*17*	9.6	11.3
Trade and other receivables	*15*	140.3	133.2
Other financial assets	*16*	164.2	148.9
Cash and cash equivalents	*18*	25.8	26.8
Gold holdings		8.6	8.0
Assets held for sale		1.7	2.7
		350.2	330.9
Total assets		**1,742.4**	1,683.3
Current liabilities			
Trade and other payables	*19*	(114.7)	(108.8)
Government borrowings	*20*	(274.2)	(235.2)
Other financial liabilities	*21*	(452.5)	(444.2)
Provisions	*22*	(14.7)	(14.9)
		(856.1)	(803.1)
Non-current liabilities			
Trade and other payables	*19*	(65.5)	(64.1)
Government borrowings	*20*	(986.4)	(939.3)
Other financial liabilities	*21*	(104.9)	(98.3)
Provisions	*22*	(290.8)	(160.4)
Net public sector pension liability	*24*	(1,424.7)	(1,493.3)
		(2,872.3)	(2,755.4)
Total liabilities		**(3,728.4)**	(3,558.5)
Net liabilities		**(1,986.0)**	(1,875.2)
Financed by taxpayers' equity:			
General reserve		(2,504.4)	(2,379.7)
Revaluation reserve		514.5	501.0
Other reserves		3.9	3.5
Total liabilities to be funded by future revenues		**(1,986.0)**	(1,875.2)

The financial statements and supporting notes on pages 49 to 116 and annex A were approved by Julian Kelly as the Accounting Officer for WGA on 7 July 2017.

Julian Kelly
Accounting Officer
7 July 2017

Statement of Changes in Taxpayers' Equity

For the year ended 31 March 2016

	General reserve £bn	Revaluation reserve £bn	Other reserves £bn	Total £bn
At 1 April 2014	(2,099.7)	255.9	3.2	(1,840.6)
Net expenditure for the year ended 31 March 2015	(152.0)	-	-	(152.0)
Net gain/(loss) on:				
Revaluation of property, plant and equipment	-	22.2	-	22.2
Revaluation of intangible assets	-	0.6	-	0.6
Revaluation of available for sale financial assets	-	3.9	-	3.9
Revaluation of pension scheme liabilities	(134.7)	-	-	(134.7)
Other reserves movements including transfers	4.9	(7.8)	0.3	(2.6)
Balance at 31 March 2015	(2,381.5)	274.8	3.5	(2,103.2)
Restatements	1.8	226.2	-	228.0
Restated balance at 31 March 2015	(2,379.7)	501.0	3.5	(1,875.2)
Balance at 1 April 2015 (restated)	**(2,379.7)**	**501.0**	**3.5**	**(1,875.2)**
Net expenditure for the year ended 31 March 2016	(243.8)	-	-	(243.8)
Net gain/loss on:				
Revaluation of property, plant and equipment	-	31.0	-	31.0
Revaluation of intangible assets	-	0.3	-	0.3
Revaluation of available for sale financial assets	-	(0.4)	-	(0.4)
Revaluation of pension scheme liabilities	123.0	-	-	123.0
Other reserves movements including transfers	(3.9)	(17.4)	0.4	(20.9)
Balance at 31 March 2016	**(2,504.4)**	**514.5**	**3.9**	**(1,986.0)**

The general reserve includes the pension reserves. The revaluation reserve includes assets available-for-sale. Other reserves include the hedging reserve and reserves restricted for specific purposes.

Statement of Cash Flows

For the year ended 31 March 2016

	Note	2015-16 £bn	2014-15 restated £bn
Cash flows from operating activities			
Net operating expenditure	*SoRE*	(48.3)	(91.4)
Adjustments for non-cash transactions		115.9	80.5
(Increase)/decrease in inventories		1.9	(0.3)
(Increase)/decrease in trade and other receivables		(6.3)	10.1
Increase/(decrease) in trade and other payables		9.5	0.1
Use of provisions		(8.9)	(7.9)
Net cash inflow/(outflow) from operating activities		**63.8**	(8.9)
Cash flows from capital expenditure and financial investment			
Purchase of non-financial assets		(55.4)	(54.4)
Proceeds from disposal of non-financial assets		2.7	4.1
Purchase of financial assets		(88.0)	(74.8)
Proceeds from disposal of financial assets		77.4	72.3
Net cash inflow/(outflow) from capital expenditure and financial investment		**(63.3)**	(52.8)
Cash flows from financing activities			
Interest received		6.3	7.2
Financing costs of long-term liabilities, including discounting		(31.0)	(33.0)
Finance charges paid on finance leases and PFI contracts		(4.7)	(3.1)
Net Borrowings		27.9	90.5
Net cash inflow/(outflow) from financing activities		**(1.5)**	61.6
Net increase/(decrease) in cash and cash equivalents	*18*	**(1.0)**	(0.1)
Cash and cash equivalents at the beginning of the year	*18*	26.8	26.9
Cash and cash equivalents at the end of the year	*18*	**25.8**	26.8

Notes to the Accounts

Note 1. Statement of accounting policies

1.1 Basis of preparation

The financial statements have been prepared in accordance with the 'Government Resources and Accounts Act 2000' (GRAA) and International Financial Reporting Standards (IFRS), as adapted and interpreted by the Financial Reporting Manual (FReM). A number of public bodies consolidated into these financial statements do not follow the FReM. For example, local authorities follow the IFRS-based Code of Practice on Local Authority Accounting. Adjustments are made on consolidation to harmonise accounting policies where material and any exceptions are noted in these accounting policies.

In adopting the going concern basis for preparing the financial statements, the Accounting Officer has considered the Government's power to set tax rates to meet its funding requirements as well as controls over public spending which ensure that the government will continue to exercise its functions.

1.2 Accounting convention

The financial statements have been prepared under the historical cost convention, modified where appropriate to account for the revaluation of certain assets and liabilities as set out in these accounting policies.

1.3 Basis of consolidation

The financial statements consolidate a group of entities that appears to HM Treasury to exercise functions of a public nature, or to be entirely or substantially funded from public money. This group includes central government departments, non-departmental public bodies, public corporations, local authorities, the National Health Service and the devolved administrations. The Whole of Government Accounts (WGA) boundary is compared to the Office for National Statistics (ONS) classification of the public sector to ensure the accounts are consistent and comparable to other measures of financial performance, such as the National Accounts.

There are areas where the boundary diverges from the ONS classification, most significantly the exclusion of Royal Bank of Scotland (RBS), and further details are provided in the critical accounting policies in note 2. A list of all the entities consolidated in the financial statements is published on gov.uk.

1.4 Accounting standards in issue but not yet effective

The following new standards have been issued but are not yet effective:

IFRS 9 'Financial Instruments' was issued in July 2014, effective for periods beginning on or after 1 January 2018. IFRS 9 will replace IAS 39 'Financial Instruments: Recognition and Measurement'. IFRS 9 introduces new requirements for the classification and measurement approach to all types of financial assets but carries forward unchanged almost all of the accounting requirements in IAS 39 for financial liabilities. IFRS 9 introduces a forward-looking 'expected-loss' impairment model, which will result in earlier recognition of expected credit losses, and a simplified model for hedge accounting to more closely align the accounting treatment with risk management activities. WGA will be most affected by the new impairment model and changes to disclosure requirements for financial instruments.

IFRS 15 'Revenue from Contracts with Customers' was issued in May 2014, effective for periods beginning on or after 1 January 2018. IFRS 15 will replace IAS 18 'Revenue Recognition' and IAS 11 'Construction Contracts'. The standard establishes a principles based approach for revenue recognition and is based on the concept of recognising revenue for obligations only when they are satisfied and the control of goods or services is transferred. It also introduces more extensive disclosure requirements. For WGA, IFRS 15 will impact the accounting and disclosure of revenue other than taxation, and in particular there may be an impact on the timing of revenue recognition.

IFRS 16 'Leases' was issued in January 2016, effective for periods beginning on or after 1 January 2019, but has yet to be endorsed by the EU. IFRS 16 will replace IAS 17 'Leases'. IFRS 16 largely removes the distinction between operating and finance leases for lessees by introducing a single lessee accounting model that requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. This is a significant change in lessee accounting and will increase the leased assets and lease liabilities recognised on the balance sheet within WGA.

It is not possible to quantify the effect that these new standards will have on WGA as it will be dependent on the impact in each underlying account.

1.5 Foreign Currency

Transactions that are denominated in a foreign currency are translated into sterling at the rate of exchange ruling on the date of each transaction, except where rates do not fluctuate significantly. In this case, an average rate for the period is used. Monetary assets and liabilities denominated in foreign currency at the financial year end are translated at the rates ruling at that date. Foreign exchange gains and losses resulting from the settlement of such transactions, and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies, are recognised in the Statement of Revenue and Expenditure, except when deferred in equity as qualifying cash flow hedges.

1.6 Revenue

Taxation revenue

Taxes and duties are measured at the fair value of the consideration received or receivable net of repayments. Revenue is recognised when a taxable event has occurred, the revenue can be measured reliably, and it is probable that the associated economic benefits from the taxable event will flow to the government. No revenue is recognised if there are significant uncertainties regarding recovery of the taxes and duties due.

Revenues are deemed to accrue evenly over the period for which they are due. Taxes and duties are accounted for on an accruals basis, except for stamp duty and National Insurance Classes 1A, 1B and 3. These are accounted for on a cash basis and do not have a material impact on the accounts. In addition, some repayments are accounted for on a cash basis.

Taxable events for the material tax streams are as follows:

Revenue type	Revenue recognition point
Income tax	Earning of assessable income during the taxation period
Social security	Earning of income on which National Insurance is payable
Corporation tax	Earning of assessable profit during the taxation period
Value Added Tax	Undertaking of taxable activity during the taxation period
Other excise duties	Date of production, date of import or movement of goods out of a duty suspended regime
Stamp duty	When property or shares are purchased
Council Tax	Residency in, or ownership or tenancy of, a chargeable dwelling for any period in the financial year
National Non-Domestic Rates	Occupation or ownership of a relevant non-domestic property for any period in the financial year

Income tax excludes tax credits which are recognised separately as an expense.

The tax gap is not recognised in these financial statements. The tax gap is the difference between the amount of tax that should, in theory, be collected if all individuals complied with both the letter and spirit of the law, and what is actually collected. It comprises of the revenue that is lost through non-payment, use of avoidance schemes, interpretation of tax effect of complex transactions, error, failure to take reasonable care, evasion, the hidden economy and organised criminal attack. Information on the size of the tax gap is included in Chapter 1.

Other revenue

Revenue from the sale of goods and services is measured at the fair value of the consideration received or receivable, and is recognised when the goods or services are provided. Income from the European Union (EU) in respect of supported projects is recognised at the point that the expenditure on those projects is recognised. Grants and similar financing for capital items, to the extent that they have not been eliminated on consolidation, are recognised immediately in the Statement of Revenue and Expenditure unless it is likely that the grant will need to be repaid, in which case the grant is deferred in the Statement of Financial Position.

1.7 Expenditure

Social security benefits

Social security benefits are statutory entitlements payable to private individuals and households, including the state pension. Social security benefits are accounted for as expenditure in the period to which they relate.

Social security benefits include tax credits, which are recognised in the year in which claims are assessed and awards authorised. Where under or overpayments are identified, either during the award year or subsequently, adjustments are made to expenditure.

Staff costs

Staff costs include salaries and wages, the costs of pensions and other employee benefits. Staff costs that can be attributed directly to the construction of an asset have been capitalised. Average staff numbers include staff engaged on capital projects.

Public sector pension scheme costs include current service costs and past service costs, both of which are explained in further detail in accounting policy note 1.19.

Grants and subsidies

Grants and subsidies are recorded as expenditure during the period that the underlying event or activity giving entitlement to the grant occurs. Entitlement to a grant varies according to the details of individual schemes and the terms of the offers made. Unpaid and unclaimed grants are charged to the Statement of Revenue and Expenditure on the basis of estimates of claims not received and are included in accruals in the Statement of Financial Position.

Interest costs

Interest costs on government borrowing are determined using the effective interest rate method. The effective interest rate is the rate that exactly discounts estimated future cash flows to the instrument's initial carrying amount. The majority of government's borrowings are at fixed interest rates. For variable rate borrowings the current rate applicable to that product is used and this treatment is also applied to index-linked borrowings. Gilts with the same maturity and coupon rate are sometimes issued in separate tranches and may have a different effective interest rate due to market conditions. However, once issued, gilts with the same maturity and coupon rate are indistinguishable from each other and so are accounted for as one issue using a weighted average effective interest rate.

1.8 Property, plant and equipment

Property, plant and equipment is initially recognised at cost and subsequently valued based on current value in existing use. For non-specialised assets, such as offices, this is the market value based on its current use less depreciation. For specialised assets, including the road and rail network held by central government, this is replacement cost less depreciation. However, road network assets held by local government and Scottish Water infrastructure assets are valued at historical cost less depreciation. Further details on the accounting estimates involved in valuing infrastructure assets are included in the critical accounting policies in note 2.

Land and buildings are usually professionally valued at 5 year intervals or when material changes are known to have arisen, and are subject to annual internal reviews. Gains on revaluation are taken to the revaluation reserve. Losses on revaluation for a particular asset are debited to the revaluation reserve if gains for that asset have been previously recorded, otherwise the full amount is charged to the Statement of Revenue and Expenditure.

Assets under construction are measured at cost less any recognised impairment loss and are not depreciated. Heritage assets and community assets are either not capitalised or included at cost or a token value and are not revalued.

Military equipment comprises non-current assets used by the military for which there is no civilian use. It includes items such as tanks, fighter aircraft and warships. It is initially recognised as a tangible non-current asset at its direct purchase or production cost, and is then depreciated over its useful economic life. In all other respects it is treated in the same way as other non-current asset categories. Development expenditure on military equipment, which meets the capitalisation criteria, is capitalised as an intangible asset.

1.9 Investment properties

Investment properties comprise of land or buildings held for rental revenue or for capital appreciation. Investment properties are measured initially at cost and are subsequently measured at fair value. Gains or losses arising from a change in fair value or disposal are recognised in the Statement of Revenue and Expenditure.

1.10 Intangible assets

Intangible assets are recognised if it is probable that they will result in future economic benefits to the government and if their cost can be measured reliably. Intangible assets are initially recognised at cost and subsequently valued based on current value in existing use. Where no active market exists, intangible assets are revalued using indices or another suitable model.

1.11 Depreciation and amortisation

Depreciation or amortisation is charged to write down the cost or valuation of an asset to its residual value over its estimated useful economic life. Residual values and useful economic lives are reviewed annually. Assets acquired through finance leases or Private Finance Initiative (PFI) contracts are depreciated over the shorter of the lease term and the estimated useful life. Any impairment in value in addition to depreciation is recognised immediately in the Statement of Revenue and Expenditure.

The depreciation period varies based on the estimate made by each WGA entity of the useful economic life of their assets. Generally, property, plant and equipment are depreciated over the following timescales:

Type	Period
Scottish water infrastructure	Up to 150 years
Road and rail network	Up to 100 years
Freehold land	Not depreciated
Buildings	Up to 60 years
Assets under construction	Not depreciated
Military equipment	Up to 35 years
Plant and machinery	Up to 30 years
Transport equipment	Up to 50 years
IT equipment	Up to 10 years
Furniture and fittings	Up to 20 years
Investment properties	Not depreciated

Intangible assets are typically amortised over the following timescales:

Type	Period
Military equipment	Up to 35 years
Development expenditure	Up to 35 years
Other intangible assets	Up to 15 years

1.12 Inventories

Inventories are valued at the lower of cost and net realisable value with the exception of inventory held by the Ministry of Defence. The Ministry of Defence hold inventory at current cost based on replacement purchase price or estimated through indexation. Where there is no expectation of consumption or sale in the ordinary course of business, the value is impaired to reduce it to net realisable value.

1.13 Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and current balances with banks and other financial institutions. They are readily convertible to known amounts of cash, and are subject to insignificant risk of changes in value and have an original maturity of three months or less. The carrying amount of these assets approximates their fair value. Bank overdraft amounts are included within trade and other payables in the Statement of Financial Position.

1.14 Gold holdings

Gold is valued at fair value based on the sterling equivalent of the London Bullion Market Association dollar denominated spot bid price at the reporting date. Changes in fair value are recognised in the Statement of Revenue and Expenditure.

1.15 Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently at amortised cost. The value of receivables is shown after an allowance for irrecoverable debts. Changes in the carrying amount of the allowance, for example as a result of increases in bad debts, are recognised in the Statement of Revenue and Expenditure.

1.16 Leases

Leases in which a significant proportion of the risks and rewards of ownership are transferred to government are finance leases and the leased assets are treated as if they had been purchased. The corresponding liability to the leasing company is shown as a finance lease liability and the accounts distinguish between payments of interest and capital.

All other leases are operating leases and the costs in respect of operating leases are recognised in the Statement of Revenue and Expenditure on a straight-line basis.

The Ministry of Defence has not applied IFRIC 4 'Determining whether an Arrangement Contains a Lease' to all of its contracts. Further information regarding this department from FReM can be found in paragraph 3.15 in Chapter 3 Governance statement.

1.17 Private Finance Initiative (PFI)

PFI contracts in which the government controls or regulates what services the private sector operator must provide with the assets; and controls any significant residual interest in the asset at the end of the contract, are recorded on the government's balance sheet as if they had been purchased. The corresponding liability to the PFI operator is recognised as a PFI liability and the accounts distinguish between payments of interest, capital and charges for services.

If the above conditions are not met then the private sector provider recognises the asset and all payments are recognised as charges for services.

A number of WGA entities have PFI contracts which should not be recognised on the Statement of Financial Position because, under IFRIC 12, the private sector contractor was, on balance, considered to have greater control over the use of the asset. WGA entities reported off-balance sheet contracts in their accounts in different ways in 2015-16, as the accounting standards allow flexibility as to how to present the information. Therefore it is not possible to provide a summary of all PFI contracts in this account. Included in Note 27 is a list of the most material PFI contracts that have been reported.

1.18 Provisions

Provisions are recognised when the government has a present obligation as a result of a past event and it is probable that the government will be required to settle that obligation. Provisions are measured at the best estimate of the expenditure required to settle the present obligation at the reporting date and are discounted to present value where the time value of money is material.

Where some or all of the expenditure required to settle a provision is expected to be recovered from a third party the recoverable amount is treated as an asset. The net provision expense after deducting expected recoveries from third parties is recognised in the Statement of Revenue and Expenditure.

1.19 Pension liabilities

The pension liability relates to public sector pension liabilities for current and former government employees, plus a small component for other approved organisations that qualify for membership of these government schemes. The government operates both defined benefit and defined contribution pension schemes. The defined benefit pension schemes are either funded (meaning that the scheme is a separate entity, which receives contributions and invests them to fund pension payments) or unfunded (meaning that there is no separate fund and the government is directly liable to fund pension payments as they fall due). The pension liability excludes the state pension paid to the general public which is included within overall expenditure and recorded as welfare spend.

For defined benefit pension schemes, the difference between the fair value of scheme assets (if any) and the present value of the scheme liability is recognised as a net asset or liability on the Statement of Financial Position. The scheme liability is calculated by discounting expected future benefit payments back to the reporting date using a discount rate based on high quality corporate bonds, usually interpreted as corporate bonds with a credit rating of AA. The expected future benefit payments are calculated allowing for pensionable service to the reporting date, future increases to benefits in accordance with scheme rules (known as the projected unit method) and projections of earnings for current employees up to the date of retirement, leaving service or earlier death. The pension liability is therefore an estimate of the amount of money that would need to be invested in high quality corporate bonds at the reporting date to cover all the expected future benefit payments accrued up to the reporting date.

Current service costs are the increase in the present value of the scheme liabilities arising from current members’ service over the year. They are determined by the individual scheme actuaries and were calculated using the discount rate at the start of the year.

Past service costs are changes in the present value of the scheme liabilities related to employee service in prior periods arising in the current period as a result of the introduction, change, or improvement to retirement benefits. These also include any gains or losses in relation to events defined as settlements or curtailments.

Pension financing costs are the increase during the period in the present value of the scheme liabilities because the benefits are one period closer to settlement. The financing cost is based on the discount rate (including inflation) at the start of the year and is calculated on the gross liability of unfunded schemes (which is shown gross) and the net liability of funded schemes (i.e. net of assets).

The gains and losses on revaluation reflect three elements:

The first of these elements is the change in the underlying assumptions used by the actuaries to determine the value of scheme liabilities. This includes changes in the assumptions such as financial assumptions, mortality rates and projected salary increases.

The second element relates to where in-year experience differs from assumptions previously used to determine the liabilities. For example, relating to assumptions about general salary and pension increases.

The third element relates to funded schemes and reflects differences between the asset returns experienced in-year and the interest on the assets included in the Statement of Revenue and Expenditure.

The current service costs, any past service costs, including those arising from settlements or curtailments, and pension financing costs are recognised as an increase in the pension liability and are charged to the Statement of Revenue and Expenditure. The gain or loss on revaluation of pension scheme assets and liabilities is recognised in the Statement of Other Comprehensive Income.

Payments to defined contribution pension schemes are recognised in the Statement of Revenue and Expenditure as they fall due.

1.20 Financial instruments

Financial assets

Depending on the purpose for which a financial asset is held or acquired it is classified as one of: at fair value through profit or loss, held-to-maturity investments, loans and receivables or available-for-sale assets.

Fair value through profit or loss	Financial assets held for trading or designated as at fair value through profit or loss. Derivatives are also classified as held for trading unless they are designated as hedges. Assets are recognised initially at fair value and transaction costs are expensed. Gains and losses arising from change in fair value are recognised in the Statement of Revenue and Expenditure.
Held-to-maturity investments	Non-derivative financial assets with fixed or determinable payments and fixed maturity, where there is a positive intention and ability to hold to maturity. Assets are recognised initially at fair value and subsequently at amortised cost with annual assessments for impairment.
Loans and receivables	Non-derivative financial assets with fixed or determinable payments that are not traded in an active market. Assets are recognised at fair value and subsequently at amortised cost using the effective interest rate method with annual assessments for impairment.
Available-for-sale assets	Non-derivative financial assets classified as 'available-for-sale' or not classified in any of the other three categories of financial assets. Assets are initially measured at fair value including transaction costs and gains or losses arising from changes in fair value are recognised in the Statement of Other Comprehensive Income.

The table below summarises the accounting treatment for government's financial assets:

Financial asset	Category used
Trade and other receivables	Loans and receivables
Debt securities	Fair value through profit or loss
Loans and deposits	Loans and receivables or held to maturity investments
Student loans	Loans and receivables
Equity investments	Available-for-sale or fair value through profit or loss
International Monetary Fund (IMF) quota subscription	Loans and receivables
IMF Special Drawing Rights holdings	Fair value through profit or loss

Financial liabilities

The majority of the government's financial liabilities are classified at amortised cost. The only exceptions are deposits by banks which can also be classified at fair value through profit or loss and IMF Special Drawing Rights allocation which are classified at fair value through profit or loss.

1.21 Contingent liabilities and contingent assets

Contingent liabilities and contingent assets are not recognised as liabilities or assets in the Statement of Financial Position, but are disclosed in the notes to the accounts. A contingent liability is a possible obligation arising either from past events whose existence will be confirmed only by uncertain future events, or a present obligation arising from past events which is not recognised because either an outflow of economic benefit is not probable or the amount of the obligation cannot be reliably measured. A contingent asset is a possible asset whose existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the control of the entity. Where the time value of money is material, the contingent liabilities and assets are stated at discounted amounts.

Note 2. Critical accounting estimates and judgements

2.1 WGA boundary

The 'Government Resources and Accounts Act (GRAA)' requires HM Treasury to prepare WGA for "a group of bodies each of which appears to HM Treasury (a) to exercise functions of a public nature, or (b) to be entirely or substantially funded from public money".

In complying with the GRAA, HM Treasury has made a judgement to base the consolidation boundary on entities classified to the public sector by the Office for National Statistics (ONS). This has the benefit of aligning the boundary of WGA to the boundary for national accounts and increases the usefulness of WGA as a tool for understanding the public finances.

The immaterial exceptions to this policy are:

- WGA excludes a small number of entities such as the National Audit Office and Audit Scotland that are accountable to their respective parliaments or assemblies rather than an executive arm of the government, and therefore do not form part of government
- minor entities are excluded on the basis that they are too small to have any material impact on WGA. The criteria used for minor bodies in 2015-16 was that they had to have gross expenditure, income, assets and liabilities of less than £10.0 million. For example, this includes some district councils

The material exceptions to this policy are housing associations and RBS.

Housing Associations

Housing associations were classified to the public sector on 30 October 2015 by the ONS. The government is implementing a package to deregulate housing associations and return them to the private sector. Therefore the exception to the WGA boundary is expected to be time limited.

RBS

RBS is recognised as an investment of government rather than being consolidated. This is on the basis that the scale of RBS would dwarf other aspects of WGA, distorting the accounts and making it difficult to determine trends. It would also be very technically challenging to consolidate RBS due to the differences in accounting policies and year-end. The government does not intend to retain its shares in RBS for the long-term, and has started to sell its holding, which makes the time and cost of consolidation less worthwhile.

The table below sets out the estimated effect of excluding RBS from the consolidation. It is based on RBS's financial results for the year ended 31 December 2015. It does not include an estimate of the changes required to align the year-end or accounting policies.

	Revenue	Expenditure	Net expenditure	Assets	Liabilities	Net liabilities
	£bn	£bn	£bn	£bn	£bn	£bn
2015-16 WGA	693.9	(937.7)	(243.8)	1,742.4	(3,728.4)	(1,986.0)
2015 RBS	16.1	(17.3)	(1.2)	815.4	(761.3)	54.1
Eliminations	(1.8)	1.8	-	(69.6)	69.6	-
WGA plus RBS	708.2	(953.2)	(245.0)	2,488.2	(4,420.1)	(1,931.9)

2.2 Taxation revenue

Taxation revenue is recognised in the period in which the event that generates the revenue occurs. Some of the accrued revenue receivable figures and other items are subject to statistical estimation of forecasts, as tax returns and tax payments can be filed at a later date. Due to the areas of uncertainty involved, actual outcomes could differ from the estimates used. HM Treasury believe that the levels of variation are acceptable and HM Revenue and Customs (HMRC) estimate that any total understatement or overstatement is unlikely to exceed £4.0 billion, which does not significantly impact the reported position and is less than 1% of total revenue reported in the Statement of Revenue and Expenditure.

2.3 Valuation of infrastructure assets

Road network assets held by local authorities are currently valued at historical cost less depreciation, which is a departure from the requirements of the FREM. Local authorities have been working towards implementing a valuation based on replacement cost less depreciation although it is uncertain whether this method of accounting will be adopted in the Code of Practice on Local Authority Accounting. In the meantime, the best proxy available for depreciated replacement cost is the calculated asset value used by the ONS in the National Accounts. The 2016 National Accounts estimated the value of the road network at £322.6 billion (2014-15: £306.6 billion) as at 31 December 2015.[1] Infrastructure assets are likely to be understated by at least £257.5 billion. Further information regarding this department from FReM can also be found in paragraph 3.17 in Chapter 3 Governance statement.

The rest of the road network and the whole of the rail network is held by central government and valued at replacement cost less depreciation. The value reflects the cost of constructing a modern equivalent asset on a greenfield sites, adjusted to reflect the current condition of the asset. Full valuations are carried out every 5 years and indices are used in interim periods.

2.4 Student loans

Student loans are held at amortised cost, with the gross value of the loans issued being discounted to net present value using the effective interest rate. The effective interest rate used is the higher of the rate intrinsic to the instrument and the real long term discount rate set by HM Treasury to approximate government's cost of borrowing. As student loans will not be fully repaid the higher of the two rates is the real long term discount rate, which for 2015-16 was RPI plus 0.7% (2014-15: RPI plus 2.2%).

The net present value calculation also takes into account an estimate of the value of student loans which will not be repaid because of the policy decisions made by the government for the loans to be written off in certain circumstances such as death, disability or the age of the student. This estimate is sensitive to assumptions on borrowers' earnings which are based on latest forecasts from the Office for Budget Responsibility.

[1] UK National Accounts, The Blue Book, 2016, Table 9.9 'Other Structures'

The method for determining the carrying value of the student loan book in the accounts is set by the FReM and is likely to be higher than the amount that they could be sold for. This is because the discount rate used by a market investor in valuing the future cash flows would likely be higher given that the investment is more risky than gilts.

2.5 Public sector pension liability

The assessment of the pension liabilities requires various assumptions about future unknowns in order to determine the expected future benefit payments. These assumptions include life expectancy, employee turnover rates, projections of price inflation and projections of earnings for current employees. A discount rate is then required to discount the future benefit payments to produce a net present value.

The key financial assumptions used by the actuaries of government pension schemes to determine the 2014-15 and 2015-16 WGA pension liabilities are set out below:

			2015-16			2014-15
	Unfunded		Funded	Unfunded		Funded
	Central Government[2] %	Local Government[3] %	Local Government %	Central Government %	Local Government %	Local Government %
Rate of increase in salaries[4]	4.2	1.0-4.7	0.9-4.3	4.2	1.8 – 4.6	1.5 – 4.4
Rate of increase of pensions in payment[5]	2.2	0.9-3.0	1.7-3.5	2.2	1.2 – 3.0	1.8 – 3.2
Discount rate –real[6]	1.37	-	-	1.3	-	-
Discount rate – nominal	3.6	2.3-10.6	2.7-4.0	3.55	2.2 – 9.9	3.0 – 4.4
Price inflation assumption	2.2	0.9-3.4	1.7-3.5	2.2	1.8 – 3.8	1.8 – 3.8

2.6 Provision for nuclear decommissioning

Nuclear Decommissioning Authority's (NDA's) nuclear decommissioning provision forms the bulk of the overall government provision for nuclear decommissioning and represents the best estimate of the costs of decommissioning plant and equipment on their designated nuclear licenced sites to return them to pre-agreed end states in accordance with the Authority's published strategy. NDA's programme of work will take until the year 2137. The estimate is necessarily based on assumptions regarding processes and methods likely to be used to discharge the obligations, reflecting a combination of latest available technical knowledge, requirements of the existing regulatory regime, government policy and commercial agreements. Given the very long timescale involved and the complexity of the plants and material being handled, considerable uncertainty remains in the estimates of future costs, particularly in later years. The estimate is updated to reflect changed circumstances and more recent knowledge and changed assumptions; as a result, material adjustments could be made to the carrying amount of the nuclear decommissioning provision and related assets and liabilities in the future. The principal assumptions and sensitivities around the cost estimates were reviewed and updated by NDA management as at 31 March 2016.

[2] Central government unfunded schemes includes the Principal Civil Service Pension Scheme (PCSPS), NHS pension schemes, armed forces pension schemes and teachers' pension schemes

[3] Local government includes the local government pension schemes, police pension schemes and firefighters' pension scheme, with the exception of the police and fire schemes in Northern Ireland as they are administered by central government

[4] Rate of increase in salaries is shown inclusive of the inflation assumption but does not include promotional salary increases.

[5] Rate of increase of pensions in payment will depend upon the underlying measure of inflation and whether there are any upper or lower limits on the rate of increase

[6] The discount rate for Central Government unfunded schemes are set by HM Treasury (see Chapter 1 Box 1.A: Discount rates)

2.7 Provision for clinical negligence

The clinical negligence provision requires the directors of the NHS Litigation Authority to make judgements, estimates and assumptions to value the liability. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. They are reviewed annually by the NHS Litigation Authority, supported by its actuaries the Government Actuary's Department.

Known reported claims are individually valued using likely costs to resolve the claim and probability factors to take account of the potential of a successful defence. Whilst incurred but not reported claims are valued using actuarial models to predict likely values. Due to the long-term nature of the liabilities and the assumptions on which the estimate of the provision is based, some uncertainty about the value of the liability remains.

Note 3. Segmental reporting

Segmental reporting 2015-16

	Central Government £bn	Local Government £bn	Public Corporations £bn	Whole of Government £bn
Taxation revenue	(539.7)	(52.7)	(0.2)	(592.6)
Other revenue	(51.9)	(39.4)	(10.0)	(101.3)
Total public services revenue	(591.6)	(92.1)	(10.2)	(693.9)
Social security benefits	194.4	27.4	0.7	222.5
Staff costs	123.9	64.5	4.9	193.3
Purchase of goods and services	114.0	70.3	7.8	192.1
Interest cost on government borrowing	28.3	-	-	28.3
Increase in provisions	8.1	0.5	0.6	9.2
Other expenditure	81.6	13.3	1.9	96.8
Total expenditure on public services	550.3	176.0	15.9	742.2
Net expenditure on public services	(41.3)	83.9	5.7	48.3
Financing costs of long-term liabilities, including discounting	174.5	11.0	1.9	187.4
Net loss on revaluations and disposals of assets and liabilities	8.8	(0.8)	0.1	8.1
Net expenditure/(revenue) for the year	**142.0**	**94.1**	**7.7**	**243.8**
Property, plant and equipment	713.2	336.5	70.5	1,120.2
Other non-current assets	221.5	23.1	27.4	272.0
Current assets	260.2	40.0	50.0	350.2
Total assets	1,194.9	399.6	147.9	1,742.4
Current government borrowings	(274.2)	-	-	(274.2)
Other current liabilities	(144.3)	(26.2)	(411.4)	(581.9)
Non-current government borrowings	(986.4)	-	-	(986.4)
Provisions non-current	(270.0)	(2.2)	(18.6)	(290.8)
Net public sector pension liability	(1,188.3)	(235.8)	(0.6)	(1,424.7)
Other non-current liabilities	(107.0)	(40.9)	(22.5)	(170.4)
Total liabilities	(2,970.2)	(305.1)	(453.1)	(3,728.4)
Net assets/(liabilities)	**(1,775.3)**	**94.5**	**(305.2)**	**(1,986.0)**

WGA uses the same classification of sectors of government as the ONS.

Central government comprises government departments, the devolved administrations of Scotland, Wales and Northern Ireland, non-departmental public bodies, entities in the National Health Service, the pension liability for all teachers included within the Teachers' Pension Scheme and certain local government functions in Northern Ireland and Scotland, such as police, education and social services, which are carried out by central departments. Central government also includes academy schools. The share of central government expenditure has been increasing over time as schools convert and transfer out of the local government sector.

Local government comprises all local authorities, police and crime commissioners, fire and rescue authorities, national park authorities and waste disposal authorities in England and Wales and local authorities in Northern Ireland and Scotland.

Public corporations comprises organisations which generate more than 50% of their income from the sale of goods and services, for example the Crown Estate, British Broadcasting Corporation and Driver & Vehicle Standards Agency.

The remuneration and staff report in Chapter 4 provides a breakdown of staff numbers by sector.

Segmental reporting 2014-15 (restated)

	Central Government £bn	Local Government £bn	Public Corporations £bn	Whole of Government £bn
Taxation revenue	(516.3)	(50.2)	(0.2)	(566.7)
Other revenue	(48.3)	(34.6)	(10.3)	(93.2)
Total public services revenue	(564.6)	(84.8)	(10.5)	(659.9)
Social security benefits	190.2	26.8	0.7	217.7
Staff costs	116.6	64.1	4.8	185.5
Purchase of goods and services	115.5	68.9	7.3	191.7
Interest cost on government borrowing	27.6	-	-	27.6
Increase in provisions	21.2	0.7	4.1	26.0
Other expenditure	88.0	13.1	1.7	102.8
Total expenditure on public services	559.1	173.6	18.6	751.3
Net expenditure on public services	(5.5)	88.8	8.1	91.4
Financing costs of long-term liabilities, including discounting	53.1	11.7	0.3	65.1
Net loss on revaluations and disposals of assets and liabilities	0.8	(1.0)	(4.3)	(4.5)
Net expenditure/(revenue) for the year	48.4	99.5	4.1	152.0
Property, plant and equipment	696.4	319.3	60.1	1,075.8
Other non-current assets	234.1	21.1	21.4	276.6
Current assets	253.7	41.8	35.4	330.9
Total assets	1,184.2	382.2	116.9	1,683.3
Current government borrowings	(235.2)	-	-	(235.2)
Other current liabilities	(143.4)	(26.3)	(398.2)	(567.9)
Non-current government borrowings	(939.3)	-	-	(939.3)
Provisions non-current	(139.6)	(2.4)	(18.4)	(160.4)
Net public sector pension liability	(1,225.9)	(266.0)	(1.4)	(1,493.3)
Other non-current liabilities	(105.8)	(39.0)	(17.6)	(162.4)
Total liabilities	(2,789.2)	(333.7)	(435.6)	(3,558.5)
Net assets/(liabilities)	(1,605.0)	48.5	(318.7)	(1,875.2)

Note 4. Taxation revenue

	2015-16 £bn	% of total	2014-15 £bn	% of total
Income Tax	169.5	29%	163.1	29%
National Insurance Contributions (NIC)	102.1	17%	97.2	17%
Value Added Tax (VAT)	116.1	20%	113.9	20%
Corporation Tax	45.2	8%	40.3	7%
Hydrocarbon oils duty	27.7	5%	27.2	5%
Excise duty	26.4	4%	26.9	5%
Stamp taxes	14.8	2%	13.5	2%
Capital gains tax	7.3	1%	5.7	1%
Other taxes and duties	26.6	4%	25.0	4%
Central government taxation revenue	**535.7**	**90%**	512.8	90%
Council Tax	29.6	5%	28.2	5%
National Non-Domestic Rates (NNDR)	27.3	5%	25.7	5%
Local government taxation revenue	**56.9**	**10%**	53.9	10%
Total taxation revenue	**592.6**	**100%**	566.7	100%

There has been an increase of 5% in total tax revenue in 2015-16:

Income tax increased by 4% compared to 2014-15. This increase in pay-as-you-earn (PAYE) and Self-Assessment receipts was largely due to growth in the economy, leading to higher levels of employment and higher wages.

NICs increased by 5% compared to 2014-15. The increase is due to the growth in the economy which has led to higher levels of employment and growth in wages.

VAT increased by 2% compared to 2014-15, as a result of significant increases in receipts for the automotive, business services and utilities sectors. Additionally, the growth in wages has led to an increase in household consumer spending on goods and services, increasing VAT receipts.

Corporation Tax increased by 12% compared to 2014-15. Included in Corporation Tax for 2015-16 are Bank Surcharge receipts of £0.3 billion. Legislation was introduced in the Finance (No.2) Act 2015 to introduce the Bank Surcharge. The measure imposes a surcharge of 8% on the profits of banking companies from 1 January 2016.

Hydrocarbon oils duty increased by 2% compared to 2014-15, due to a reduction in pump prices for the majority of the year, increasing the amount of fuel purchased and therefore revenue.

Excise Duties includes duties on tobacco, alcohol, customs and vehicles. Overall, Excise duties fell by 2% compared to 2014-15 which reflects various changes in habits. Tobacco duty fell due to the continued decrease in the usage of tobacco products, whilst Vehicle Excise Duty fell as vehicles become more fuel efficient.

Stamp Taxes are taxes related to the purchase of property or shares. Overall, stamp taxes increased by 10% due to higher volumes of property transactions, and higher property prices in both the residential and commercial sectors.

Council Tax income has increased by 5% compared to 2014-15, due to an increase in the average tax rate of 1.1% and an increase in the tax base, i.e. the number of taxable dwellings.

NNDR are collected by local authorities from those that occupy a non-domestic property, based upon valuations set by the Valuation Office Agency. The total income from NNDR rose by 6% compared to 2014-15.

Note 5. Other revenue

	2015-16 £bn	2014-15 restated £bn
Sale of goods and services	35.5	33.4
Fees, levies and charges	12.8	13.2
Rental income	10.5	10.1
Interest income	6.3	7.2
Net profit on sale of assets	6.3	1.7
EU income	4.0	5.6
Private sector contributions to local services	3.1	2.6
Pension scheme income	2.5	2.4
NHS related income	2.6	2.4
Train operator franchise income	1.8	1.8
Deferred income	1.6	1.4
Licence income	1.6	1.5
Grants from private sector	1.4	1.2
CRC allowances sales and EU emissions trading scheme	1.1	1.1
Charitable income	1.0	1.4
Pensions other	0.8	1.8
Recoveries and recharges	0.4	0.9
Miscellaneous operating revenue	8.0	3.5
Total other revenue	**101.3**	93.2

The most significant source of revenue, after taxation, for government is the **sale of goods and services** analysed below:

	2015-16 £bn	2014-15 £bn
Services provided by local authorities	18.4	18.4
Public corporations	7.0	6.6
Highways and transport services provided by TfL	4.4	4.2
Central government	3.9	2.8
NHS	1.8	1.4
Total sale of goods and services	**35.5**	33.4

Services provided by local authorities include social care, planning and development, cultural and leisure provision and environmental services. Services provided by public corporations include the supply of waste and water services and advertising and services provided by central government include waste management and electricity generation.

Highways and transport services provided by Transport for London (TfL) increased by 5% compared to 2014-15. This reflected average fare increases of 1.0 % and a 3.4% increase in passenger journeys.

Fees, levies and charges include fees and charges to recover the full cost of providing services and levies. The most significant sources are analysed below:

	2015-16 £bn	2014-15 £bn
Transport / Passenger rail services	2.2	2.8
Visa, immigration and passport	1.8	1.6
Levies	1.8	1.8
Court fines and penalties	1.7	1.5
NHS fees and charges (Dental, Prescription and other)	1.5	1.5
Other fines and penalties	0.9	1.5
Other	2.9	2.5
Total fees, levies and charges	**12.8**	13.2

Rental income from local government housing relates to rents and related costs collected from local government council tenants.

EU income comprises funding received by WGA entities for projects supported wholly or partly by the EU. Much of this funding was passed onto third parties, including agricultural subsidies payments to farmers. The reduction is mainly due to reduced income received by the Department for Environment, Food & Rural Affairs.

Pension scheme income relates to employer contributions from organisations which participate in public sector pension schemes but are not themselves consolidated within the WGA boundary. Examples included GPs and charity hospices that contributed to the NHS pension scheme; higher and further education institutions and independent teaching establishments that contributed to the Teachers' Pension Scheme. It also includes non-WGA entities such as the National Audit Office, Wales Audit Office and Electoral Commission that contribute to the Principal Civil Service Pension Scheme. Employer contributions from bodies within WGA totalled £15.9 billion (2014-15: £15.3 billion) of which £13.4 billion (2014-15: £12.9 billion) have been eliminated on consolidation. Employee contributions totalled £8.3 billion (2014-15: £8.3 billion), this was netted of against current service costs in Staff costs in compliance with the FReM. **Pensions other** includes transfers in from other schemes.

Note 6. Social security benefits

	2015-16 £bn	% of total	2014-15 £bn	% of total
State Pension	91.5	41%	88.6	40%
Pension Credit	6.2	3%	6.7	3%
TV licences for the over 75's	0.6	0%	0.6	0%
Pensioner benefits	**98.3**	**44%**	95.9	43%
Disability Living Allowance	14.3	6%	14.7	7%
Attendance Allowance	5.7	3%	5.6	3%
Personal Independence Payment	3.0	1%	1.6	1%
Carer's Allowance	2.7	1%	2.5	1%
Disability and Carer's benefits	**25.7**	**11%**	24.4	12%
Employment and Support allowance	15.0	7%	13.4	6%
Jobseeker's Allowance	2.4	1%	3.2	2%
Income Support	2.9	1%	3.3	2%
Statutory Sick Pay and Maternity Pay	2.5	1%	2.4	1%
Other working age benefits	3.0	1%	2.9	1%
Working age benefits	**25.8**	**11%**	25.2	12%
Tax Credits	31.3	14%	31.1	14%
Child Benefit	11.7	5%	11.6	5%
Other benefits administered by HMRC	**43.0**	**19%**	42.7	19%
Housing benefit	28.0	14%	27.6	13%
Other benefits	1.7	1%	1.9	1%
Total social security benefits	**222.5**	**100%**	**217.7**	**100%**

Spending on **total social security benefits** increased by 2% compared with 2014-15, with the effect of lower unemployment being offset by higher spending on people with disabilities and health conditions.

The State Pension at £91.5 billion is the largest benefit by far and accounted for 41% of total social security benefit spending. Overall, just under half of benefit spending goes to **pensioner benefits** (44%). Equalising the State Pension age meant that the number of people receiving a State Pension was down slightly from the year before, at around 12.9 million. The 'triple lock' uprating policy gave an above inflation increase in 2015-16, meaning spending increased in real terms. The increase in expenditure on the Financial Assistance Scheme was due to the change in the discount rate.

Benefits paid in support for **Disability and Carer's benefits** was £25.7 billion, an increase of £1.3 billion over 2015-16 as the number of child and working-age cases rose.

Working age benefits of £25.8 billion went to people of all ages on low incomes, to protect them from poverty and improve their life chances.

Tax credits of £31.3 billion (2014-15: £31.1 billion) consists of Personal Tax credit and corporation tax reliefs. The increase is due to the increase in corporation tax reliefs mainly from Research & Development tax credit - large companies element.

Housing Benefit increased by 1% in 2015-16 as a result of incremental increases from local authorities. However, housing benefit payments from DWP to Local Authorities has actually decreased. This is a benefit paid to assist people with their rent if they are on a low income. It can pay all or part of the rent, depending on the individual's circumstance. The benefit is administered and paid by local authorities, which are then reimbursed by DWP. The DWP recovered over £1.3 billion of debt in 2015-16, which is consistent with the prior year.

Fraud and error

As the welfare system is funded by taxpayers, it is of paramount importance that government seeks to make accurate payments to claimants who are entitled to them. The departments responsible for benefit payments continue to work hard to reduce fraud and error. Refer to Chapter 1 for further information in this regard.

Note 7. Staff costs and numbers

Staff costs totalled £193.3 billion. Full details of staff costs and number of staff employed can be found in the remuneration and staff report in Chapter 4 and in the segmental analysis in note 3 of Chapter 5.

Note 8. Purchase of goods and services

	2015-16 £bn	2014-15 £bn
Central government	114.0	115.5
Local government	70.3	68.9
Public corporations	7.8	7.3
Total purchases of goods and services	**192.1**	191.7

The Department of Health reported the largest expenditure on purchases of goods and services of £64.8 billion (2014-15: £61.0 billion). Other departments that reported large expenditure include HMRC and Ministry of Defence. Further information on overall expenditure on public services can be found in the performance analysis in Chapter 1.

Note 9. Grants and subsidies

	2015-16 £bn	2014-15 £bn
Further and higher education sector	19.9	21.2
Contribution to the EU budget	11.3	11.3
EU grants and subsidies to the private sector	2.3	3.4
Overseas assistance & contributions	7.8	8.0
Cultural, heritage and sport	1.6	2.7
Transport	0.9	0.9
Housing	0.4	1.2
Scottish grants	2.8	2.2
Welsh grants	2.2	1.8
Other grants and subsidies	4.9	4.7
Total grants and subsidies	**54.1**	57.4

Further and higher education grants are paid to colleges and universities. These grants have decreased because of policy moving towards giving loans instead of grants.

The UK's **contribution to the EU budget** is the amount payable to the EU after the UK's rebate has been applied.

EU grants and subsidies to the private sector relate to projects which have been approved and funded by the EU but are administered by government, such as agricultural support. The EU reimburses the UK for this expenditure and the corresponding income is included in Note 5.

Overseas assistance and contributions includes contributions made by the Department for International Development to reduce poverty in developing countries; the majority of payments are made to multilateral organisations and non-government organisations in support of the Single Departmental Plan and UK's Aid Strategy. The Government is committed to spending 0.7% of the gross national income on international development. This amount also includes the expenditure of the Conflict Stability and Security Fund, which replaced the Conflict Pool in April 2015 and supports work in countries to reduce the risk of conflict.

Housing grants and subsidies covers a range of initiatives to improve the supply and quality of housing. Expenditure includes grants made to housing associations and other bodies to invest in affordable housing, Help to Buy and private market investment.

Scottish Government provides a range of grants to deliver their policies as reported in the portfolio outturn statements in their consolidated accounts.

Welsh Government provides a range of grant schemes to deliver their policies and create a fairer, more prosperous Wales. This includes funding to businesses and third sector organisations in order to improve the economy, encompassing a wide range of activities such as business start-ups, regeneration, energy saving initiatives, training and tourism.

Note 10. Depreciation and impairment

	Note	2015-16 £bn	2014-15 £bn
Depreciation of property, plant and equipment	*12*	29.8	26.5
Amortisation of intangible assets	*14*	3.6	3.9
Impairments		9.3	15.0
Total depreciation and impairments		**42.7**	45.4

Impairments refers to the impairment of PPE and Intangibles, trade receivables, financial assets and revaluation expenditure.

Note 11. Finance expense

	2015-16 £bn	2014-15 £bn
Interest on gilts	25.5	25.4
National Savings and Investment products	2.1	1.6
Treasury bills	0.5	0.4
Bank deposits and other	0.2	0.2
Total interest costs on government borrowing	**28.3**	27.6

Interest costs on government borrowing comprised interest on gilts, National Savings and Investment products, bank deposits and Treasury bills. It excludes interest paid on debt held by the Bank of England as part of its quantitative easing programme.

	Note	2015-16 £bn	2014-15 £bn
Pension financing costs	*24*	52.1	56.6
Provision financing costs	*22*	127.9	1.9
Other finance expense		7.4	6.6
Total financing costs of long-term liabilities		**187.4**	65.1

Pension financing costs and **provision financing costs** relate mainly to changes in the discounting of future liabilities to produce an estimate of their value today, rather than a change to the actual amount expected to be paid out. An explanation of discounting and discount rates is included in the performance analysis in Chapter 1 and further details are included in notes 22 and 24.

Other finance expense includes £4.7 billion (2014-15: £3.1 billion) of financing costs from PFI and finance leases. Further details on obligations under finance leases and PFI contracts are included in notes 26 and 27.

Note 12. Property, plant and equipment

Property, plant and equipment 2015-16

	Infrastructure assets	Land and buildings	Assets under construction	Military equipment	Other assets	Total
	£bn	£bn	£bn	£bn	£bn	£bn
Cost of valuation:						
At 1 April 2015 (restated)	748.0	427.4	48.8	71.3	105.1	1,400.6
Additions	5.1	10.1	29.7	3.0	3.2	51.1
Revaluations and impairments	6.5	16.5	(3.2)	0.9	(0.2)	20.5
Reclassifications and transfers	7.4	6.7	(21.8)	2.5	3.6	(1.6)
Disposals	(0.9)	(7.0)	(0.2)	(2.6)	(4.5)	(15.2)
At 31 March 2016	**766.1**	**453.7**	**53.3**	**75.1**	**107.2**	**1,455.4**
Depreciation:						
At 1 April 2015 (restated)	(186.8)	(47.5)	-	(39.5)	(51.0)	(324.8)
Charged in year	(9.1)	(11.0)	-	(3.4)	(6.3)	(29.8)
Revaluations and impairments	1.9	3.2	-	(0.5)	0.4	5.0
Reclassifications and transfers	(0.3)	0.9	-	-	0.4	1.0
Disposals	0.8	6.6	-	2.1	3.9	13.4
At 31 March 2016	**(193.5)**	**(47.8)**	**-**	**(41.3)**	**(52.6)**	**(335.2)**
Carrying amount at 31 March 2015	561.2	379.9	48.8	31.8	54.1	1,075.8
Carrying amount at 31 March 2016	**572.6**	**405.9**	**53.3**	**33.8**	**54.6**	**1,120.2**
Asset financing:						
Owned	564.3	371.0	52.3	33.8	49.4	1,070.8
Finance leased	-	6.5	-	-	4.1	10.6
On balance sheet PFI contracts	8.3	28.4	1.0	-	1.1	38.8
Carrying amount at 31 March 2016	**572.6**	**405.9**	**53.3**	**33.8**	**54.6**	**1,120.2**

Infrastructure assets include the:

- railway network held by Network Rail of £280.1 billion (2014-15 restated: £278.1 billion)
- strategic road network assets held by the Highways England of £110.0 billion (2014-15: £111.9 billion)
- highways network asset held by local authorities of £65.1 billion (2014-15: £62.1 billion)
- networked assets held by Scottish Water of £52.2 billion (2014-15: £41.8 billion)

The value of infrastructure assets has increased by £11.4 billion during 2015-16 reflecting new additions and the completion of assets under construction totalling £12.2 billion. These included investments in the rail and road networks by the Department for Transport and investment in transport infrastructure by TfL. Further information on the valuation of infrastructure assets is included in the critical accounting policies in note 2.

Land and buildings increased by £26.0 billion overall. The most significant revaluation related to land and buildings held by the Department for Education, amounting to £6.8 billion.

Reclassifications and transfers include assets reclassified between assets under construction to other types of assets, transfers to and from intangible assets and transfers to and from operating expenditure or reserves. Of the £21.8 billion outflow from assets under construction, £6.4 billion relates to the Ministry of Defence. This is made up mainly of £2.5 billion transferred into military equipment, £1.4 billion transferred into transport equipment and £1.1 billion into buildings. Other large reclassifications and transfers under assets under construction include £3.9 billion relating to the completion of infrastructure within the Department for Transport.

Other assets consist of:

	Plant and machinery	Transport equipment	IT equipment	Furniture, fittings and other	Total other assets
	£bn	£bn	£bn	£bn	£bn
Carrying amount at 31 March 2015	17.7	13.4	5.3	17.7	54.1
Carrying amount at 31 March 2016	**17.5**	**14.9**	**5.3**	**16.9**	**54.6**

Property, plant and equipment 2014-15

	Infrastructure assets £bn	Land and buildings £bn	Assets under construction £bn	Military equipment £bn	Other £bn	Total £bn
Cost of valuation:						
At 1 April 2014	385.7	403.0	42.5	72.5	101.7	1,005.4
Additions	11.2	11.5	21.0	1.2	5.2	50.1
Revaluations and impairments	(4.0)	11.3	(0.9)	0.2	0.5	7.1
Reclassifications and transfers	3.0	2.9	(14.9)	1.4	1.9	(5.7)
Disposals	(0.4)	(3.1)	(0.2)	(3.9)	(5.7)	(13.3)
At 31 March 2015	395.5	425.6	47.5	71.4	103.6	1,043.6
Restatements	352.5	1.8	1.3	(0.1)	1.5	357.0
At 31 March 2015 (restated)	748.0	427.4	48.8	71.3	105.1	1,400.6
Depreciation:						
At 1 April 2014	(57.8)	(45.2)	-	(39.2)	(50.9)	(193.1)
Charged in year	(5.9)	(10.2)	-	(4.0)	(6.4)	(26.5)
Revaluations and impairments	4.9	5.3	-	0.3	0.1	10.6
Reclassifications and transfers	-	1.5	-	0.2	1.2	2.9
Disposals	0.7	1.4	-	3.2	5.0	10.3
At 31 March 2015	(58.1)	(47.2)	-	(39.5)	(51.0)	(195.8)
Restatements	(128.7)	(0.3)	-	-	-	(129.0)
At 31 March 2015 (restated)	(186.8)	(47.5)	-	(39.5)	(51.0)	(324.8)
Carrying amount at 31 March 2014	327.9	357.8	42.5	33.3	50.8	812.3
Carrying amount at 31 March 2015 (restated)	561.2	379.9	48.8	31.8	54.1	1,075.8
Asset financing:						
Owned	553.1	339.5	47.6	31.8	49.0	1,021.0
Finance leased	0.6	10.7	0.3	-	1.0	12.6
On balance sheet PFI contracts	7.5	29.7	0.9	-	4.1	42.2
Carrying amount at 31 March 2015 (restated)	561.2	379.9	48.8	31.8	54.1	1,075.8

Note 13. Investment properties

	2015-16 £bn	2014-15 £bn
As at 1 April	14.9	13.9
Additions	0.6	0.5
Revaluations and impairments	0.7	1.0
Disposals	(0.4)	(0.5)
As at 31 March	15.8	14.9

Investment properties comprise mainly of land and buildings owned by local authorities. They provide rental income for the funding of services, as part of a financial strategy to minimise the use of general reserves to meet ongoing expenditure.

Note 14. Intangible assets

Intangible assets 2015-16

	Military equipment £bn	Development expenditure £bn	Software £bn	Licences and other £bn	Total £bn
Cost or valuation:					
At 1 April 2015	30.3	11.0	7.7	11.0	60.0
Additions	1.8	0.7	0.2	0.9	3.6
Revaluations and impairments	0.3	-	0.1	-	0.4
Reclassifications	(0.1)	(0.1)	0.5	-	0.3
Disposals	(0.4)	(0.3)	(0.2)	(1.4)	(2.3)
At 31 March 2016	31.9	11.3	8.3	10.5	62.0
Amortisation:					
At 1 April 2015	(10.6)	(4.4)	(5.1)	(7.5)	(27.6)
Charged in year	(0.9)	(0.5)	(0.7)	(1.5)	(3.6)
Revaluations and impairments	(0.2)	-	(0.1)	(0.1)	(0.4)
Reclassifications	-	-	-	0.3	0.3
Disposals	0.3	0.2	0.2	1.6	2.3
At 31 March 2016	(11.4)	(4.7)	(5.7)	(7.2)	(29.0)
Carrying amount at 31 March 2015	19.7	6.6	2.6	3.5	32.4
Carrying amount at 31 March 2016	20.5	6.6	2.6	3.3	33.0

Military equipment primarily covers the development of new equipment and the improvement of the effectiveness and capability of existing military equipment. The Ministry of Defence's 2015-16 Annual Report and Accounts includes details of intangible assets with a carrying amount greater than £0.5 billion, the most significant of which is the ongoing development costs for the Typhoon Airframe which in 2015-16 amounted to £5.4 billion (2014-15: £5.8 billion).

Intangible assets 2014-15

	Military equipment £bn	Development expenditure £bn	Software £bn	Licences and other £bn	Total £bn
Cost or valuation:					
At 1 April 2014	29.2	10.4	7.0	10.5	57.1
Additions	1.8	0.8	0.2	1	3.8
Revaluations and impairments	0.4	0.1	-	0.2	0.7
Reclassifications	(0.5)	0.2	0.6	0.1	0.4
Disposals	(0.6)	(0.5)	(0.1)	(0.8)	(2.0)
At 31 March 2015	30.3	11.0	7.7	11.0	60.0
Amortisation:					
At 1 April 2014	(9.8)	(4.1)	(4.4)	(6.9)	(25.2)
Charged in year	(1.1)	(0.6)	(0.8)	(1.4)	(3.9)
Revaluations and impairments	(0.2)	-	-	(0.1)	(0.3)
Reclassifications	-	-	(0.1)	-	(0.1)
Disposals	0.5	0.3	0.2	0.9	1.9
At 31 March 2015	(10.6)	(4.4)	(5.1)	(7.5)	(27.6)
Carrying amount at 31 March 2014	19.4	6.3	2.6	3.6	31.9
Carrying amount at 31 March 2015	19.7	6.6	2.6	3.5	32.4

Note 15. Trade and other receivables

	2015-16 £bn	2014-15 £bn
Non-current		
Taxation and duties due	5.0	5.1
Trade receivables	0.8	1.2
Other receivables	9.4	6.5
Prepayments and accrued revenue	1.1	1.2
Welfare overpayments	2.1	2.7
Sub-total	**18.4**	16.7
Less: provision for impairment of receivables	(4.0)	(4.0)
Total non-current trade and other receivables	**14.4**	12.7
Current		
Accrued tax revenue receivable	95.6	89.7
Taxation and duties receivable	26.0	27.9
Trade receivables	8.9	8.7
Other receivables	10.8	10.5
Prepayments and accrued revenue	13.6	11.1
Welfare overpayments	0.4	1.5
Court fines	2.5	2.2
Sub-total	**157.8**	151.6
Less: provision for impairment of receivables	(17.5)	(18.4)
Total current trade and other receivables	**140.3**	133.2
Total trade and other receivables	**154.7**	145.9

Accrued tax revenue receivable represents amounts of taxes and duties relating to 2015-16 that were not yet due or received from taxpayers at time of HMRC publication, where these have not been included in taxation and duties due and collection is reasonably certain. The increase is broadly in line with the increase in tax revenue for 2015-16.

Taxation and duties receivables represent all taxpayer liabilities that have been established, irrespective of whether due or overdue, for which payments have not been received at the HMRC Statement of Financial Position date.

The **provision for impairment of receivables** is analysed below:

	Non-current £bn	Current £bn	2015-16 £bn	2014-15 £bn
Taxation and duties due	2.4	8.8	11.2	12.6
Welfare payments	1.1	0.1	1.2	1.4
Court fines	-	1.9	1.9	1.7
Other trade and other receivables	0.5	6.7	7.2	6.7
Total provision for impairment of receivables	**4.0**	**17.5**	**21.5**	22.4

Note 16. Other financial assets

	2015-16 £bn	2014-15 £bn
Non-current		
Loans and deposits	48.3	63.1
Student loans	62.0	46.2
Equity investments	53.5	72.6
IMF quota subscription	19.7	10.0
Derivatives and other financial assets	25.3	24.7
Total non-current other financial assets	208.8	216.6
Current		
Debt securities	83.2	66.1
Loans and deposits	61.5	58.0
Student loans	2.4	2.3
Equity investments	0.9	1.7
IMF Special Drawing Rights	7.2	8.9
Derivatives and other financial assets	9.0	11.9
Total current other financial assets	164.2	148.9
Total other financial assets	373.0	365.5

Loans and deposits decreased in 2015-16 due to a reduction in the UKAR mortgage loans as a result of portfolio sales and redemptions. Loans and deposits consists of:

	Non-current	Current	2015-16 £bn	2014-15 £bn
Loans	44.4	3.4	47.8	65.3
Deposits	3.9	14.3	18.2	15.5
Repurchase agreements	-	43.8	43.8	40.3
Total	48.3	61.5	109.8	121.1

Loans include £35.5 billion of mortgage loans made by UKAR:

	2015-16 £bn	2014-15 £bn
Residential mortgages	34.7	51.1
Commercial loans	0.4	0.5
Unsecured loans	0.4	1.0
Total mortgage loans	35.5	52.6

Deposits mainly consist of deposits made by local government at commercial institutions of £17.3 billion.

Repurchase agreements increased by 9% and are funds advanced to banks (or bank subsidiaries) and central clearing counterparties under reverse repurchase agreements where securities were held as collateral and returned when the funds are repaid. Reverse sale and repurchase agreements were valued daily, and, depending on whether the value of the collateral rose or fell, collateral were returned to the provider of collateral, or additional securities requested from the provider of collateral. Further details are available in the 2015-16 accounts of the Exchange Equalisation Account, Debt Management Account, and Bank of England.

Student loans are valued at the gross value of the loans issued discounted to net present value using the effective interest rate method and adjusted to take into account an estimate of the value of student loans which will not be repaid because of policy reasons, such as age of the student or loan.

The value of student loans assets has increased year on year. This is partly due to increased student numbers and therefore a higher volume of loans, particularly from 2015-16 when the cap on student numbers was lifted, and an impairment reversal in year due to a favourable movement in the HM Treasury's long term discount rate. The 2015-16 movement is analysed below:

	2015-16 £bn	2014-15 £bn
As at 1 April	48.5	38.8
New loans issued (net of impairment)	10.2	7.3
Interest	1.2	1.9
Repayments	(2.1)	(2.0)
Effect of change in discount rate	7.2	-
Impairment adjustments	(0.6)	2.5
As at 31 March	**64.4**	48.5

The **equity investments** held by the government are set out below:

	2015-16 £bn	2014-15 £bn
Royal Bank of Scotland (RBS)	18.8	32.0
Lloyds Banking Group	4.4	12.2
European Investment Bank	8.1	7.1
Other	23.1	23.0
Total equity investments	**54.4**	74.3

The decrease in the value of the RBS shares was mainly due to a downwards revaluation of £9.9 billion and net sales (additions less disposals) of £3.3 billion. The decrease in the value of the Lloyds Banking Group ordinary shares was due to share sales of £7.1 billion and a downwards revaluation of £0.7 billion. Further details regarding these equity investments can be found in the 2015-16 accounts of HM Treasury. The increase in value of the government's shareholding in the European Investment Bank is as a result of exchange rate movements during 2015-16 and an increase in the European Investment Bank's net assets.

The **IMF quota subscription** and **Special Drawing Rights (SDRs)** relate to the UK's investments in the IMF. On becoming a member of IMF in 1944, the UK was required to pay a quota subscription to the IMF in a mixture of Special Drawing Rights (SDRs), the IMF's unit of account, and other widely accepted currencies. The UK's quota subscription of 20,155 million SDRs was equivalent to £19.7 billion at 31 March 2016, an increase of £9.7 billion compared to the prior year. This increase was mainly as a result of £9.1 billion of cash subscribed to the IMF. The UK also holds SDRs as a result of allocations made by the IMF, and subsequent purchases and sales of SDRs from or to other IMF members. These had a sterling value of £7.2 billion at 31 March 2016.

Debt securities primarily relate to securities issued or guaranteed by the governments of the United States, Euro-area countries and Japan which are used to manage the government's foreign currency reserves. The government increased its holdings of foreign currency reserves during the year.

Derivatives and other financial assets include derivatives and other investments.

Note 17. Inventories

	Raw materials and consumables	Other	2015-16 Total	2014-15 Total
	£bn	£bn	£bn	£bn
As at 1 April	8.7	2.6	11.3	11.8
Additions	7.8	4.2	12.0	13.1
Disposals	(9.8)	(3.6)	(13.4)	(12.8)
Write-offs	(0.2)	(0.1)	(0.3)	(0.7)
Revaluation	-	-	-	(0.1)
As at 31 March	6.5	3.1	9.6	11.3

Raw materials and consumables includes £4.6 billion (2014-15: £6.8 billion) of supplies and spares for immediate and potential use by the Ministry of Defence. During 2015-16, £2.0 billion of inventories held by the Ministry of Defence have been reclassified to non-current assets.

Note 18. Cash and cash equivalents

	2015-16 £bn	2014-15 £bn
Balance at 1 April	26.8	26.9
Net change in cash and cash equivalent balances	(1.0)	(0.1)
Balance at 31 March	25.8	26.8
The following balances at 31 March were held at:		
Government Banking Service	(3.5)	(3.1)
Commercial banks and cash in hand	15.4	15.7
Short term investments	13.9	14.2
Balance at 31 March	25.8	26.8

Note 19. Trade and other payables

	2015-16 £bn	2014-15 £bn
Current		
Trade and other payables	39.3	38.4
Accruals and deferred income	43.2	42.0
Refunds of taxation and duties payable	30.2	26.7
Imputed finance lease element of on-balance sheet PFI contracts	1.7	1.4
Obligations under finance leases	0.3	0.3
Total current trade and other payables	114.7	108.8
Non-current		
Trade and other payables	11.4	9.9
Accruals and deferred income	11.9	12.6
Imputed finance lease element of on-balance sheet PFI contracts	37.5	37.1
Obligations under finance leases	4.7	4.5
Total non-current trade and other payables	65.5	64.1
Total trade and other payables	180.2	172.9

Trade and other payables and **accruals and deferred income** were held across a wide range of public sector entities and relate to both day-to-day business delivery costs and other financial obligations.

Refunds of taxation and other duties payable relates mainly to Council Tax and business rates owed to the taxpayer and to amounts due to VAT traders where their claim was received after the end of the year and amounts in respect of corporation tax, income tax and other small taxes expected to be repayable by HMRC pending finalisation of taxpayer liabilities.

Further information on **obligations under finance leases** can be found in note 26 while further information on **PFI commitments** can be found in note 27.

Note 20. Government borrowings

	2015-16 £bn	2014-15 £bn
Current		
National Savings and Investment products (NS&I)	135.1	123.9
Treasury bills	78.3	65.4
Gilts	60.8	45.9
Total current government borrowings	**274.2**	235.2
Non-current		
Gilts	986.4	939.3
Total non-current government borrowings	**986.4**	939.3
Total government borrowings	**1,260.6**	1,174.5

The increase in total government borrowing is mainly due to additional gilts and Treasury bills issued by DMO. Further information on the government's financial risk, including liquidity and funding risk, is included in note 23.

NS&I products are a range of secure savings and investments offered to the public, that are backed by the Exchequer. They provide the government with a source for financing public spending. Further details of these products, and NS&I's 2015-16 accounts, can be found on the NS&I website.[7]

Treasury bills are issued by the Debt Management Account and, along with other money market operations, are used by the Debt Management Office to meet the government's daily cash requirements. Further details on these operations can be found in the Debt and reserves management report 2015-16', HM Treasury, March 2015, available at https://www.gov.uk/government/publications/debt-and-reserves-management-report-2015-to-2016.

Gilts are UK government sterling denominated listed bonds that are fixed rate or index-linked with the return linked to movements in the Retail Price Index. As the government's debt manager, the Debt Management Office (DMO) sells gilts to the market to ensure sufficient funding is available to meet the government's financial commitments. Gilts held by public sector entities are eliminated on consolidation and removed from the balance above, with the exception of gilts held by funded public sector pension schemes. Further details regarding gilts are available in the 2015-16 Debt and Reserves Management Report[8] and the 2015-16 accounts of the National Loans Fund.[9]

[7] http://nsandi-corporate.com/about-nsi/our-performance/our-annual-report-and-accounts/
[8] https://www.gov.uk/government/publications/debt-and-reserves-management-report-2015-to-2016
[9] https://www.gov.uk/government/publications/national-loans-fund-account-2015-to-2016

Note 21. Other financial liabilities

	2015-16 £bn	2014-15 £bn
Current		
Deposits by banks	357.3	354.9
Banknotes in circulation	67.8	63.8
Bank and other borrowings	9.0	10.6
IMF Special Drawing Rights liability	9.9	9.4
Debt securities	3.2	2.7
Derivatives	5.2	2.8
Financial Guarantees	0.1	-
Total current other financial liabilities	**452.5**	444.2
Non-current		
Deposits by bank	3.5	2.7
Bank and other borrowings	66.0	58.4
Debt securities	6.5	22.4
Derivatives	28.0	13.8
Financial Guarantees	0.3	0.4
Other financial liabilities	0.6	0.6
Total non-current other financial liabilities	**104.9**	98.3
Total	**557.4**	542.5

Deposits by banks comprise mainly £338.6 billion of deposits, held primarily by the Bank of England, and £18.6 billion of reverse sale and repurchase agreements (reverse repo). Reverse sale and repurchase agreements are where an entity purchases securities and agrees to sell them back at a specified time and price. Securities pledged by an entity as collateral via reverse repo remain on its own statement of financial position.

Banknotes are issued by the Bank of England. Demand for banknotes has continued to grow, resulting in a 6% increase in the notes in circulation in 2015-16. The Bank of England is responsible for maintaining confidence in the currency, by meeting demand with good-quality banknotes that the public can readily exchange.

Bank and other borrowings reflects loans and overdrafts. The largest component in this category relates is £29.3 billion of Network Rail long term debt.

International Monetary Fund (IMF) Special Drawing Rights (SDRs) allocation comprised a liability to the IMF of £9.9 billion for those SDRs that have been allocated to the UK when the country became a participant in the Special Drawing Rights Agreement and that have been allocated subsequently. A corresponding asset of £7.2 billion for the UK's actual holdings of SDRs is included in note 16.

Debt securities comprise securitised notes and covered bonds issued by HM Treasury group and Bank of England to securitise loans to customers and to raise unsecured medium term funding. There has been a significant 71% reduction in the long term position as the government buys back securities.

The most significant **derivatives** relate to contracts for difference held by the Department of Energy & Climate Change with a fair value of £12.6 billion (2014-15: £2.5 billion) to facilitate investment in low-carbon generation through provision of support payments which top up generators' income and remove their exposure to electricity price uncertainty. Due to uncertainties in future electricity prices it is not possible to quantify with certainty the settlement of these liabilities or the impact on future financial results. The carrying value of £12.6 billion does not include unamortised deferred "day 1 liabilities" of £18.0 billion as measured by the Department's valuation model at initial recognition but excluded from the carrying value in accordance with accounting standards.

Other significant derivatives relate to Pension Protection Fund of £13.6 billion (2014-15: £10.1 billion) are mainly interest rate swaps, options, credit default swaps and forward foreign exchange contracts to support liability-driven investment.

Note 22. Provisions for liabilities and charges

Provision for liabilities and charges

	Nuclear decommissioning £bn	Clinical negligence £bn	Other provisions £bn	2015-16 total £bn	2014-15 total £bn
At 1 April	82.9	29.3	63.1	175.3	154.6
Pay-outs made in year	(0.6)	(1.2)	(7.1)	(8.9)	(7.9)
Increase in expected future pay-outs	3.3	6.0	7.6	16.9	35.4
Change in discount rate	94.8	25.4	5.0	125.2	-
Discount rate unwind	1.7	-	1.0	2.7	1.9
Provisions not required written back	(0.4)	(1.9)	(3.3)	(5.6)	(8.4)
Transfers to payables	-		(0.1)	(0.1)	(0.3)
At 31 March	181.7	57.6	66.2	305.5	175.3

Provision movement

	2015-16 Total £bn	2014-15 Total £bn
Amounts included in the SORE:		
Increase in provisions	9.2	26.0
Provision expense in cost to public services	9.2	26.0
Discount rate changes	125.2	-
Discount rate unwind	2.7	1.9
Provision financing costs	127.9	1.9
Total expenditure recognised in the SORE	137.1	27.9
Amounts included in the SOFP	2.0	0.7
Pay-outs made in year	(8.9)	(7.9)
Total provision movement	130.2	20.7

Provision profile

	Nuclear decommissioning £bn	Clinical negligence £bn	Other provisions £bn	2015-16 total £bn	2014-15 total £bn
Within 1 year	3.6	2.3	8.8	14.7	14.9
Between 1 and 5 years	13.1	10.9	20.0	44.0	49.2
Thereafter	165.0	44.4	37.4	246.8	111.2
Total provision liability	**181.7**	**57.6**	**66.2**	**305.5**	175.3
Current provisions	3.6	2.3	8.8	14.7	14.9
Non-current provisions	178.1	55.3	57.4	290.8	160.4

The **total provision liability** has increased by £130.2 billion as at 31 March 2016. Of this, £125.2 billion was due to a change in the discount rates used to calculate their values in today's prices. Further information on discounting is included in the performance analysis in Chapter 1.

Each year the government reviews its obligations against all provisions and reviews the assumptions and judgements used to estimate the value of each provision. The estimates can be subject to significant revision if new information becomes available. Further information on the significant assumptions used in valuing the provisions for nuclear decommissioning and clinical negligence is included in the critical accounting policies in note 2.

The **provision for nuclear decommissioning** represents the best estimate of the cost in today's prices of decommissioning the plant and equipment on each designated nuclear licenced site and returning them to pre-agreed end states. This programme of work is forecast to take until 2137 to complete.

The provision increased by £98.8 billion in 2015-16, largely as a result of the change in the discount rate used to produce a current value. Only £3.3 billion of the increase related to changes in cost estimates or new liabilities taken on.

Some expenditure is recoverable from third parties under commercial agreements. In these cases expenditure in the Statement of Revenue and Expenditure is shown net of changes in the amount recoverable from third parties. The amount of recoverable costs included in the provision as at 31 March 2016 was £5.0 billion (2014-15: £3.2 billion).

The largest element of the provision relates to the Sellafield site which is the largest, most hazardous site that remains the government's highest priority for clean-up. Further information on the approach that the government is taking to manage its nuclear liabilities is included in the performance analysis in Chapter 1.

In respect of the Nuclear Liabilities Fund, assets of £8.9 billion have been recognised in the statement of financial position but these assets can only be used in respect of nuclear decommissioning costs.

The provision for nuclear decommissioning was subject to an emphasis of matter on uncertainties inherent in the provisions relating to the costs of dealing with nuclear decommissioning in the Audit Opinion of the Comptroller & Auditor General. Further details are available in the 2015-16 accounts of the Nuclear Decommissioning Authority.

The **provision for clinical negligence** represents the value in today's prices of the cost of claims arising from harm that occurred up to 31 March 2016. As many claims are not paid out immediately but instead involve payments over many years, the liability includes determined claims as well as claims that are considered likely to be determined in the claimant's favour.

The provision increased by £28.3 billion in 2015-16, largely as a result of the change in the discount rate used to produce a current value. The NHS Litigation Authority (now NHS Resolution) manage claims against the NHS in England and they recorded a 4.6% decrease in the number of new clinical claims reported compared to the prior year (2015-16: 10,965 claims, 2014-15: 11,497). Even though there was a 4.6% decrease in the number of new claims, the value of the provision has increased.

Further information on the actions being taken by government on clinical negligence is included in the performance analysis in Chapter 1.

Other provisions included a wide range of provisions across all parts of the public sector. These included provisions in relation to: injury benefits, medical costs, criminal injuries compensation, legal costs, compulsory purchases, concessionary fuel allowance to ex-miners, mine water treatment, public safety and subsidence, subsidence pumping stations and tip management, claims in respect of structural damage and diminution of value of properties affected by transport schemes, and compensation payments for termination of employment. The most significant provisions included in this balance are:

- £19.5 billion (2014-15: £19.1 billion) held by the Pension Protection Fund relating to liabilities to pay compensation to members and claims from pension schemes. The Pension Protection Fund retains the assets of the pension plans it rescues and generates investment growth to support the obligations it acquires. At 31 March 2016, it had net investments of £23.4 billion, nearly £4.0 billion in excess of its liabilities[10]
- £7.2 billion (2014-15: £4.7 billion) held by the Department for Work and Pensions (DWP) for the Financial Assistance Scheme (FAS). FAS provides assistance to members of defined benefit occupational pension schemes that were wound up under-funded when their employers became insolvent during the period 1 January 1997 to 5 April 2005. The FAS provision is held to provide for liabilities arising from

[10] https://www.gov.uk/government/publications/pension-protection-fund-annual-report-and-accounts-2015-to-2016

any FAS qualifying schemes once the assets from such schemes have transferred to government. The increase in the provision of £2.5 billion is primarily due to the change in the discount rate. Had the discount rate not changed from 2014-15 the provision would have decreased by £0.1 billion as a result of a reduction in the estimated number of future FAS members

- £6.9 billion (2014-15: £7.5 billion) held by HMRC relating to the repayment of tax receipts resulting from oil and gas field decommissioning, for the two periods 2016-17 to 2020-21 and 2021-2022 to 2041-42. These are expected to cost the Exchequer £1.7 billion and £5.2 billion respectively
- £5.9 billion (2014-15: £7.2 billion) held by HMRC relating to a number of legal and other disputes

Note 23. Financial instruments

This financial instruments note has two parts. The first part provides information on the significance of financial instruments on the government's balance sheet. The second part provides information about the nature and extent of risks arising from financial instruments and what the government does to manage these risks.

Financial assets by category

	Note	Cash & cash equivalents £bn	Loans and receivables £bn	Held to maturity investments £bn	Available for sale assets £bn	Designated as fair value £bn	Held for trading at fair value £bn	2015-16 Total £bn	2014-15 Total £bn
Cash and cash equivalents	*18*	25.8	-	-	-	-	-	**25.8**	26.8
Trade and other receivables	*15*	-	154.7	-	-	-	-	**154.7**	145.9
Debt securities	*16*	-	-	-	6.8	18.7	57.7	**83.2**	66.1
Loans and deposits	*16*	-	99.1	1.9	-	-	8.8	**109.8**	121.1
Student loans	*16*	-	64.4	-	-	-	-	**64.4**	48.5
Equity investments	*16*	-	-	-	44.5	5.4	4.5	**54.4**	74.3
IMF quota subscription	*16*	-	19.7	-	-	-	-	**19.7**	10.0
IMF Special Drawing Rights	*16*	-	-	-	-	-	7.2	**7.2**	8.9
Other	*16*	-	1.8	1.2	7.6	2.3	21.4	**34.3**	36.6
Total financial assets		**25.8**	**339.7**	**3.1**	**58.9**	**26.4**	**99.6**	**553.5**	**538.2**

Financial liabilities by category

	Note	Carried at amortised cost £bn	Designated as fair value £bn	Held for trading at fair value £bn	2015-16 Total £bn	2014-15 Total £bn
Trade and other payables	*19*	180.2	-	-	180.2	172.9
Government borrowings	*20*	1,260.6	-	-	1,260.6	1,174.5
Deposits by banks	*21*	334.0	3.5	23.3	360.8	357.6
Banknotes in circulation	*21*	67.8	-	-	67.8	63.8
Bank and other borrowings	*21*	75.0	-	-	75.0	69.0
Derivatives	*21*	-	14.6	18.6	33.2	16.6
Debt securities	*21*	9.7	-	-	9.7	25.1
IMF Special Drawing Rights liability	*21*	-	-	9.9	9.9	9.4
Financial Guarantees	*21*	0.4	-	-	0.4	0.4
Other	*21*	0.6	-	-	0.6	0.6
Total financial liabilities		**1,928.3**	**18.1**	**51.8**	**1,998.2**	**1,889.9**

In most cases the value of assets and liabilities shown on the balance sheet either equals or is a reasonable approximation of fair value. The main exceptions are government borrowings and the Contracts for Differences (CfD) liability (included in derivatives in the table above). Gilt-edged securities have a carrying amount of £1,047.2 billion (2014-15 restated: £985.2 billion) and a fair value of £1,276.3 billion (2014-15 restated: £1,205.9 billion), reflecting the higher amount that investors are willing to pay in order to secure a certain level of interest payment. The CfD liability has a carrying value of £12.6 billion and a fair value of £30.6 billion. The difference of £18 billion relates to a 'day one' loss from when the contracts were first entered into and is required by accounting standards to be deferred. This additional liability will be gradually recognised in the financial statements over the contract lifetime.

The government also has gold holdings which are treated as being similar to a financial asset and, as such, reported at fair value based on the sterling equivalent of the London Bullion Market association dollar denominated spot bid price as at 31 March 2016. During 2015-16 the price of gold rose from £799 to £860 an ounce, an increase of 8%, giving rise to a revaluation gain of £605 million (2014-15: gold price rose from £775 to £799 an ounce, an increase of 3%, giving rise to a revaluation gain of £246 million).

Fair value hierarchy

Assets and liabilities carried at fair value are valued using a 'fair value hierarchy' which gives highest priority to quoted prices in active markets for identical instruments (level 1 inputs), second priority to valuation techniques based on observable inputs (level 2) and lowest priority to valuation techniques using unobservable inputs. Where valuation techniques are based on unobservable inputs (level 3) then the appropriate valuation technique is chosen, including use of discounting of future cash flows and the use of the net asset values underlying the unquoted equity investment. The table below summarises asset and liability fair values based on the valuation technique used.

	Level 1	Level 2	Level 3	2015-16 Total	2014-15 Total
	£bn	£bn	£bn	£bn	£bn
Financial assets at fair value					
Debt Securities	76.1	6.7	0.4	83.2	66.1
Equity investments	41.0	2.4	11.0	54.4	74.3
IMF special drawing rights	7.2	-	-	7.2	8.9
Loans and deposits	-	8.8	-	8.8	-
Other	3.7	24.4	3.2	31.3	49.1
Financial liabilities at fair value					
Deposits by banks	(10.1)	(16.7)	-	(26.8)	(39.7)
IMF SDR allocation	(9.9)	-	-	(9.9)	(9.4)
Other	(0.8)	(19.3)	(13.1)	(33.2)	(19.2)

The most significant individual level 3 liability balance is the CfD contracts which uses a discounted cash flow methodology. Further details can be found in the annual report and accounts of the Department for Energy and Climate Change.[11]

Liquidity and funding risk

The government's objective when funding its operations is to minimise, over the long term, the costs of meeting the government's financing needs, taking into account risk, while ensuring that debt management policy is consistent with the aims of monetary policy.

Each year, the government assesses the costs and risks associated with different possible patterns of debt issuance taking into account the most up-to-date evidence and information about market conditions and demand for debt instruments. This information is used to set the Debt Management Office's (DMO's) financing remit which is published alongside the Budget and updated during the year to reflect changes to government's cash requirements.

Refinancing risk is the risk that the government will need to roll over high levels of debt continuously, or that redemptions will be concentrated in particular years. This risk is mitigated by taking decisions which spread gilt issuance along the maturity spectrum. The issuance profile used in 2015-16 is summarised below:

	Short conventional (0-7 years)	Medium conventional (7-15 years)	Long conventional (over 15 years)	Index-linked	Unallocated
2015-16 debt issuance %	25.4	20.0	28.0	23.5	3.1

The government's cash management objective is to ensure that sufficient funds are always available to meet any net daily cash shortfall and, on any day when there is a net cash surplus, to ensure this is used to the best advantage. HM Treasury and the DMO work together to achieve this. The Treasury is responsible for daily forecasts of net flows into or out of the Exchequer. Its objective is to provide the DMO with timely and accurate forecasts of the expected net cash position over time. The DMO then carry out market transactions to either fund or place the net cash positions in order to minimise the costs of cash management while operating within the risk appetite approved by ministers.

[11] https://www.gov.uk/government/collections/decc-annual-reports-and-accounts

In 2015-16 the DMO carried out its cash management objective primarily through market instruments and Treasury bill sales. The DMO operates within agreed risk limits and the main market instruments used are sterling-denominated repurchase agreements and reverse repurchase agreements. The following balances were held by the DMO as at 31 March 2016:

- £19.6 billion of secured lending under reverse sale and repurchase agreements and recognised as loans and deposits
- £7.5 billion of liabilities where government has sold securities and agrees to buy them back at a specified time and price

For further details see the DMO's 2015-16 annual report and accounts.[12]

Local authorities adopt independent liquidity risk management, and this is done within a statutory framework. Local authorities are required by the Local Government Finance Act 1992 to provide a balanced budget, which ensures sufficient funds are raised to cover annual expenditure. Medium term plans generally set targets for liquidity ratios, which are approved as part of the annual budget setting process. To manage liquidity risk, local authorities can access borrowings from the money markets to cover any day to day cash flow need and can access longer term funds from financial institutions or from the government's Public Works Loan Board.

Interest rate risk

At present, annual debt management decisions are made in the context of an elevated level of debt relative to gross domestic product (GDP), high but falling government borrowing and fiscal consolidation. As a result, subject to cost-effective financing, the government has decided to maintain a relatively high proportion of fixed-rate exposure at a relatively long average maturity in the debt portfolio to limit exposure to interest rate volatility. The government is exposed to cash flow interest rate risk on its remaining floating-rate investments and borrowings.

The most significant floating rate investments and borrowings are index-linked gilts and NS&I products, debt issued by Network Rail and student loans. Other central government departments do not invest or access funds from commercial sources, so have negligible exposure to interest rate risk.

Index-linked gilts expose the government to both interest rate risk and inflation risk whereby interest and redemption amounts paid on index-linked gilts vary monthly in line with changes in RPI. If interest rates were to increase by 100 basis points then this would increase government's borrowing costs by £423 million and if RPI were to increase by 100 basis points then government's borrowing costs would rise by £4.1 billion. An element of this would be eliminated within the government boundary.

Network Rail has a combination of fixed, floating, index-linked debt issuances. Like with the government's gilt portfolio, this gives rise to interest rate risk and inflation risk. If interest rates were to increase by 100 basis points then this would increase Network Rail's borrowing costs by £1.2 billion and if RPI were to increase by 100 basis points then Network Rail's borrowing costs would rise by £0.2 billion.

The interest rate on pre 2012 student loans is the lower of RPI and the Bank of England base rate plus 1%. The amount of interest repayable is therefore subject to fluctuations in base rates and RPI. The impact of the interest rate risk for student loan issued under the pre 2012 scheme is factored into the carrying value as the student loan repayment model calculates the impact of interest rate on expected future cash flows. There is inherent risk in forecasting the amount of

[12] https://www.gov.uk/government/publications/uk-debt-management-office-annual-report-and-accounts-2015-to-2016

interest payable and if the UK experiences base rates that are lower than RPI the future cash flows will be impaired further.

Counterparty risk

The categories where the main counterparty risk are found are: debt securities (£83.2 billion), loans and deposits (£109.8 billion), student loans (£64.4 billion) and IMF balances (£26.9 billion). The bodies where the majority of balances lie with are: Exchange Equalisation Account (EEA) (£87.8 billion), Department for Business, Innovation and Skills (BIS) (£56.9 billion), HM Treasury (£40.1 billion) and National Loans Fund (NLF) (£21.4 billion).

Limits are set for both individual entities and groups of related entities. In addition, there are limits to contain the overall exposure to each relevant country's banking sector, certain instruments traded, and maturity of repo and foreign exchange transactions with counterparties. The creditworthiness of counterparties and security issuers is subject to regular scrutiny by the Bank of England and review by the Bank's Credit Ratings Advisory Committee; assessments are performed both routinely, and dynamically, in response to market or specific entity conditions.

The majority of **debt securities** (£69.0 billion) are held in the EEA, and comprise the UK's official holding of international reserves. The Government holds foreign currency reserves on a precautionary basis to meet current policy objectives to regulate the exchange value of sterling and any potential future changes in policy.

Foreign currency assets inevitably carry some element of credit risk. In order to keep this risk at a low level, the government predominantly invests in securities issued, or guaranteed by, the national governments of the United States, euro area countries and Japan. The EEA debt securities are held at an equivalent external rating of AA and above (£64.5 billion) and A to AA (£4.5 billion) and were held within Europe (£31.5 billion), North America (£34.4 billion), and Asia-Pacific (£3.1 billion). Further details on the government's credit risk management of foreign currency reserves can be found in the annual report and accounts of the EEA.[13]

Other significant debt securities include those lent under the Funding for Lending Scheme (FLS). Under FLS participating banks and building societies can until January 2018 borrow Treasury Bills from the Bank of England in exchange for eligible collateral. The aim of the FLS is to increase the supply of credit to the real economy by incentivising Banks and other financial institutions to boost their lending to UK households and businesses. The FLS has contributed to a fall in bank funding costs.

The NLF issues Treasury Bills for sale to the Debt Management Account (DMA) which makes them available to be borrowed by the Bank of England. As at 31 March 2016, on an amortised cost basis, £86.4 billion (2014-15: £77.9 billion) of Treasury Bills issued to the DMA by the NLF for the FLS were outstanding; further details are available from the accounts of both the National Loans Fund and the Bank of England.

Stock collateral is also taken by the DMA when entering reverse sale and repurchase contracts to reduce its exposure to credit losses.

[13] https://www.gov.uk/government/collections/hmt-eea

Loans and deposits mainly comprise of mortgages made by UKAR (£35.5 billion) which are not rated, and reverse sale and repurchase agreements (£43.9 billion).

The impact of credit risk on UKAR's loan book is shown by the following table of allowances for mark-downs of impaired assets:

		2015-16		2014-15
	Balance sheet value	**Provision**	Balance sheet value	Provision
	£bn	**£bn**	£bn	£bn
Loans secured on residential property	34.7	0.7	51.1	0.9
Other secured loans	0.4	0.1	0.5	0.1
Unsecured personal loans	0.4	0.1	1.1	0.2
Total UKAR loans	**35.5**	**0.9**	52.7	1.2

For more details on disclosures relating to UKAR, please refer to the accounts of HM Treasury.

Reverse sale and repurchase agreements are mainly entered into by the Bank of England, DMA, and EEA. Exposures to credit risk are fully collateralised and assets held as collateral are revalued daily. The government returns collateral to the provider of collateral, or requests additional collateral, depending on whether the value of collateral has risen or fallen. Details on collateral held under these agreements can be found in the accounts of the entities above.

The government intentionally takes on counterparty risk through **student loans**. Eligible students can get loans regardless of their credit rating in order to support the policy aim of encouraging students to enter higher and further education. There is no obligation to repay the loan until the borrower's income reaches a certain income threshold and there are other circumstances when the loan will be written off, for example based on the age of the student. Therefore, even though most repayments are collected by HMRC as part of the tax collection process, not all of the loans will be repaid.

Of the total student loans provided by government (£64.4 billion), the Department for Business Innovation & Skills holds £56.9 billion. The face value of the loan book was £75.8 billion compared to a balance sheet value of £56.9 billion (2014-15: face value of £64.2 billion compared to a balance sheet value of £42.2 billion). The impact of credit risk and policy decisions on repayment conditions on these loans are shown by the following table of allowances for mark-downs of impaired assets:

		2015-16		2014-15
	Balance sheet value	**Provision for impairment**	Balance sheet value	Provision for impairment
	£bn	**£bn**	£bn	£bn
Pre 2012 higher education loans	33.7	10.8	32.3	13.3
Post 2012 higher education loans	23.0	7.9	9.8	8.6
Advanced learner loans	0.2	0.1	0.1	0.1
Total student loans held by Department for Business Innovation & Skills	**56.9**	**18.8**	42.2	22.0

The table above shows that the overall level of impairment decreased during 2015-16 despite new loans being issued. This was mainly as a result of a decrease in the long-term discount rate set by HM Treasury which is used to discount future cash flows to produce a present value. There was also a £1.2 billion increase in the total amount of cash expected to be recovered as a result of the policy decision to freeze the £21,000 repayment threshold for all post 2012 higher education loans. This increase was however offset by revised short and long-term economic forecasts published by the OBR.

Balances with the International Monetary Fund (IMF) are made up of the IMF quota subscription (£19.7 billion) and IMF Special drawing rights (£7.2 billion). Special drawing rights (SDRs) are an international reserve asset created by the IMF. SDRs represent a claim to currency held by IMF member countries for which they may be exchanged. The government's holdings result from SDR allocations made by the IMF, any subsequent purchases and sales of SDRs from or to other IMF members and fair value changes.

The largest balance within **other financial instruments** is derivatives (£16.5 billion). Of the derivative balance the largest individual material balances are with the Pension Protection Fund (PPF) (£12.5 billion), and EEA (£1.6 billion). The PPF manage the risks associated with this by using counterparties rated at least A- (or subject to increased collateral) and are subject to overall exposure limits. The EEA manage the risks associated with this by counterparty and issuer limits and collateralisation. Further details can be found in the PPF and EEA accounts.

Foreign exchange rate risk

The government is mainly exposed to foreign exchange risk on the UK's official holdings of international reserves ('the Official Reserves'). Foreign currency reserves are held on a precautionary basis that could be used, when necessary, to regulate the exchange value of sterling, and is the mechanism through which any UK government exchange rate intervention would be conducted, for example in the event of any unexpected shocks.

The Official Reserves comprise two components: reserves that are hedged for currency and interest rate risk ("the hedged reserves"), and the remaining reserves which are unhedged for currency and interest rate risk ("the unhedged reserves"). The Official Reserves comprises assets held by the Exchange Equalisation Account (EEA) consisting of the UK's reserves of gold, foreign currency assets, and IMF Special drawing rights, and assets held in the National Loan Fund (NLF) comprising the UK's Reserve Tranche Position at the IMF and lending to the IMF.

The Treasury has appointed the Bank of England to act as its agent in the day-to-day management of the EEA in accordance with an agreed framework and to manage the foreign currency assets and liabilities associated with the reserves of the NLF. [14] The Bank of England monitors and controls market risk primarily by using a Value at Risk (VaR) model, which estimates a loss level that will not be exceeded at a specified confidence level, over a defined period of time, that losses will not exceed the VaR figure in 99 out of a 100 two-week periods.

The Bank reports the VaR on a benchmark reserve on a six-monthly basis. The values of the benchmark reserves are based on market-to-market prices at the end of the period.

[14] An annual Service Level Agreement between the Treasury and the Bank of England, a summary is included in a Treasury report entitled 'Management of the Official Reserves' available at https://www.gov.uk/government/publications/management-of-the-official-reserves.

Benchmark Reserves

	$ Millions 2015	$ Millions 2016
Hedged Reserves		
VaR as at 31March	102	68
Unhedged Reserves		
VaR as at 31March	1,237	1,228

In addition to foreign currency reserves, the government is exposed to foreign exchange risk through the UK's transactions with the IMF. The UK's quota subscription and lending to the IMF are both denominated in SDR and are subject to valuation adjustments by the IMF. The UK's liabilities to the IMF, although denominated in sterling, are also subject to valuation adjustments by the IMF.

Investments in financial institutions primarily relates to the value of the UK's capital investment in the European Investment Bank (EIB) of £8.1 billion (2014-15: £7.1 billion) as based on the UK's share of the EIB's net assets in euros. Therefore the government is exposed to foreign exchange rate risk on the fair value of this equity investment.

Price Risk

The Government is exposed to price risk on its shareholdings in RBS and Lloyds Banking Group. The fair value of these UK listed shares fluctuates as a result of changes in market prices. Market prices for a particular share may fluctuate due to factors specific to the individual share or its issuer, or factors affecting all shares traded in the market. The UK Financial Investments Limited (a wholly-owned subsidiary of HM Treasury) is responsible for the development and execution of an investment strategy for disposing of the investments in RBS and Lloyds Banking Group in an orderly and active way, within the context of protecting and creating value for the taxpayer.

Note 24. Public sector pensions

Pension liabilities

The public sector pension liabilities are summarised in the following table with figures separated out for each of the principal bodies with schemes. The table also shows the change in the net liabilities between 2014-15 and 2015-16.

	Scheme liabilities £bn	Scheme assets £bn	2015-16 Net liabilities £bn	2014-15 Net liabilities £bn	% change in scheme liabilities 2014-15 to 2015-16
Unfunded schemes					
NHS (UK)	443.8	-	443.8	452.2	(1.9)
Teachers (UK)	311.9	-	311.9	316.9	(1.6)
Civil Service	205.8	-	205.8	214.8	(4.2)
Armed Forces	145.2	-	145.2	154.6	(6.1)
Police	130.3	-	130.3	145.2	(10.3)
Royal Mail	38.3	-	38.3	40.3	(5.0)
Fire	26.0	-	26.0	28.9	(10.0)
Other unfunded	19.1	-	19.1	20.2	(5.4)
	1,320.4	**-**	**1,320.4**	1,373.1	(3.8)
Funded schemes					
Local government	297.3	(205.3)	92.0	106.5	(13.6)
Other funded	73.0	(60.7)	12.3	13.7	(10.2)
	370.3	**(266.0)**	**104.3**	120.2	(13.2)
Total	**1,690.7**	**(266.0)**	**1,424.7**	1,493.3	(4.6)

The Local Government Pensions Scheme (LGPS) is the largest funded scheme. The LGPS (England and Wales) consists of 91 separately administered funds, with the LGPS (Scotland) having a further 11 funds. The individual local authority employers that contributed to these funds recognised their proportion of the scheme liabilities in their statement of accounts. The local government funded schemes balance disclosed above includes the portion of the pension liability of the LGPS that was reported in the financial accounts of the individual local authority employers.

Other unfunded schemes includes schemes within the UK Atomic Energy Authority (UKAEA Pension Scheme) £6.7 billion (2014-15: £6.8 billion); and the Research Councils (RCPS) £4.2 billion (2014-15: £4.4 billion).

Other funded schemes comprise largely of schemes within Department for Education - academies in the Local Government Pension Scheme £4.0 billion (2014-15: £4.0 billion), Department for Transport - including Network Rail £3.1 billion (2014-15: £ 3.6 billion); Ministry of Justice £1.3 billion (2014-15: £1.6 billion), BBC £1.0 billion (2014-15: £0.9 billion); and Department for Environment Food and Rural Affairs £0.9 billion (2014-15: £1.2 billion).

It also includes other LGPS liabilities for bodies within the WGA boundary which are not local authorities.

In addition to updates provided in annual accounts, public sector pension schemes carry out periodic full actuarial valuations which are used to set employer contribution rates. The last full published actuarial valuations for a majority of the unfunded pension schemes were carried out as at 31 March 2012, which set the employer contribution rates for a 4 year period from 1 April 2015.

Decrease in pension liabilities

The table below breaks down the changes in the present value of scheme liabilities over the financial year.

	Unfunded £bn	Funded £bn	Total £bn
Gross Liability at 1 April 2015	1,372.80	383.7	1,756.50
Current service costs	30.1	10.1	40.2
Past service costs	1.2	0.2	1.4
Settlements/curtailments	-	(0.8)	(0.8)
Interest on scheme liabilities	48.1	12.4	60.5
Contribution by scheme participants	8.9	2.1	11.0
(Gains)/Losses on revaluation:			
Experience gains and losses arising on liabilities	(23.5)	(3.7)	(27.2)
Changes in assumptions underlying the value of liabilities	(77.1)	(24.0)	(101.1)
Benefits paid	(40.0)	(11.3)	(51.3)
Transfers in/(out)	(0.1)	1.6	1.5
Liability at 31 March 2016	1,320.4	370.3	1,690.7

Overall, the public sector pension liability decreased by £68.6 billion during the year. This is broken down as follows:

	2015-16 Total £bn	2014-15 restated Total £bn
Net liability at 1 April	1,493.3	1,303.1
Net (gains)/losses on revaluation	(123.0)	134.7
Current service costs (net of employees' contributions)	40.2	36.1
Net interest costs	52.1	56.6
Unfunded schemes benefits paid	(40.0)	(37.8)
Past service costs	1.4	0.6
Net settlements/curtailments	(0.4)	(0.7)
Contribution by unfunded scheme participants	8.9	8.9
Contribution by funded scheme employers	(8.4)	(9.1)
Net transfers in/(out)	0.6	0.9
Net liability at 31 March	1,424.7	1,493.3

As summarised in the above tables, the change in the net pension liability is largely dictated by 4 factors:

- the revaluation gain or loss, which at this year end reduces the liability but in previous years has increased the liability
- the current service costs which increase the liability
- the net interest costs which increase the liability
- the benefits paid from the unfunded schemes which reduce the liability

This volatility in the **revaluation gain or loss** is predominantly due to the change in assumptions, in particular the discount rate net of inflation and demographic assumptions. The discount rate for central government schemes is determined by those responsible for the management of the individual pension funds and is based on yields of high quality (AA) corporate bonds. The return on corporate bonds is only used to discount the future benefit payments to the present day, therefore whilst movement in the assumption has a significant impact on the liability figure in the accounts from year to year, as shown by the sensitivity analysis, it does not influence the level of benefits received by the members.

The key financial assumptions are shown in Note 2.5 and show that, for the central government unfunded schemes, the (net of CPI) discount rate increased from 1.3% in 31 March 2015 to 1.37% in 31 March 2016. The increase in discount rate decreases the present value of liabilities as the future payments will now be discounted with a greater factor. This revaluation benefit from the discount rate is recognised in other comprehensive income rather than against net expenditure.

The table below shows the approximate sensitivity of the unfunded liability to changes in key assumptions. The sensitivity will be broadly similar for the gross liability of the funded schemes.

	% change	£bn change
Increasing the assumption by 0.5% a year:		
Discount rate	-10%	-132
Rate of increase in pensions	8%	106
Rate of increase in salaries	1%	13
Increasing assumed life expectancy in retirement by 1 year:	3%	40

The **current service cost** is an estimate made by scheme actuaries of the benefit earned by employees in the year and it is used to determine standard contribution rates for each scheme. In 2015-16 these standard contribution rates increased for a number of schemes, including NHS, Armed Forces and local government, resulting in higher levels of employer's expenditure. The actual rate of employer contributions is determined as part of a funding valuation using different assumptions. They key difference between the assumptions used for funding valuations and pension accounts is the discount rate. The discount rate for accounts is set each year by HM Treasury to reflect the requirements of accounting standard IAS 19.

The **net interest cost** reflects the increase in the present value of the pension liability during the year because the benefits are one period closer to settlement. The financing cost is based on the discount rate (including inflation) at the start of the year and is calculated on the gross liability of unfunded schemes and the net liability of funded schemes. The expense from unwinding the discount rate is recognised against net expenditure.

From 1 April 2015 a majority of the unfunded schemes were reformed. Over the long term this is expected to reduce the current service cost compared to the position if the reforms hadn't taken place.

Pension assets

Funded pension schemes hold the following assets:

	Local government £bn	Other funded £bn	2015-16 total £bn	2014-15 total £bn
Equity investments	122.1	22.9	145.0	148.4
Bonds	30.8	14.1	44.9	45.3
Other	52.4	23.7	76.1	63.0
Total market value	**205.3**	**60.7**	**266.0**	256.7

The 'other' balance consisted of property, cash and other alternative assets, such as hedge funds and private equity, diversified growth funds, or infrastructure investments, which have varying levels of performance.

Increase in pension assets

The table below breaks down the increase in the fair value of funded scheme assets over the financial year.

	2015-16 £bn
Gross assets at 1 April	**263.3**
Interest on scheme assets	8.4
Actual return less interest on scheme assets	(5.3)
Contributions by employers	8.4
Contributions by scheme participants	2.1
Benefits paid	(11.3)
Assets distributed on settlements	(0.4)
Transfers in/out	0.8
Gross assets at 31 March	**266.0**

Amounts recognised in the financial statements

Amounts recognised in the Statement of Revenue and Expenditure are as follows:

	Unfunded	Funded (net)	2015-16 Total	2014-15 Total
	£bn	£bn	£bn	£bn
Current service cost	30.1	10.1	40.2	36.1
Past service cost	1.2	0.2	1.4	0.6
Settlements/curtailments	-	(0.4)	(0.4)	(0.7)
Net financing cost	48.1	4.0	52.1	56.6
Total recognised in the Statement of Revenue and Expenditure	**79.4**	**13.9**	**93.3**	92.6

Amounts recognised in the Statement of Other Comprehensive Income are as follows:

	2015-16 £bn	2014-15 £bn
(Gain)/loss on revaluation of net liabilities:		
Actual return less expected return on scheme assets	5.3	(13.2)
Experience gains and losses arising on liabilities	(27.2)	(2.6)
Changes in assumptions underlying the value of liabilities	(101.1)	150.5
(Gain)/loss on revaluation of (net) liabilities	**(123.0)**	134.7

The actual return on the assets was slightly lower than the interest on the assets over the year 2015-16 (the interest is determined based on the discount rate applicable at the start of the year).

Note 25. Capital commitments

Capital commitments comprise future commitments to capital expenditure that are contracted for but not provided for in the financial statements. Capital commitments for the acquisition of property, plant and equipment, loans and investments for capital projects and intangible assets for which no provision has been made in these financial statements amounted to £48.4 billion (2014-15 restated: £49.4 billion).

The most significant capital commitments included those reported by the Ministry of Defence of £19.1 billion (2014-15: £19.9 billion), Transport for London of £4.1 billion (2014-15: £3.7 billion), Department of Transport of £3.9 billion (2014-15: £5.0 billion) and Department for Education of £3.3 billion (2014-15: £4.0 billion). No other individual capital commitments exceeded £3.0 billion.

Note 26. Commitments under leases

Operating leases

Total future minimum lease payments under operating leases are given in the table below analysed according to the period in which the lease expires.

	2015-16 Total £bn	2014-15 Total £bn
Obligations under operating leases comprised:		
Total payments within 1 year	2.6	2.7
Total payments between 1 and 5 years	6.2	6.3
Total payments thereafter	9.4	10.2
Total future minimum lease payments under operating leases	18.2	19.2

The most significant operating leases included Department of Health of £2.8 billion (2014-15: £3.0 billion), Ministry of Justice of £1.8 billion (2014-15: £1.8billion), Department for Transport of £1.2 billion (2014-15: £0.8 billion) and Transport for London of £1.0 billion (2014-15: £1.0 billion).

Finance leases

Total future minimum lease payments under finance leases are given in the table below, analysed according to the period in which the lease expires.

	2015-16 Total £bn	2014-15 Total £bn
Obligations under finance leases comprised:		
Total payments within 1 year	0.6	0.6
Total payments between 1 and 5 years	1.9	2.0
Total payments thereafter	21.9	21.4
Total	**24.4**	24.0
Less interest element	(19.5)	(18.9)
Total present value of obligations	**4.9**	5.1

The most significant finance lease relates to a land and buildings lease entered into by the Ministry of Defence of £1.7 billion (2014-15: £1.7 billion) to provide homes for service personnel and their families.

Note 27. Commitments under Private Finance Initiative (PFI) contracts

PFI contracts recognised on the Statement of Financial Position

PFI assets are recognised on the Statement of Financial Position where the government controls or regulates the services, to whom they are provided, the price, and any significant residual interest in the asset at the end of the contract.

The net book value of PFI assets included in the Statement of Financial Position was £38.8 billion (2014-15: £42.2 billion) as at 31 March 2016. The PFI liability for the present value of capital amounts payable was £39.2 billion (2014-15: £38.5 billion).

The net present value of future obligation of £40.5 billion excluding service charges was different from the liability recognised on the Statement of Financial Position of £39.2 billion for a number of reasons. Some WGA entities included costs such as contingent rents and lifecycle replacement costs in future obligations but not in the liability figure. Some WGA entities also reported future obligations but had not recognised a liability in their accounts as the related PFI asset had not yet been commissioned.

The substance of these contracts is that the government has a number of finance leases which comprise two elements: imputed finance lease charges and service charges.

Details of the imputed finance lease charges are given in the table below:

Obligations for future periods arise in the following periods:	**2015-16 £bn**	2014-15 £bn
No later than one year	4.6	4.7
Later than one year and not later than 5 years	17.0	17.3
Later than 5 years	57.7	59.5
Sub-total	**79.3**	81.5
Less interest charges allocated to future periods	(38.8)	(40.4)
Net present value of obligations	**40.5**	41.1

Details of the minimum service charge are given in the table below:

Obligations for future periods arise in the following periods:	**2015-16 £bn**	2014-15 £bn
No later than one year	5.5	6.5
Later than one year and not later than 5 years	19.3	22.7
Later than 5 years	70.4	79.6
Total service charges	**95.2**	108.8

Future obligations arising 'later than 5 years' may arise for another 30 to 40 years, depending on the individual contract.

The PFI obligations by segment of government were:

	2015-16 £bn	2014-15 £bn
Central government departments and entities within the NHS	43.8	44.4
Local authorities	34.0	35.6
Public corporations	1.5	1.5
Gross present value of future finance lease obligations	**79.3**	81.5

Details of all of the government's PFI schemes are published on the gov.uk website.[15]

PFI contracts not recognised on the Statement of Financial Position

During the 2015-16 financial year, a number of WGA entities had PFI contracts which were not recognised on the Statement of Financial Position because the private sector contractor was, on balance, considered to have greater control over the use of the asset.

The most significant of these was a contract of £2.5 billion (2014-15 £1.6 billion) Public Finance 2 (PF2) entered into by the Department for Education. The majority of the increase in year is due to the department launching a further tranche of school improvements.

HM Treasury has considered whether assets not recognised on the Statement of Financial Position of any one entity should be consolidated as a shared ownership asset. It concluded that there are none with a significant value that should be included in 2015-16 WGA that are not already consolidated.

[15] https://www.gov.uk/government/publications/private-finance-initiative-and-private-finance-2-projects-2016-summary-data

Note 28. Other financial commitments

Commitments from other non-cancellable contracts that are not leases or PFI contracts are as follows:

	2015-16 **£bn**	2014-15 restated **£bn**
Financial commitments expiring in future years:		
No later than one year	13.9	17.9
Later than one year and not later than 5 years	18.3	16.2
Later than 5 years	5.4	5.0
Total financial commitments	**37.6**	39.1

The most significant other financial commitments are summarised below:

Entity	**Description of Commitment**	**2015-16** **Commitment £bn**	2014-5 Commitment £bn
Department of Health	Service contracts for Informatics programmes, formally known as the NHS National Programme of Information Technology, as well as commitments relating to the purchase of childhood and adult vaccines and research and development for improved health care.	4.8	4.6
Ministry of Justice	Commitments in respect to a number of non-cancellable contracts for contracted out services including the management of prisons.	3.8	4.3
BBC	Long term outsourcing arrangements for information technology, finance support and facilities management as well as programme acquisitions and sports rights.	3.5	3.4

Note 29. Contingent liabilities disclosed under IAS 37

Quantifiable contingent liabilities

Total quantifiable contingent liabilities are as follows:

	2015-16 **£bn**	2014-15 £bn
Export guarantees and insurance policies	11.6	13.4
Clinical negligence	26.7	14.0
Taxes subject to challenge	49.1	35.6
Transport infrastructure projects	7.6	6.4
Other	9.3	7
Total quantifiable contingent liabilities	104.3	76.4

Individually significant contingent liabilities with a potential liability of at least £3.0 billion are detailed below:

Department	Contingent liability	2015-16 Potential Liabilities £bn	2014-15 Potential Liabilities £bn
Department for Transport	The Department for Transport supports the delivery of the Cross Rail project, and has provided indemnities and assurances to parties carrying risks that they would be unable to bear	4.5	3.8
Export Credits Guarantee Department	The Export Credit Guarantee Department supported exports and investments through issuing and renewing guarantees and insurance policies. It issues guarantees and insurance against loss for, or on behalf of, exporters of goods and services and overseas investors from the UK, and supports the provision of fixed-rate export finance.	11.7	13.4
Department of Health	The Department of Health is the actual or potential defendant in a number of actions regarding alleged clinical negligence. In some cases, costs have been provided for or otherwise charged to the Department's accounts. In other cases, there is a large degree of uncertainty as to the department's liability and amounts involved.	26.5	14.0
HM Revenue and Customs (HMRC)	HMRC is engaged in a number of legal and other disputes which can result in claims by taxpayers against HMRC. This covers a range of cases, including Corporation Tax and VAT.	49.1	35.6

There was a decrease in contingent liabilities for the Export Credits Guarantee Department of £11.7 billion (2014-15: £13.4 billion). The main driver for this decrease was that in 2015-16 there was a significant amount of run off of business £2.8 billion compared with £1.7 billion in the prior year. Run off in 2015-16 was in fact larger than new business written in the year therefore overall 'at risk' amounts decreased.

Further information on liabilities arising from clinical negligence and taxes subject to challenge can be found in note 22 on provisions. In addition, Chapter 1 provides trend information on the government's exposure to quantifiable contingent liabilities.

Non-quantifiable contingent liabilities

Contingent liabilities can also be unquantifiable. The most significant liabilities are detailed below:

Legal claims

Non-quantifiable contingent liabilities have arisen as a result of a number of legal claims, compensation claims and tribunal cases made against a range of WGA entities, for which no reliable estimate of liability could be made.

Commitments in relation to pension scheme deficits

Non-quantifiable contingent liabilities have arisen as a result of commitments made by several WGA entities to provide funding for pension liabilities of individual pension schemes, should those schemes require deficits to be funded.

Contingent liabilities for reinsurance arising from acts of terrorism

Pool Re and Pool Re (Nuclear) are mutual reinsurance companies owned by insurers. They provide insurance cover to industrial and commercial property and nuclear facilities for damage and consequent business interruption arising from terrorist attacks in Great Britain. HM Treasury carries the contingent liability for the risk that the losses incurred by Pool Re or Pool Re (Nuclear) exceed their available resources. These arrangements are set out in the Reinsurance (Acts of Terrorism) Act 1993. Maximum potential liabilities under this arrangement are considered unquantifiable.

Civil nuclear liabilities

The Department for Business, Innovation and Skills has a range of civil nuclear liabilities arising from both the United Kingdom Atomic Energy Authority and British Nuclear Fuels Limited and obligations under international nuclear agreements and treaties.

Financial Assistance Scheme

Regulations came into force in April 2010 enabling the transfer to government of pension scheme assets that qualify for the Financial Assistance Scheme (FAS), along with their associated pension liabilities. It is estimated that the total value of assets transferred to government will reach £1.9 billion. However, it will not be possible for the Department for Work and Pensions to estimate the impact on the FAS pension liability until all the assets transfer.

Contingent liability in relation to the Channel Tunnel

The Department for Transport has a statutory liability under the Channel Tunnel Act 1987 that if, after termination of the Channel Tunnel concession, it appears to the Secretary of State that the operation of the tunnel will not be resumed in the near future, necessary steps shall be taken to ensure that the land is left in a suitable condition in accordance with the scheme.

Contingent liability in relation to Transport for London

TfL guarantees the payments of certain of its subsidiaries under a number of other service and construction contracts. It guarantees Crossrail Limited’s payments to Canary Wharf Properties (Crossrail) Limited under a Development Agreement. It has guaranteed amounts owed by London Bus Services Limited to the Fuel Cells and Hydrogen Joint Undertaking under a Grant agreement for the 3EMOTION Environmentally Friendly, Efficient Electric Motion project. It has also provided an indemnity to Berkeley 55 Limited in respect of future Mayoral CIL payments that Berkeley 55 Limited may be charged in relation to the fit out of the Crossrail station at Woolwich.

Service Life Insurance

The government provides access to life insurance for Ministry of Defence service personnel through Service Life Insurance. Details of the scheme and key features can be found at: www.sli365.com.

Note 30. Remote contingent liabilities reported to Parliament

In addition to the contingent liabilities reported in note 29, government departments additionally disclose contingent liabilities where the risk of crystallisation is remote. These remote contingent liabilities are not required to be disclosed under accounting standards but are reported here on the basis that guarantees, indemnities and letters of comfort expose the taxpayer to financial risk.

Quantifiable remote contingent liabilities

The potential costs of the government's quantifiable remote contingent liabilities are as follows:

	1 April 2015 Total restated £bn	Increase in year £bn	Liabilities crystallised in year £bn	Obligation expired in year £bn	31 March 2016 Total £bn
Guarantees	60.9	8.3	-	(0.4)	**68.8**
Indemnities	14.9	1.8	-	(0.2)	**16.5**
Letters of comfort	-	-	-	-	**-**
Total	**75.8**	**10.1**	**-**	**(0.6)**	**85.3**

Individually significant remote contingent liabilities with a potential liability of at least £5.0 billion are detailed below:

Department	Remote contingent liability	2015-16 Potential liabilities £bn	2014-15 Potential liabilities £bn
HM Treasury (Consolidated Fund Account)	The UK is liable for callable capital to the European Investment Bank (EIB). Under Article 5 of the EIB Statute, the Board of Directors may call upon each member state to pay its share of the balance of the subscribed capital should the bank have to meet its obligations.	28.3	25.8
Department for International Development	Contingent liabilities in respect of callable capital on investments in international financial institutions.	13.0	12.2
HM Treasury (Consolidated Fund Account)	This represents the UK's maximum liability from current outstanding loans to EU Member States and Third Countries for which the risk is ultimately borne by the EU Budget. Loans are issued under the following initiatives: the European Financial Stabilisation Mechanism (EFSM); the Balance of Payments Facility; and the Guarantee Fund to Third Countries.	11.6	9.1
Department for Culture, Media and Sport	The Government Indemnity Scheme indemnifies lenders to museums, galleries and other institutions when mounting exhibitions or taking long-term loans for study or display. This figure also includes non-statutory indemnities granted in respect of art on loan from the Royal Collection.	6.8	6.1
Department for Transport	The Department for Transport has contingent liabilities arising from the signing of new, replacement and extended passenger rail franchises agreements, and other agreements to encourage railways investment (£3.6 billion). It also has contingent liabilities for the HS1 concession agreement (£3.1 billion).	6.7	6.8

The contingent liability for the UK's share of callable capital to the EIB is priced in euros and the increase during 2015-16 is due to exchange rate movements. Exchange rate movements accounted for part of the increase in the UK's maximum liability from loans to EU Member States and Third Countries. In addition, the total amount lent increased in 2015-16 and the share of the UK's liability was updated based on the financing of the EU budget.

Non-quantifiable remote contingent liabilities

Remote contingent liabilities can also be unquantifiable. The most significant liabilities are detailed below:

Regional development banks and funds

The Department for International Development has entered into non-quantifiable contingent liabilities relating to the maintenance of the value of subscriptions paid to the capital stock of regional development banks and funds, such as the African and Asian Development Banks.

National Health Service

The Department of Health has entered into a number of unquantifiable or unlimited contingent liabilities with various health bodies and private companies. There were 17 unquantifiable indemnities. None of these are a contingent liability within the meaning of IAS 37 since the possibility of a transfer of economic benefit in settlement is too remote.

Nuclear matter

Indemnities have been given to UK Atomic Energy Authority (UKAEA) by the Department for Business, Innovation and Skills to cover indemnities given to carriers against certain claims for damage caused by nuclear matter in the course of carriage.

Guarantee to protect British Telecom's pension liabilities

When BT was privatised in 1984, the government gave a guarantee (contained in the Telecommunications Act 1984) in respect of certain liabilities of the privatised company. This guarantee only applies if BT were to enter insolvent winding up and is approximately the size of the BT pension scheme deficit at that point. The latest triennial valuation of the pension scheme as at 30 June 2014 valued the deficit at £7.0 billion.

Fire and Rescue Service

The Department of Communities and Local Government has unquantifiable contingent liabilities, including the Indemnity given to the Fire and Rescue Services in respect of possible incidents as a result of mass decontamination.

Note 31. Related party transactions

Related parties in the context of WGA are public sector entities that have not been consolidated into the 2015-16 WGA. The most significant WGA related party is the Royal Bank of Scotland Group plc. In the course of normal business, WGA entities entered into arms-length banking transactions with this institution, including loans, deposits, reimbursement of related expenses, payment of management fees, interest receipts and dividends. The volume and diversity of these transactions make comprehensive disclosure impractical.

Due to the nature of HM Revenue and Customs' business, it had a large number of transactions relating to taxation income with other public sector entities not within the WGA boundary.

Local government entities had transactions with municipal ports, airports and parish councils, primarily through the provision of funding. They also had transactions with local government pension schemes and record their share of the schemes assets and liabilities in their accounts. Further details are available in the 2015-16 accounts of the individual entities.

The Department for Business, Innovation and Skills, through the Skills Funding Agency, and local authorities, provided funding to further education colleges in England and Wales for research and provision of further education courses. Through the Higher Education Funding Council, it provided funding for research and higher education courses.

On 30 October 2015 the Office for National Statistics (ONS) reclassified some Private Registered Providers of social housing from the private sector to the public sector as non-financial public corporations. The Department for Communities and Local Government became the sponsor department for these bodies.

Note 32. Events after the reporting period

The following events that have occurred after the reporting period have been identified as significant to WGA. The FReM modifies financial reporting requirements for the purposes of WGA in that the requirement that the financial statements be adjusted for significant transactions or events that occur between the date of the consolidated entity's reporting date and the WGA reporting date do not apply, and therefore all such events are non-adjusting.

Article 50

On 29 March 2017 the UK Government submitted notification to leave the EU in accordance with Article 50 of the Treaty on European Union (Article 50). Since the reporting date the negotiation process was formally launched on 19 June 2017 and the EU issued a position paper setting out their principles for the financial settlement. The negotiation process between the UK and the EU will last two years. During this period the UK remains a full member of the EU with full rights and obligations arising from membership.

Any subsequent changes in legislation, regulation and funding arrangements are subject to the outcome of the negotiations. As a result, an unquantifiable remote contingent liability is disclosed in HM Treasury Annual Report and Accounts 2016-17. In accordance with accounting standards, no contingent assets can be recognised.

During this two year period, which includes the full duration of the next accounting period, the UK remains a full member of the EU with all the rights and obligations arising from membership. There are no significant impacts on the financial statements in the short term from making the formal notification.

The financial arrangements for the withdrawal from the EU remain subject to negotiation. Consequently, this is considered a non-adjusting event and there is no impact on 2015-16 financial statements.

Sale of final shares in Lloyds Bank

During financial year 16-17 Lloyds Banking Group ordinary shares decreased by £3.5bn primarily due to share sales (disposals) with a carrying value of £3.5bn, for which £3.3bn of proceeds were received. During financial year 17-18 HM Treasury sold its remaining Lloyds Banking Group ordinary shares with a carrying value of £935m, fully returning Lloyds Bank to the private sector. The proceeds received were £949m.

UK Asset Resolution (UKAR) sale of Northern Rock assets

On 13 November 2015 UKAR announced that it had agreed to sell a £13.0 billion asset portfolio of ex-Northern Rock assets to affiliates of Cerberus. This portfolio included £12.0 billion of mortgages which were sold to Cerberus in December 2015 and a further £1.0 billion of assets which completed after the end of the reporting period in April and May 2016, generating a small accounting profit.

UKAR sale of Bradford & Bingley Mortgage assets

In October 2016, UK Asset Resolution (UKAR) launched a programme of sales of Bradford & Bingley mortgage assets. On 31 March 2017, the Chancellor authorised an £11.8 billion sale of Bradford & Bingley loans acquired by the taxpayer during the financial crisis. The sale proceeds of £11.4bn (following natural run-down of £0.4bn) were received by Bradford & Bingley on 25 April 2017.

Agreement to build Hinkley Point C

The Department for Business, Energy and Industrial Strategy (BEIS) entered into a series of contracts with NNB Generation Company Limited (NNBG) to build Hinkley Point C (HPC) nuclear power plant on 29th September 2016. These include a Contract for Difference (CfD) between NNB and the Low Carbon Contracts Company, an agreed Funded Decommissioning Programme (FDP) and associated FDP documents including Waste Transfer Contracts (WTCs) between NNBG and BEIS.

The CfD includes a strike price of £92.50/ MW/h. The government is contractually committed to top up the amount that NNBG receives from the sale of electricity at the wholesale price prevailing on generation, to £92.50/ MW/h for 35 years from initial generation, or until the project has generated 910,000,000 MWh. The Fair Value (FV) of the expected payments, discounted using the derivative rate of 0.7% is £26.8 billion at inception on 29 September 2016 (figure not yet audited).

The Funded Decommissioning Programme (FDP) and related documents including WTCs concern the provision NNBG must make for their waste and decommissioning liabilities. NNBG is required to make prudent provision for its waste and decommissioning liabilities as set out in its FDP. To meet their liabilities, NNGB must set up a fund with an independent governance framework and will pay into it so that it is on track to fund the liabilities that arise from decommissioning and waste management.

Alongside the FDP, the Government has entered into two WTCs. These sets out terms on which Government will take title to and liability for the spent fuel and intermediate level waste (ILW) from the site after decommissioning in order to dispose of the waste safely. More information can be found in the 2016-17 accounts of BEIS.

Pension Court cases reform

The government is facing legal challenge on the 'transitional protection' offered in the 2013 Public Service Pensions Act to public sector workers within 10 years' of normal pension age as at 1 April 2012. Those covered by transitional protection have remained in their existing final salary pension schemes, with all others moved to the reformed career average schemes from 1st April 2015. Four workforces – the judiciary, firefighters, police and Ministry of Defence police – have claimed that transitional protection is age discriminatory, and indirectly gender and race, discriminatory. There have now been two Employment Tribunal hearings, with transitional protection found to be unlawful for the judiciary but lawful for firefighters. The government has appealed the ruling for the judiciary and the claimants have appealed the ruling for firefighters. These will now go to the Employment Appeals Tribunal, which is expected to issue a ruling in November 2017.

Note 33. Prior period adjustments

Prior period adjustments in WGA arose from WGA bodies restating, reclassifying or correcting figures in their 2014-15 accounts. The impact of the material restatements on the Statement of Revenue and Expenditure and Statement of Financial Position is shown below.

Employees' Pension Contributions were disclosed as Other Income, which did not comply with the prescribed treatment contained in the IFRS Framework. In order to realign WGA with the IFRS framework and provide comparative disclosure to other public-sector organisations, the Employees' Pension Contributions in the amount of £8.3 billion have been re-classified from Other Income to Staff Costs resulting in a reduction to the Current Pension Service Cost. 2014-15 has been re-stated accordingly.

Network Rail has been consolidated in the Department for Transport accounts for the first time in their 2015-16 group accounts. Network Rail prepares its accounts under International Financial Reporting Standards (IFRS), however there are a number of accounting policy differences between IFRS and government financial reporting as directed by the FReM. The most significant difference is that in their own accounts Network Rail value assets (£56.0 billion) at value in use, as this most closely reflects business value. However, under government financial reporting, within these accounts, assets are valued at Department Replacement Cost (DRC) which is £280.0 billion and a prior period adjustment has been done to account for this change in accounting policy.

Restatement of the Statement of Revenue and Expenditure
For the year ended 31 March 2015

	Note	2014-15 reported £bn	Restatement adjustment £bn	2014-15 restated £bn
Taxation revenue	*4*	(566.7)	-	(566.7)
Other revenue	*5*	(101.5)	8.3	(93.2)
Total public services revenue		(668.2)	8.3	(659.9)
Social security benefits	*6*	217.7	-	217.7
Staff costs	*7*	193.8	(8.3)	185.5
Purchase of goods and services	*8*	191.7	-	191.7
Grants and subsidies	*9*	57.4	-	57.4
Depreciation and impairment	*10*	45.4	-	45.4
Interest costs on government borrowing	*11*	27.6	-	27.6
Increase in provisions		26.0	-	26.0
Total expenditure on public services		759.6	(8.3)	751.3
Net expenditure on public services		91.4	-	91.4
Financing costs of long-term liabilities, including discounting	*11*	65.1	-	65.1
Revaluation of financial assets and liabilities		(4.5)	-	(4.5)
Net expenditure for the year		152.0	-	152.0

Restatement of the Statement of Financial Position
As at 31 March 2015

	Note	2014-15 reported £bn	Restatement adjustment £bn	2014-15 restated £bn
Non-current assets				
Property, plant and equipment	*12*	847.8	228.0	1,075.8
Investment property	*13*	14.9	-	14.9
Intangible assets	*14*	32.4	-	32.4
Trade and other receivables	*15*	12.7	-	12.7
Other financial assets	*16*	216.6	-	216.6
		1,124.4	228.0	1,352.4
Current assets				
Inventories	*17*	11.3	-	11.3
Trade and other receivables	*15*	133.2	-	133.2
Other financial assets	*16*	148.9	-	148.9
Cash and cash equivalents	*18*	26.8	-	26.8
Gold holdings		8.0	-	8.0
Assets held for sale		2.7	-	2.7
		330.9	-	330.9
Total assets		1,455.3	228.0	1,683.3
Current liabilities				
Trade and other payables	*19*	(108.8)	-	(108.8)
Government borrowing and financing	*20*	(235.2)	-	(235.2)
Other financial liabilities	*21*	(444.2)	-	(444.2)
Provisions for liabilities and charges	*22*	(14.9)	-	(14.9)
		(803.1)	-	(803.1)
Non-current liabilities				
Trade and other payables	*19*	(64.1)	-	(64.1)
Government borrowing and financing	*20*	(939.3)	-	(939.3)
Other financial liabilities	*21*	(98.3)	-	(98.3)
Provisions for charges	*22*	(160.4)	-	(160.4)
Net public sector pension liability	*24*	(1,493.3)	-	(1,493.3)
		(2,755.4)	-	(2,755.4)
Total liabilities		(3,558.5)	-	(3,558.5)
Net liabilities		(2,103.2)	228.0	(1,875.2)
Financed by Taxpayer's Equity:				
General reserve		(2,381.5)	1.8	(2,379.7)
Revaluation reserve		274.8	226.2	501.0
Other reserves		3.5	-	3.5
Total liabilities to be funded by future revenues		(2,103.2)	228.0	(1,875.2)

Note 34. Date authorised for issue

The financial statements were authorised for issue on 11 July 2017.

6 Certificate and Report of the Comptroller and Auditor General

Certificate of the Comptroller and Auditor General

I certify that I have audited the financial statements of the Whole of Government Accounts (the WGA) for the year ended 31 March 2016 under the Government Resources and Accounts Act 2000. These comprise the consolidated statements of: Revenue and Expenditure, Comprehensive Income and Expenditure, Financial Position; Changes in Taxpayers' Equity; Cash Flows; and the related notes. These financial statements have been prepared under the accounting policies set out within them. I have also audited the information in the Remuneration and Staff Report that is described as having been audited.

Respective responsibilities of the Accounting Officer and auditor

As explained more fully in the Statement of Accounting Officer's Responsibilities, the Accounting Officer is responsible for the preparation of consolidated accounts for a group of entities each of which appears to HM Treasury (the Treasury) to exercise functions of a public nature, or to be entirely or substantially funded from public money, which presents a true and fair view of the state of affairs of the whole of government. My responsibility is to audit, certify and report on the financial statements in accordance with the Government Resources and Accounts Act 2000. I conducted my audit in accordance with International Standards on Auditing (UK and Ireland). Those standards require me and my staff to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Treasury; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the Overview and Performance Analysis; Statement of Accounting Officer Responsibilities; Governance Statement; Remuneration and Staff Report and the Annex to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my certificate.

Basis for qualified opinion on financial statements

Qualification arising from disagreements on the definition and application of the accounting boundary

The Government Resources and Accounts Act 2000 (the Act) requires the Treasury to produce a set of accounts for a group of bodies which appears to the Treasury to exercise functions of a public nature or to be entirely or substantially funded from public money. The Act also states that the accounts should present a true and fair view and conform to generally accepted accounting practice subject to such adaptations as are necessary in the context. The Treasury has adopted a framework for the accounts which is based on International Financial Reporting Standards adapted for the public sector.

However, in note 1.3 to this account, the Treasury defines the accounting boundary for the accounts by reference to those bodies classified as being in the public sector by the Office for National Statistics. I consider that it would be more appropriate to assess the accounting boundary with reference to the accounting standards.

I also consider that the Treasury's accounting policy has not been applied consistently in 2015-16. A number of significant bodies, including Royal Bank of Scotland, have not been included in the accounts, even though they are classified by the Office for National Statistics as being in the public sector; and which I also consider should be included in the accounts in line with applicable accounting standards.

Although I cannot quantify the effect of these omissions on the accounts with certainty as I do not have information needed to identify the transactions that would have to be eliminated to provide a consolidated view, the most significant impact could be on the Statement of Financial Position. The exclusion of the following categories of bodies could affect the Statement, illustrating the potential impact:

- Royal Bank of Scotland which, as at 31 December 2015, had gross assets of £815.4 billion and gross liabilities of £761.3 billion; and
- other bodies which have estimated gross assets of £14.9 billion and gross liabilities of £5.6 billion.

Qualification arising from disagreement relating to inconsistent application of accounting policies

The Treasury's accounting policies state that the WGA is prepared on an International Financial Reporting Standards (IFRS) basis, as adapted or interpreted for the public sector context. A number of bodies consolidated in the WGA do not adopt the same framework under which the accounts are prepared. These bodies fall under the following categories:

- bodies in the local government sector that follow the Code of Practice on Local Authority Accounting in the UK;
- bodies that follow either pure IFRS or UK GAAP; and
- bodies that follow the Charities Statement of Recommended Practice.

Accounting standards require that, where the effect of such inconsistent accounting policies is material, adjustments should be made on consolidation. The Treasury has not provided a full analysis of these differences, although the accounts narrative does note some of these, and it has not been able to quantify fully the impact of the different accounting frameworks or accounting policies on the WGA, but it is material in some areas. The most significant example of the use of different accounting policies is where assets included in the WGA are not valued on a consistent basis, for example infrastructure assets held by local authorities.

Infrastructure assets held by local authorities are valued at historic cost, whereas those held by central government bodies are valued at depreciated replacement cost. The Treasury's estimate of the understatement of infrastructure assets due to the difference in valuation between historic cost and depreciated replacement cost for local authority assets is at least £257.5 billion (note 2.3 to the accounts).

Qualification arising from disagreement and limitation in audit scope from underlying statutory audits of bodies falling within the accounts.

The external auditors of the financial statements of a number of bodies that are consolidated into these accounts qualified their audit opinion. Of these, two are of material significance to the WGA, qualifications of the accounts of the Ministry of Defence and the Department for Education.

- **Ministry of Defence accounts:** The Ministry of Defence does not hold sufficient records to enable compliance with the financial reporting framework and account for the expenditure, assets and liabilities arising from certain contracts in accordance with International Accounting Standard 17, Leases. Consequently, I have concluded that the Ministry of Defence has omitted a material value of leased assets and lease liabilities from its Statement of Financial Position as at 31 March 2016 and for the relevant comparative figures. This has also led to a material misstatement of the Statement of Revenue and Expenditure for 2015-16 and 2014-15. I am unable to quantify the impact on the financial statements because the Ministry of Defence has not maintained the records or obtained the information required to comply with International Financial Reporting Standards in this respect.
- **Department for Education accounts:** The Department has recognised academy trust land and buildings of £43 billion in its Statement of Financial Position as at 31 March 2016. The audit evidence available to me was limited in respect of this balance because the departmental group was unable to demonstrate that these all met the recognition criteria for non-current assets under International Accounting Standard 16 Property, Plant and Equipment; and had been valued in accordance with the requirements of IAS 16 and HM Treasury guidance. The audit evidence available was also limited in respect of the equivalent balances reflected in the 31 March 2015 and 31 March 2014 Statements of Financial Position.

Qualification of the 2014-15 Statement of Revenue and Expenditure arising from limitation of audit scope due to a lack of evidence supporting the completeness of the elimination of intra-government transactions and balances

The 2015-16 financial statements are not qualified with respect to the elimination of intra-government transactions and balances. However, there remain material values of intra-group transactions in the 2014-15 comparative financial statements, which have not been eliminated. Accounting standards require that balances and transactions held and made between bodies consolidated into these accounts shall be eliminated in full. The Treasury has a process in place to identify intra-government balances and transactions between bodies consolidated into the accounts, and most balances and transactions have been eliminated. For 2015-16, the Treasury was able to provide additional analysis of the net impact of the remaining intra-group transactions. This was not available for 2014-15, so I was unable to evaluate the net effect of the remaining intra-group transactions in the 2014-15 comparative financial statements.

The effect of not adjusting for these could lead to a potential overstatement of up to £6.5 billion in gross income and expenditure within the Statement of Revenue and Expenditure. As I was unable to assess whether the underlying net impact of these transactions was material, my qualification regarding the lack of evidence supporting the completeness of eliminations in the 2014-15 Statement of Revenue and Expenditure remains.

Qualified opinion on financial statements

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

- the financial statements give a true and fair view of the state of the affairs of the Whole of Government Accounts as at 31 March 2016 and of its net deficit for the year then ended; and
- the financial statements have been properly prepared in accordance with the Government Resources and Accounts Act 2000.

Emphasis of matter – nuclear decommissioning provisions

In forming my opinion on the truth and fairness of these financial statements, I have considered the adequacy of the disclosures made in areas where there is significant uncertainty in the values reported in Note 2.6 to the financial statements, which concerns the uncertainties inherent in estimating the likely costs of the liabilities of the Nuclear Decommissioning Authority. As explained in the note; the lengthy timescales; final disposition plans for waste and spent fuel; timing of final site clearance; and the confirmation of site end states mean that the ultimate liability will vary as a result of subsequent information and events. This may result in significant adjustment over time to the value of the provision, which currently stands at £181.7 billion (£82.9 billion in 2014-15) as reported in note 22 to the financial statements.

Opinion on other matters

In my opinion:

- the parts of the Remuneration and Staff Report to be audited have been properly prepared in accordance with HM Treasury directions made under the Government Resources and Accounts Act 2000;
- the information given in the Overview and Performance Analysis; Governance Statement; Remuneration and Staff Report; and Annex, for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception

In respect solely of the limitations on audit scope referred to in the basis for qualified opinion paragraphs above:

- the financial statements and the parts of the Remuneration and Staff Report to be audited are not in agreement with the accounting records or returns; and
- I have not received all of the information and explanations I require for my audit.

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

- returns adequate for my audit have not been received from component bodies not visited by my staff; or
- the Governance Statement does not reflect compliance with the Treasury's guidance.

My report includes more details of the matters leading to my qualified opinion.

Sir Amyas C E Morse
Comptroller and Auditor General
11 July 2017

National Audit Office
157-197 Buckingham Palace Road
Victoria
London SW1W 9SP

Report of the Comptroller and Auditor General

6.1 **The Whole of Government Accounts (WGA) provides the most complete and accurate picture of the financial performance and position of the UK public sector in 2015-16.** HM Treasury (the Treasury) consolidates the financial activities of over 6,000 organisations into the WGA. It includes both central and local government bodies as well as public corporations such as the Bank of England, but does not include independent public sector organisations such as Parliament, the Crown Estate or the National Audit Office.

6.2 **The WGA is increasingly important to the ongoing management of the public finances and the Treasury has increased the impact and profile of the accounts**. The Office for Budget Responsibility and the Institute for Fiscal Studies use the WGA in their reports on the management and sustainability of the public finances, and the data collected for Public Corporations is shared with the Office of National Statistics every year to feed into the annual National Statistics publication. The IMF's recent evaluation of the UK's fiscal transparency has praised the WGA's wide coverage and completeness and recognises its potential relevance to policy making. The comprehensive nature of the accounts and their reach across the public sector, provides the opportunity for the Treasury to use the data to enhance its ability to assess financial risk across the sector and improve its overall approach to managing the government's finances.

6.3 **Government borrowing grew by £86.1 billion and an increase in tax revenues did not offset the increase in government expenditure caused by a rise in long-term future liabilities.** In 2015-16, the WGA net expenditure (the shortfall between income and expenditure) increased by £91.8 billion, to £243.8 billion. This is due to an increase in total expenditure from £811.9 billion to £937.7 billion, arising from a £126 billion increase in provision financing costs due to the application of a revised discount rate to calculate the value of future liabilities; a £6.7 billion increase in pension scheme costs; and a £4.8 billion increase in social security benefits. These costs are offset by an increase in overall revenues from £659.9 billion to £693.9 billion, which is largely due to an increase in Income Tax, National Insurance Contributions and Corporation Tax. Within net expenditure wages and salaries are broadly stable at £149.6 billion compared to £148.5 billion, in the light of average full-time equivalent staff numbers increasing by 27,656.

6.4 **The Treasury has significantly improved the presentation of the 2015-16 WGA to provide more insightful narrative information on the cross government finances; and the main drivers of the movements in the financial statements.** For example, the Treasury has provided comparative charts covering the major expenditure streams, income, assets, liabilities and financial risks, which show how government has evolved since 2011-12; and detail on the major movements in the valuations of assets and liabilities, focussing on the impact of the change in discount rates on provisions and pensions. This helps to inform users of the accounts of the underlying reasons for movements in the government's overall financial position and represents a significant step forward for the WGA. Collecting and presenting consistent data in this format will be important in understanding how the government is delivering its financial strategy as the new Parliament evolves and the UK exits from the European Union.

6.5 **The Treasury has taken steps to make disclosures more detailed and transparent, but the WGA lacks specific detail in key areas that would enable a full analysis of the public finances.** There remains limited information on the purchase of goods and services by government or the distribution of public spending across the regions or the main areas of government activities. As the UK exits from the European Union and the process of managing the government's deficit progresses, these disclosures and the underlying data will be increasingly relevant and useful; and will improve the ability to scrutinise the Treasury's management of the public finances.

6.6 **The utility of the WGA is affected by the timeliness of its publication and significant challenges remain for the Treasury to meet its target of publishing the accounts within nine months of the year-end.** The Department for Education, a significant component for WGA, has made progress in finalising its annual accounts and plans to publish its 2016-17 accounts in July 2017. However, the Treasury will not be able to meet its aim of publishing the WGA by the end of December until the Department for Education is able to bring together the financial results of the academy sector in the Sector Annual Report and Accounts in time for it to produce the consolidated WGA data in line with its planned timetable to meet its nine month target.

6.7 **The Treasury has made significant progress in increasing the accuracy and completeness of transactions and balances in the WGA, allowing me to reduce the scope and number of qualifications of my opinion**. The 2015-16 WGA is an accurate reflection of the use of public resources, but my opinion remains qualified. As detailed in the appendix to this report, I have removed my qualification relating to the accuracy and completeness of intra government eliminations for 2015-16; and reduced the scope of my qualification on inconsistent accounting treatments. Inconsistent accounting treatments related to local government infrastructure remain despite the Treasury working with the local government sector as the project timetable has slipped[1]. My qualifications relating to the boundary of the WGA; and the underlying qualifications in the Ministry of Defence and Department for Education have not changed for 2015-16.

Recommendations

6.8 Although responsibility for the underlying transactions lies with the various bodies included in the WGA, my recommendations are aimed at the Treasury, because of its overarching responsibilities for the management of the public finances and the preparation of the WGA. The Treasury should:

- **Continue to raise the profile of the WGA within government and embed it into the routine monitoring of the risks to public finances**. As fiscal policy evolves and the UK exits from the European Union, the Treasury should ensure it presents consistent data in the WGA. This would provide greater insight into its approach to managing the risks to the public finances; and the government's portfolio of assets, long term liabilities and potential exposures.

- **Enhance the disclosures that support the financial information in the WGA, to enable the reader to assess fully the profile of spend across government.** The Treasury should improve the disclosures in the WGA on the purchases of goods and services; and the regional allocation of spending, revenue, assets and liabilities.

- **Continue its work to improve the quality and timeliness of data within the WGA**. In cases of late or erroneous data, the Treasury should set out an action plan for ensuring improvements are made with the relevant component bodies. The Treasury should focus in particular on the impact of the Department for Education's approach to the academies sector. I recommend that the Treasury agrees an action plan for managing the flow of data from the academy sector with the Department to ensure that the accuracy and timeliness of the WGA is not adversely affected by the change in its approach to consolidating the academies.

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[1] http://www.cipfa.org/policy-and-guidance/highways-network-asset-briefing

- **Build on developments in financial management and reporting across government to remove the inconsistencies in accounting approach and policies**. Eliminating the major inconsistencies in asset valuation and ownership; liability recognition; and the application of the boundary of the WGA, would improve the usefulness of the WGA by providing a stable base within the numbers upon which to analyse the government's financial position and performance. Where other organisations or component bodies are instrumental in making progress with the removal of the residual inconsistencies, such as the Chartered Institute of Public Finance and Accountancy or government departments, the Treasury should agree the necessary steps with those bodies to ensure that progress is made.

Part One

How the WGA is being used

6.9 The WGA is underpinned by and supports the government's accruals based budgeting and financial reporting framework and is increasingly being seen as best practice around the world. The International Monetary Fund is promoting the adoption of accruals based accounting methodologies, and the development of comprehensive statements of accounts for developed countries as a mechanism for ensuring transparency and greater accuracy in the presentation and management of the public finances.[2] The IMF's evaluation of the UK's fiscal transparency in 2016 credited the WGA's 'wide institutional coverage' of the public sector along with the completeness of its wider balance sheet and reporting of in-year flows with placing the UK 'at the forefront of fiscal reporting practices worldwide'.[3] The WGA is a uniquely comprehensive product, covering over 6000 bodies; as it is the only set of audited consolidated country accounts that includes both central and local government activities.

6.10 The WGA forms a key part of the mechanisms for understanding the government's financial performance and position. Together with the statistically based National Accounts produced by the Office for National Statistics, and the Office for Budget Responsibility's forecasts of economic performance and the public finances; the WGA provides a mechanism for holding government to account for its long-term financial performance.

6.11 The WGA provides a unique standpoint that is not matched by any of the other elements of the government financial management framework. Through the WGA, it is possible to evaluate the details of government's income and spending; and the full portfolios of assets and liabilities that it holds. While the information in the WGA is incomplete in this regard, as demonstrated by the qualifications on the accounting boundary and the inconsistent accounting frameworks that are set out in appendix to this report; there is no more comprehensive record of what the government spends, receives, owns, owes and is committed to than the WGA.

6.12 The WGA's portfolio perspective is becoming increasingly valuable as the number of accounts increases, and as consistent presentation of data improve the ability to understand the details of the government's financial flows and its portfolios of assets and liabilities. I have published a series of reports which build on this portfolio level view and explore some of the major risks to public finances highlighted in the WGA, focussing on the government's pension liabilities[4]; its financial assets[5]; and provisions, contingent liabilities and guarantees[6]. These reports examine how the significant risks to the wider government balance sheet have changed in recent years and consider how government currently manages them at the macro level. I will also be presenting a similar report on government's approach to managing borrowing later in 2017.

[2] http://www.imf.org/external/pubs/ft/wp/2016/wp1695.pdf

[3] http://www.imf.org/external/pubs/ft/scr/2016/cr16351.pdf

[4] https://www.nao.org.uk/report/evaluating-the-government-balance-sheet-pensions/

[5] https://www.nao.org.uk/report/evaluating-the-government-balance-sheet-financial-assets-and-investments/

[6] https://www.nao.org.uk/report/evaluating-the-government-balance-sheet-provisions-contingent-liabilities-and-guarantees/

6.13 The WGA is helping to bring focus to government's financial management approach and facilitating the Treasury's drive to take a more active role in the management of the key cross government risks, in the following ways;:

- The information within the WGA is being used by the Treasury to inform its assessment of the risks to the government's finances and the extent of the potential liabilities that it needs to manage, which is an increasing area of activity.
- The OBR utilises the information in the WGA in the production of its Fiscal Sustainability Report;[7] and Fiscal Risk Report.[8]
- The data collected for Public Corporations is shared with the Office of National Statistics every year to feed into the annual national statistics publication.[9]
- WGA is the only place that reconciles accounting information to the National Accounts adding to the transparency of public finances.

6.14 Outside of government, the WGA is being used by a number of professional bodies indicating the WGA is becoming a key product to assist commentators to understand the government's financial position and develop best practice in fiscal management:

- The Institute for Fiscal Studies (IFS) – The IFS published an analysis of the WGA in the Green Budget for 2017, which supported its analysis of the budget and its deliverability.[10]
- The International Monetary Fund (IMF) – The IMF published an analysis of the use of consolidated financial accounts in developed countries and the role that they can play in supporting transparency, accountability and effective fiscal management.[11]

6.15 I have previously recommended that the profile of the WGA should be raised within government and for it to be used more effectively to help decision making. In its report on the 2014-15 WGA,[12] the Committee of Public Accounts also recommended that the Treasury sets out how it will ensure that the government makes better use of the WGA to inform decisions.

[7] http://budgetresponsibility.org.uk/fsr/fiscal-sustainability-report-january-2017/
[8] http://budgetresponsibility.org.uk/frr/fiscal-risks-report-october-2016/
[9] https://www.ons.gov.uk/economy/grossdomesticproductgdp/compendium/unitedkingdomnationalaccountsthebluebook/2016edition
[10] http://www.ifs.org.uk/publications/8129
[11] http://www.imf.org/external/pubs/ft/wp/2016/wp1695.pdf
[12] Committee of Public Accounts The Government Balance Sheet: 19th report of 2016-17 session: HC485

Part Two

Improving the production of the WGA

6.16 The Treasury has significantly improved the quality of the disclosures and narrative description in the WGA Overview and Performance Analysis section this year. For example, the Overview and Performance Analysis provides analysis of the major expenditure, income, assets, liabilities and financial risks; and detail on the drivers of major movements in the valuations of assets and liabilities. The trends in this information will be increasingly important to understanding how the government is delivering its financial strategy as the number of data points increases over time; the new Parliament evolves; and the UK exits from the European Union, particularly the wider impacts that are not captured by the statistical releases on the government finances.

6.17 In particular for 2015-16, the Treasury has sought to explain the major trends in net and total expenditure across government; the presentation of the risks to the public finances; the disclosure of the extent of fraud and error across the whole of government; and the net liability position. These explanations are illustrated by charts in the Treasury's Overview and Performance Analysis section of the WGA, which provide comparative data back to 2011-12. This helps to inform users of the accounts of the underlying reasons for movements in the government's overall financial position and represents a significant step forward for the WGA.

6.18 The 2015-16 WGA shows the financial impact of the government's major fiscal consolidation and growth programmes. This demonstrates the contribution a comprehensive accounting standards based picture of the government's finances can make to the transparency agenda and in demonstrating the overall impact of the government's fiscal policies. There are a number of areas where economic growth and fiscal consolidation measures can be seen within the WGA: net and total expenditure; increases in taxation revenue; revisions to the social security benefits regime under the control of the Department for Work and Pensions; and changes in the employment profile in the public sector.

6.19 There are still elements of government's activities that still lack detail in the WGA. For example, note 8 to the WGA, which shows expenditure on the purchases of goods and services by government, does not provide further analysis as to how funds have been spent, such as on consultancy and accommodation. In addition, the WGA does not include additional disclosures showing how public spending is distributed between individual regions or nations across the UK. The Treasury has included an analysis of public expenditure by function within the Overview and Performance Analysis section of the WGA for the first time this year, but this is based on statistical data rather than WGA data. This lack of granularity within the WGA reduces the ability of the reader of the accounts to evaluate the nature and extent of spend on categories of goods and services and the balance of government activities in the regions.

6.20 Since the inception of WGA, the Treasury has focused on improving the quality of the data feeding into the accounts, removing the qualifications to the audit opinion, and improving the timeliness of publication. Improving the speed of production of the WGA is crucial to its increasing usefulness. Producing a set of consolidated accounts of government's activities closer to the reporting date increases the relevance of the numbers and the ability of the government to use the trends in the financial statements to inform its financial strategy and policies.

6.21 In March 2015, the Treasury made the significant step of publishing the 2013-14 WGA within a calendar year of the reporting date. Given the scale and complexity of the consolidation, this represented an achievement. However the production and publication of the 2014-15 and 2015-16 accounts has once more fallen back to over a year after the reporting year-end, with the 2015-16 version published in July 2017. Aside from the announcement of a

General Election in April 2017, the main reason for this delay has been the difficulty the Department for Education has faced in producing its own consolidated view of its financial position and responsibilities.

Department for Education

6.22 The Department for Education (DfE) group reported net expenditure of £46.7 billion in 2015-16. This represents a significant component of the WGA and data that is essential to the production of complete accounts. £39.6 billion of DfE expenditure relates to capital and resource grants, the majority of which are to educational bodies and local authorities. Information relating to these payments is required by the Treasury to identify transactions to be eliminated in the WGA in order to provide an accurate consolidated view of the government's finances.

6.23 During 2015-16, the DfE faced continuing challenges in consolidating the growing number of academies into its accounts, which had a knock-on impact on the ability of the Treasury to produce the WGA. The 2015-16 DfE accounts were laid in Parliament on the 20 December 2016, and I provided an adverse opinion on them covering a number of issues including material levels of misstatement and uncertainty, limitations in the evidence available to me to audit academy trust land and buildings, and a number of breaches of parliamentary spending totals.

6.24 For 2016-17, the DfE has agreed with Parliament that it can separate the reporting of the academy trusts from its own financial statements and will, therefore, produce a Sector Annual Report and Accounts (SARA). The SARA will have a 31 August year end, and will consolidate the results of all of the academies independently from the DfE's own figures. This is likely to mean that the DfE is able to produce its own accounts earlier and without qualification, but there will continue to be delays in the production of the SARA into 2018. The DfE is aiming to produce the 2015-16 SARA by 31 October 2017 and the 2016-17 SARA by summer recess in 2018, which will mean that the results of the academies will not be available for inclusion in the WGA in line with the rest of government. The Treasury will, therefore, need to consider how it is to deliver the WGA for 2016-17 in the light of the differences in the reporting date between the SARA and the WGA and the timetable for the SARA's production.

Amyas C E Morse
Comptroller and Auditor General
11 July 2017

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Appendix: Scope of the audit and qualifications of the Comptroller and Auditor General's audit opinion

Summary

6.25 This part of my report explains my obligations with respect to the audit of the Whole of Government Accounts (WGA); changes to the extent and scope of the qualifications of my Audit Opinion; and why I have qualified my Audit Opinion on the 2015-16 WGA. It also provides details of the progress the Treasury has made in respect of each remaining qualification since my last report.

6.26 This is the seventh year that I have audited the WGA and I have been able to report to Parliament that these accounts are an accurate presentation of the whole of government's financial position, although I have always qualified my opinion.

6.27 The Treasury continues to make good progress towards resolving the qualification issues I have raised. I have removed my qualification related to the completeness and accuracy of intra government adjustments for the first time this year; and reduced the scope of my qualification relating to inconsistent accounting treatments. However, the remaining qualifications are more difficult to resolve.

My obligations as auditor

6.28 Under the Government Resources and Accounts Act 2000, I am required to examine and certify the WGA. International Standards on Auditing (UK and Ireland) require me to obtain sufficient evidence to allow me to give reasonable assurance that the WGA is free from material misstatement. In forming my opinion I examine, on a test basis, evidence supporting the disclosures in the financial statements and assess the significant estimates and judgements made in preparing them. I also consider whether the accounting policies are appropriate, consistently applied and adequately disclosed.

6.29 Due to the number of component bodies making up the WGA, my audit is dependent upon the work of component auditors to provide me with assurance over the accuracy of data submitted as part of the consolidation process. I send detailed instructions over the type and scope of procedures that I require to be performed to all component auditors, supplemented by training on my audit requirements where requested. I also carry out assurance work on all of the significant component audits, together with a sample of non-significant components.

Materiality

6.30 I apply the concept of materiality both in planning and performing my audit, and in evaluating the effect of misstatements on my audit and on the financial statements. This approach recognises that financial statements are rarely absolutely correct, and that an audit is designed to provide reasonable, rather than absolute, assurance that the financial statements are free from material misstatement or irregularity. A matter is material if its omission or misstatement would reasonably influence the decisions of users of the financial statements.

6.31 I calculate a materiality level before the financial statements are produced to assess the risks of material misstatement and to plan the nature, timing and extent of my audit procedures. The appropriateness of the materially threshold is considered throughout the audit and adjusted as required.

6.32 The choice of materiality requires professional judgement and, for the financial statements as a whole, I set this at £8 billion for 2015-16 which is approximately 1% of gross expenditure, although I give consideration to other benchmarks in the financial statements when setting materiality. Materiality is not only a pure quantitative measure, but also includes a qualitative aspect and my opinion is not solely based on total error being under the materiality level.

6.33 There are specific figures within the WGA which need to be disclosed in a clear and understandable way. Should there be any error in these figures, I consider the impact that these would have on the users of the financial statements even if the error is below the materiality level.

6.34 I agreed with the Treasury Corporate Audit Committee that I would report to it all corrected and uncorrected misstatements identified through my audit in excess of £100 million as well as any differences below that threshold which in my view warranted reporting on qualitative grounds.

6.35 The expenditure base for WGA may reduce in future years as public sector spending constraints continue and this could mean that my materiality level will also reduce in line with this reduced expenditure.

Scope of my financial audit

6.36 The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of my opinion which reports whether the financial statements are accurate, prepared fairly and accord with an applicable financial reporting framework. Under the Government Resources and Accounts Act 2000, I am required to audit, certify and report on the WGA.

6.37 My audit approach is risk based, informed by my understanding of the government's activities and my assessment of the risks associated with the WGA. This focusses my audit on the areas of highest risk, such as those affected by significant accounting estimates or management judgement. In this context, risk solely relates to the risk of material misstatement in the presentation of the financial statements, so a business or operational risk, on its own, is not sufficient to be considered a significant risk.

6.38 The main risks for my audit of the WGA relate to the areas of past qualification, which are set out below. These relate to three broad areas: inconsistent application of the judgements on the boundary of the WGA; inconsistent accounting treatments; and material qualification of some of the underlying accounts that feed into the WGA. I am also required to consider the following by International Standards on Auditing:

- The risk of material fraud arising from the approach to recognising revenue - which I addressed via my understanding and assessment of the approach that government has to recognising the main revenue streams via my audit of HM Revenue and Customs; and

- The risk of management using its influence to override the embedded controls that support the production of the accounts and manipulate the financial results within the WGA. For the WGA, my work is focussed on assessing the range of figures that constitute the accounts and level of adjustments that the Treasury processes to produce the consolidated figures. I addressed this via my audit of these adjustments and through my evaluation of how the transactions streams and balances within the underlying accounts that form the WGA are reflected within the consolidated financial statements.

6.39 My audit opinion on the financial statements considers the truth and fairness of the presentation of the WGA but does not consider whether the activities presented in the WGA represent value for money. I have statutory authority to examine and report to Parliament on whether departments and the bodies they fund have used their resources efficiently, effectively, and with economy and exercise these functions through my programme of value for money reports.

Removal of qualifications to the Whole of Government Accounts for 2015-16

6.40 The WGA has been qualified since its inception on multiple grounds. For 2015-16, I have been able to remove my 2015-16 qualification relating to the elimination of transactions and balances to form the WGA and reduce the scope of my qualification on inconsistent accounting treatments, due to the inclusion of a consistent valuation of Network Rail's infrastructure assets in the WGA.

Removal of the unsupported eliminations adjustments qualification

6.41 The WGA is a consolidated account which is prepared by including the financial activities of over 6,000 government controlled entities. Transactions and balances between these are removed so that income, expenditure, assets and liabilities are not overstated between bodies within the group, as required by accounting standards. To present a true and fair picture of the financial position and financial results of government, it is important that the removal of these intra-government transactions and balances is materially complete and accurate.

6.42 The Treasury collects information from each of the bodies in the WGA on all intra-government transactions with details of the relevant counter-party. The Treasury uses this data to match balances and transaction streams and remove them from the WGA. Despite the work by the Treasury, there remains uncertainty over the figures in the financial statements because of the difficulty the Treasury faces in accurately removing these transactions and balances. This uncertainty arises where:

- either of the entities declare different intra-government transactions or balances (requiring an assumption to be made as to the correct amount to remove); or
- only one entity declares an intra-government transaction or balance (a particular issue between central and local government bodies); or
- neither body declares an intra-government transaction or balance.

6.43 Using the available evidence, I have estimated the maximum level of uncertainty as being up to £7.1 billion (£6.5 billion in 2014-15) in gross income and expenditure and up to £4.4 billion (£2.6 billion in 2014-15) in gross assets and liabilities (**Figure 1**). The estimated errors reside mainly within the individual primary statements.

Figure 1

Sources of uncertainty about transactions removed and the impact on the financial statements

	Statement of Revenue & Expenditure	Statement of Financial Position
Entities declaring different intra-government transactions or balances	4.2	1.8
Only one entity declares an intra-government transaction or balance	1.4	1.6
Subtotal of errors that can be linked to specific entities	**5.6**	**3.4**
Neither entity within an expected relationship declares an intra-government transaction or balance	1.5	1.0
Impact on the financial statements (potential overstatement)	**7.1**	**4.4**

NOTES

All figures in £ billions

Source: NAO analysis of WGA 2015-16

6.44 The level of error has reduced steadily since 2010-11, and has stayed at the same level since 2013-14 (**Figure 2**). While the estimated level of uncertainty within the statement of revenue and expenditure, and the potential gross overstatement of income and expenditure has increased by £0.6 billion from the 2014-15 financial statements. The level has now been broadly stable and below my assessment of materiality, which for 2015-16 was defined as £8 billion as set out in paragraph 8 of this appendix, for the last three years. The level of this error and its stability has enabled me to consider the impact of the error on a net basis.

Figure 2

Level of potential overstatement in the WGA (£ billion)

	2015-16	2014-15	2013-14	2012-13	2011-12	2010-11
Statement of Revenue and Expenditure	7.1	6.5	7.3	9.1	16.0	22.6
Statement of Financial Position	4.4	2.6	2.2	3.7	5.1	10.4

All figures in £ billions

Source: NAO analysis of WGA 2015-16

6.45 In my report on the 2014-15 WGA, I recommended that the Treasury should undertake further work to reduce the uncertainties in the elimination of intra-government transactions and balances. During 2015-16, the Treasury produced further analysis for the 2015-16 WGA that showed the net impact of the outstanding error on the Statement of Revenue and Expenditure and the individual lines within it, which is £1.1 billion for 2015-16 as shown in **Figure 3**.

6.46 **Figure 3** also demonstrates that the areas of the Statement of Revenue and Expenditure which are impacted most significantly by the error is other revenue (£2.5 billion); grants and subsidies (£1.9 billion) followed by purchase of goods and services (£1.5 billion). Each of these areas are sections of the WGA where there are largest flows of transactions between the bodies within the accounting boundary. For each of these lines, the error does not change the presentation of the figures by, for example, transferring an increase in costs or income to a reduction. As a result, I have been able to conclude that this error is not significant in the context of the financial statements.

Figure 3

	2015-16 WGA SORE £bn	2014-15 WGA SORE £bn	Maximum net error £bn
Taxation revenue	(592.6)	(566.7)	-
Other revenue	(101.3)	(93.2)	(2.5)
Total public services revenue	(693.9)	(659.9)	(2.5)
Social security benefits	222.5	217.7	-
Staff costs	193.3	185.5	0.2
Purchase of goods and services	192.1	191.7	1.5
Grants and subsidies	54.1	57.4	1.9
Depreciation and impairment	42.7	45.4	-
Interest costs on government borrowing	28.3	27.6	0.1
Increase in provisions	9.2	26.0	-
Total expenditure on public services	742.2	751.3	3.6
Net expenditure on public services	48.3	91.4	1.1
Financing costs of long-term liabilities, including discounting	187.4	65.1	-
Revaluation of financial assets and liabilities	8.1	(4.5)	-
Net expenditure for the year and net error	243.8	152.0	1.1
Total gross error (sum of errors excluding their effect)			6.1
Impact of additional small errors			1.0
Total gross error in the SORE as per Figures 1 and 2			7.1

All figures in £ billions

Source: HMT analysis of WGA 2015-16

6.47 My overall consideration of the level of error, therefore, has taken into account:

- the stable gross error at levels below my materiality threshold (£7.1 billion);
- the level of overall net error (£1.1 billion), which demonstrates that the impact of the error on the overall presentation of the Statement of Revenue and Expenditure is immaterial by value.
- the assurance I have been able to gain that this error does not impact materially on the presentation of the individuals lines in the Statement of Revenue and Expenditure.

6.48 As a result of these factors, I have concluded that I am able to remove my qualification related to the elimination of intragroup transactions and balances for the first time for 2015-16

6.49 In order to reach this position, the Treasury has worked over the last three years to improve its analysis of the eliminations data and its approach to removing known sources of transactions between bodies within the WGA, for example transactions between central and local government. However, with such an extensive body of components preparing information, some error in the data preparation is inevitable and it is possible that the level of error cannot be reduced much further under the current method of collation and preparation of the WGA. This means that the error is unlikely to fall significantly below the level that remains within the 2015-16 WGA.

6.50 The process of eliminating transactions and balances is made more complicated by the significant level of manual intervention that is required by the Treasury to reach this level. The Treasury, therefore, needs to consider how it can improve the overall process of modelling the transactions between bodies within the WGA and introducing a greater level of automation in the process, to ensure that I am able to continue to provide a clean opinion on the process of eliminating transactions and balances. This will be increasingly important as the Treasury seeks to bring forward the timetable for the finalisation of the WGA to December following the year end of the accounts.

Inconsistent accounting treatments

6.51 For each WGA up to and including 2015-16, I qualified my audit opinion in respect of the consistency of the approach to the valuation of infrastructure assets. Network Rail's infrastructure valuation made a significant contribution to this qualification. The ONS reclassified Network Rail as a public sector body from September 2014 and it was consolidated into the WGA for the first time with effect from 1 April 2014. Network Rail values the railway network at its fair value in its own statutory financial statements. As there is no active market in railway infrastructure assets, Network Rail has derived the fair value of the network using income from the regulated asset base (RAB) as a proxy for discounted cash flows.

6.52 However, upon consolidation into government and the Department for Transport’s (DfT) accounts, an income-based valuation model for the rail infrastructure is not appropriate in light of the substance of DfT’s wide-ranging role in the rail economy and the requirements of the government’s Financial Reporting Manual.

6.53 All parties agreed, therefore, to prepare the rail network valuation on a depreciation replacement cost basis in the DfT's consolidated 2015-16 financial statements. This was successfully completed by 15 September 2016. Therefore, the WGA for 2015-16 includes £280.1 billion valuation of the rail network that has been produced on the same basis as other central government infrastructure. This means I have been able to remove this element of my qualification arising from inconsistency in accounting treatments. However, my overall qualification in this area remains due to ongoing inconsistencies in the approach to valuing local authority infrastructure as set below.

Remaining qualifications owing to disagreements and limitations of scope in my audit

6.54 I have qualified my opinion on the 2015-16 WGA because, in a number of significant areas, the WGA does not comply with International Financial Reporting Standards as adapted for the public sector context, and this has a material effect on the figures presented.

6.55 My qualifications relate to:

- the definition of public bodies that the Treasury has used to determine the boundary of the WGA; and
- the inconsistent application of accounting standards.

6.56 I have also limited the scope of my opinion on the 2015-16 WGA because of the following issues which meant I was unable to obtain sufficient and appropriate audit evidence on which to base my opinion in certain areas:

- material issues arising within the audit opinions of accounts included in the WGA where component auditors have limited the scope of their audit.

Qualified audit opinion relating to the WGA boundary

6.57 I have qualified my opinion because, in my view, the Treasury has not complied with applicable accounting standards in determining which bodies to include in the WGA. Significant assets and liabilities have therefore been left out of the financial statements.

6.58 I cannot quantify the impact of this on the WGA with certainty, as I do not have information needed to identify the transactions that would have to be eliminated to provide a consolidated view. However, for illustrative purposes, I have examined the impact of adding the gross assets, liabilities, income and expenditure published in the individual accounts of public sector bodies that the Treasury did not include in the WGA. Although these figures are only illustrative, they demonstrate that the exclusions represent material omissions from the WGA (**Figure 4**).

Financial reporting requirements

6.59 In my previous Reports[13], I have noted that in determining the boundary for the whole of government, the Treasury has adopted the classifications of public bodies used by the Office for National Statistics (ONS), rather than apply accounting standards which require including bodies that are subject to government control and that define control as 'the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities'.[14]

6.60 As a consequence of the Treasury adopting statistical, rather than accounting, standards when it comes to defining 'control', the WGA excludes a number of significant bodies. The Treasury has also not applied its own criteria consistently as there are a number of bodies that fall within both statistical and accounting definitions of government 'control' but have not been included in the WGA. These include:

- bodies that are not controlled by government, such as Parliament;
- a number of small bodies that have not been consolidated on the basis of size; and
- other bodies that are partly or wholly owned by the government, such as the Royal Bank of Scotland.

[13] Comptroller and Auditor General, Report on the Whole of Government Accounts 2014-15, May 2016
Comptroller and Auditor General, Report on the Whole of Government Accounts 2013-14, March 2015
Comptroller and Auditor General, Report on the Whole of Government Accounts 2012-13, June 2014
Comptroller and Auditor General, Report on the Whole of Government Accounts 2011-12, July 2013
Comptroller and Auditor General, Report on the Whole of Government Accounts 2010-11, October 2012
Comptroller and Auditor General, Report on the Whole of Government Accounts 2009-10, November 2011
[14] International Financial Reporting Standard 10 – Consolidated Financial Statements.

6.61 I consider it appropriate to exclude those bodies that are not controlled by the government, as this treatment meets with accounting standards; and that it is acceptable to exclude the small bodies as they do not represent a significant exclusion from the WGA. By adopting generally accepted accounting standards, I consider that the Royal Bank of Scotland, further education institutions and trust ports, as listed in **Figure 4**, should be included in the WGA. However, despite the government's controlling shareholding in RBS, which means I need to include it within the qualification on technical grounds, I support the Treasury's exclusion of RBS from the WGA as its scale and the nature of its activities would distort the reflection of government's core activities within the financial statements.

Figure 4

Gross accounts figures from bodies that have been excluded from WGA as compared to the total figures in the WGA (for illustrative purposes)

	Revenue	Expenditure	Impact on the net deficit	Assets	Liabilities	Impact on the net liability
Royal Bank of Scotland	19.4	20.6	(1.2)	815.4	761.3	54.1
Further education institutions	-	-	-	13.0	5.1	7.9
Trust Ports	0.3	0.3	-	1.5	0.4	1.1
Other	-	-	-	0.4	0.1	0.3
Total excluding RBS	**0.3**	**0.3**	**0**	**14.9**	**5.6**	**9.3**
Total	**19.7**	**20.9**	**(1.2)**	**830.3**	**766.9**	**63.4**

NOTES

1. No amounts have been included for income and spending of Further Education Institutions because the majority of their operations are funded through government grants, which are included in Note 9 to the WGA. Their assets and liabilities have been estimated from data provided by Skills Funding Agency (covering England only) for 2010-11.
2. Trust Ports - figures have been estimated from available accounts for year-ended 31 December 2015.
3. London Councils and other minor bodies.
4. The bodies have been treated as if they had always been entirely owned by the public sector. For Royal Bank of Scotland, no account has been taken of the residual private sector shareholdings or intra-government transactions and balances.
5. Not all bodies have a March year-end, e.g. figures for the banks relate to the year ending 31 December 2015.
6. All figures are in £ billions.

Source: NAO analysis of WGA 2015-16 and published accounts.

Progress since 2014-15

6.62 There has been progress in including the appropriate bodies in the 2015-16 WGA as Further Education Institutions in Scotland and Northern Ireland have been brought into the WGA for the current year and the Treasury has restated the balances for 2014-15 as far as is necessary.

6.63 The position of the remaining elements of the qualification is as follows

- **Royal Bank of Scotland**: As at the date of this report the government’s ownership of the Royal Bank of Scotland continued to exceed the generally accepted threshold of control. The Treasury continue to account for its holding of 72 percent of the share capital as an equity investment.

- **Further education institutions**: In my Reports on the WGAs for 2011-12[15] and 2010-11,[16] I recommended that the Treasury should review its criteria for including bodies within the WGA, taking into account changes in the control government exerts over English further education institutions following the passage of the Education Act 2011. The Treasury continues to exclude English institutions from the WGA as the ONS determined that these bodies fall outside of the public sector following the 2011 Act.[17] However, under accounting standards, there remains in my view sufficient government control to warrant their inclusion.

- **Trust Ports**: The Treasury is considering the status of Trust Ports with a view to bringing them within the 2017-18 WGA.

6.64 Although the Treasury continues to make progress in consolidating more bodies into the WGA, my qualification on this matter is likely to remain until all significant government controlled entities are included in line with accounting standards. As a result, I am unlikely to include the technical qualification on the WGA boundary until the government sells a significant proportion of its shareholding in the Royal Bank of Scotland.

Qualification arising from disagreement relating to the inconsistent application of accounting policies

6.65 I have qualified my opinion due to the impact of the inconsistent application of accounting policies.

6.66 The financial reporting framework that WGA must follow is set out in the government Financial Reporting Manual which applies International Financial Reporting Standards (IFRS), as adapted for the public sector context. However, for 2015-16, some of the bodies included in the WGA prepared their accounts based on accounting frameworks that are inconsistent with the requirements of the Financial Reporting Manual.

6.67 Under accounting standards, the Treasury should identify the impact of the different frameworks and make appropriate adjustments to the WGA, where material, so that the WGA is prepared on the same basis.[18] I do not have the information to fully quantify the effect of all inconsistencies that exist as a result of inconsistent financial reporting frameworks, however it is clear that there are material inconsistencies within the 2015-16 WGA.

Local government infrastructure valuation

6.68 Material misstatement in the WGA arises from differences between the financial reporting frameworks used by local government, which requires local authorities to value their infrastructure assets using historic cost, and central government which values assets at their depreciated replacement cost, in line with the requirements of the government Financial Reporting Manual.

6.69 Local authority infrastructure assets consist primarily of local highways infrastructure but also of other assets such as coastal defences, airports and light rail, including the London underground network.

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15 C&AG's Report within Whole of Government Accounts 2011-12, HC531, July 2013, Paragraph 2.29.

16 C&AG's Report within Whole of Government Accounts 2010-11, HC687, October 2012, Box 6, paragraph 7.69.

17 http://www.ons.gov.uk/ons/rel/na-classification/national-accounts-sector-classification/classification-update---may-2012/reclassification-of-further-education-corporations-and-sixth-form-colleges-in-england---article.html#tab-Executive-Summary

18 International Accounting Standard 27 – Consolidated and Separate Financial Statements

6.70 The Treasury notes that the 2016 National Accounts[19] estimates the value of the road network at £322.6 billion (2014: £306.6 billion) as at 31 December 2015. On this basis, road infrastructure assets alone are likely to be understated by at least £257.5 billion.

Progress since 2014-15

6.71 In my Report on the 2014-15 WGA, I recommended that the Treasury should continue to support the Chartered Institute of Public Finance and Accountancy (CIPFA) in considering the basis of valuing assets and take steps to ensure that data collected is considered reliable.

6.72 CIPFA has recently announced that it no longer plans to pursue a revised approach to valuing local authority infrastructure, due to a lack of commitment from government to fund the central costs of producing the valuation.[20] Therefore, it is currently unclear whether the project to amend the Code of Practice on Local Authority Accounting to require local authorities to account for their highways infrastructure assets using depreciated replacement cost accounting in their own financial statements will be completed. This means that it my qualification on this matter is likely to, unless the Treasury finds a mechanism for resolving this issue.

6.73 The Treasury should work with CIPFA to address the limited funding difficulties and ensure that the planned changes to the Code of Practice on Local Authority Accounting are brought back on track or an alternative approach to achieving a consistent valuation of infrastructure assets is defined. Treasury should also put in place plans to obtain depreciated replacement cost values for the remaining non-highways infrastructure assets.

Qualification arising from disagreement and limitation of audit scope from underlying statutory audits of bodies falling within the Account

6.74 Where the external auditors of bodies in the WGA qualify their opinions on the statutory financial statements, I am required to consider the impact of these 'true and fair' qualifications on my opinion on the WGA. In 2015-16, external auditors qualified their opinions of 10 accounts (6 accounts in 2014-15).

6.75 The most significant of these qualifications relate to the departmental accounts of the Ministry of Defence and Department for Education for 2015-16. Given the significance of these qualifications, I have also qualified my opinion on the WGA.

6.76 Further details can be found in my audit opinions and within the annual accounts of the Department for Education[21] and the Ministry of Defence.[22]

Progress since 2014-15

Ministry of Defence

6.77 In the 2014-15 Ministry of Defence annual report and accounts, the Ministry states that it has conducted a review of its most significant contract arrangements and has identified a number of lease type arrangements which are not currently recognised and cannot be accurately quantified. The Ministry has, in agreement with the Treasury, decided not to obtain more detailed information on its leases on the grounds that doing so would not represent value for money. In 2014-15, the Ministry confirmed that it is possible to account for existing contracts in compliance with IAS 17, but this would create significant challenges for the Ministry. This position remains for the 2015-16 accounts, though the Ministry has agreed to undertake an

[19] Office for National Statistics, The UK national balance sheet: 2016 estimates, Table 9, August 2016
[20] http://www.cipfa.org/policy-and-guidance/highways-network-asset-briefing
[21] Department for Education Annual Report and Accounts 2015-16, HC 326 20 December 2016
[22] Ministry of Defence Annual Report and Accounts 2015-16, HC 342, 14 July 2015

exercise during 2016-17 to determine the feasibility of implementing lease accounting for new contracts which involve single use contractor sites and assets.

6.78 Consequently, no conclusion can be drawn as to whether the existing contracts represent leases and the financial impact of the omission of potential assets and liabilities cannot be determined with sufficient accuracy. This decision will have an ongoing impact on the audit opinion I am able to provide on the financial statements for the foreseeable future.

Department for Education

6.79 The 2015-16 Department for Education (DfE) accounts were qualified on the basis of incomplete and inaccurate valuation of academies' land and buildings assets.

6.80 In 2015-16, the number of academies continued to increase but the DfE has not addressed the difficulty in consolidating them. As a result, the scope of this issue has grown to £43 billion during the year. The DfE has agreed with Parliament that the academies will be brought together in a Sector Annual Report and Accounts (SARA), which will stand aside from its own consolidated figures. However, the SARA will not address the underlying challenge of obtaining an accurate valuation of the academy land and buildings. Therefore, this is likely to continue to be a source of continued qualification within the WGA until the problems with the accuracy of data and oversight are addressed.

Other issues on which I have not qualified my opinion

6.81 There are two other issues that I wish to draw attention to, although I have not qualified my opinion for these issues:

- I have included an emphasis of matter paragraph in my audit opinion for one account that is significant to the WGA. This relates to the uncertainties in estimating costs of the liabilities of the Nuclear Decommissioning Authority. This value has been calculated based on reasonable assumptions, but could change with future events.
- The external auditor of 17 accounts[23] (18 in 2014-15) included in the WGA qualified their audit opinions owing to the existence of material irregular transactions; that is not using resources in accordance with Parliamentary intentions. Of these, two are of significance to the WGA and cover error and fraud in benefit payments and tax credit payments. These irregularities have led me to qualify my regularity opinion on the financial statements of the Department for Work and Pensions[24] and HM Revenue and Customs[25]. Because the scope of my audit of the WGA, which is set out in the Government Resources and Accounts Act 2000, does not require me to provide an opinion on regularity, irregular transactions do not lead to a qualification of my audit opinion on the WGA.

[23] Included in this number are four accounts qualified on a 'true and fair' basis.

[24] Department for Work and Pensions Annual Report and Accounts 2015-16, Session 2016-17, HC331, 7 July 2016

[25] HM Revenue and Customs Annual Report and Accounts 2015-16, Session 2016-17, HC338, 14 July 2016

A Comparison to the National Accounts

A.1 The numbers reported in WGA are based on accounting standards. Whilst accounting standards provide a comprehensive picture, government typically reports on the public finances using National Accounts rules which apply internationally agreed standards for measuring economic activity. This reporting is carried out by the independent Office for National Statistics (ONS) and is available to a much shorter timescale than WGA.

A.2 Although there are differences between the two frameworks, there is more that is common and the two views can be combined to provide a more complete picture of government's fiscal risk. For example, the Office for Budget Responsibility (OBR) independently assesses the future sustainability of the public finances through its annual Fiscal Sustainability Report and utilises information on long-term liabilities published in WGA.

A.3 The rest of this chapter explains the differences between accounting standards and national accounts and then provides a reconciliation from WGA to the National Accounts.

Comparison between accounting standards and National Accounts

A.4 The accounting standards followed by WGA are International Financial Reporting Standards (IFRS) and the statistical rules followed by the National Accounts are set out in the European System of Accounts (ESA). Both frameworks have core similarities:

- They are both prepared on an accruals basis (recognition of economic events regardless of when cash transactions occur)
- They each prepare a statement of financial position, income and expenditure analysis and details of other changes
- They both exclude future tax revenue, future assets, and liabilities that will be incurred in the future (such as future benefit and state pension payments).

Comparing WGA expenditure to the Public Sector current budget deficit

A.5 The public sector current budget deficit is an important balance in the fiscal framework. The current budget deficit is the difference in the financial year between accrued current revenue and expenditure as defined in the National Accounts.

A.6 One of the main differences between the current budget deficit used in National Accounts and total expenditure used in WGA is that the National Accounts exclude the financing costs of long-term liabilities as set out in the previous section. Instead, the National Accounts recognise these liabilities when they are due to be paid.

Comparison to Public Sector Net Debt

A.7 Public sector net debt can be defined as the public sector's consolidated gross debt, less its assets that could be readily sold as defined in the National Accounts.

A.8 The difference between the National Accounts and WGA measures of public sector net debt and net liabilities is primarily due to differing treatments of the public sector pension liability, property, plant and equipment and provisions.

Differences between WGA and National Accounts

A.9 The differences between IFRS and ESA in how they recognise and value certain assets, liabilities and items of expenditure are summarised below.

Differences between WGA (IFRS) and National Accounts (ESA)

Area	WGA treatment	National Accounts treatment
Grants to fund capital expenditure	Is recognised as an expense in-year as it doesn't result in an asset for government	Is always capitalised on the basis that it results in an asset in the wider economy
Research and development expenditure	Can be capitalised if it is likely to result in an asset but is frequently recognised as an expense in-year	Is capitalised more frequently on the basis that it is an investment lasting for more than one year
PFI	Most PFI assets and liabilities are recognised on balance sheet after assessing control of the assets. PFI payments are apportioned between repaying debt, paying interest and paying for services	Most PFI assets and liabilities are not recognised on the balance sheet after assessing risks and rewards. Payments under PFI contracts are recognised as a current expense in-year for off balance sheet schemes and a capital expense in-year for on balance sheet schemes.
Depreciation of assets	Is calculated for each asset individually based on its estimated useful economic life and residual value	Is calculated using standard statistical models, high level data and asset life assumptions.
Revaluation and impairment of assets	Assets are revalued as set out in note 1 of the accounts. Assets are assessed annually for impairment compared to their carrying value	Assets are recognised at cost less depreciation and are not revalued. Only impairments caused by obsolescence or accidental damage are recognised
Profit or loss on sale of assets	Recognised as income or expenditure	Proceeds of sale are recognised but not the profit or loss
Gilts	WGA bodies hold gilts at fair value, these are eliminated out on consolidation and all the remaining gilts are held at amortised cost	Gilts are included based on their redemption price
Public sector pensions	Recognises expenditure when rights accrue to employees, even though payment is not due	Recognises expenditure as it is paid to retirees. The future liability for current employees is not recognised
Provisions	Recognises expenditure when it becomes probable that a payment will be needed as a result of past events	Recognises provisions only when they are settled (i.e. there are actual payments). Amounts expected to be paid out in future as a result of past events are not recognised
Effects of discounting future liabilities	Future cash flows are discounted to estimate the value of the liability. Changes to the cash flows and discount rate are recognised in-year	Not included
Transactions within government	Transactions are eliminated entity-by-entity in a process that takes several months. The residual elimination error is quantified and subject to audit	Transactions are eliminated using a quicker and higher-level approach. The residual elimination error can't be quantified
Asset Purchase Facility	Shows gilt purchases at fair value	Records the gilt purchases at nominal value
UK Asset Resolution (UKAR)	Includes both the liabilities and the assets.	Includes UKAR's own debts to the private sector and exclude their non-liquid financial and other assets
Housing associations	Not included within the WGA boundary	Included in the National Accounts boundary

Reconciliation to Public Sector Net Debt

A.10 Public Sector Net Debt is a measure that is calculated from the National Accounts. The government's preferred measure of Public Sector Net Debt excludes public sector banks. It equals external borrowings less liquid financial assets. The same figures can be compiled from WGA but the total net liabilities recognised within WGA are more extensive than those recognised in Public Sector Net Debt. This is partly because Public Sector Net Debt is only part of the National Accounts balance sheet and partly because WGA recognises additional assets and liabilities which are not included on the National Accounts balance sheet.

Public Sector Net Debt compared to total WGA net liabilities

	2015-16 £bn	2014-15 restated £bn	2013-14 £bn
Public Sector Net Debt (National Accounts)	1,606	1,554	1,458
Add liabilities not recognised in National Accounts:			
Net public sector pensions liability	1,425	1,493	1,303
Provisions	306	175	155
PFI contracts	33	33	33
Adjust assets measured differently in national accounts:			
Asset Purchase Facility	(50)	(49)	(46)
Unamortised premia on gilts	38	35	29
UKAR net impact on net debt	(30)	(50)	(74)
Add assets and liabilities excluded from measure of PSND:			
Property, plant and equipment	(1,120)	(1,076)	(812)
Investment property	(16)	(15)	(14)
Intangible assets	(33)	(32)	(32)
Trade and other receivables	(37)	(35)	(37)
Prepayments and accrued income	(87)	(78)	(80)
Inventories	(10)	(11)	(12)
Investments	(50)	(73)	(23)
Trade and other payables	51	49	47
Accruals and deferred income	55	54	44
Deduct liabilities not yet recognised in WGA			
Housing associations	(64)	(60)	(56)
Other adjustments including eliminations	(31)	(39)	(43)
Net liabilities (WGA)	1,986	1,875	1,840

A.11 The reconciling amounts included in the table above are calculated as the difference between the value of a balance in WGA and the value of the same balance in the National Accounts. These amounts are therefore not directly comparable to the amounts included in the Financial Statements in Chapter 5.

Reconciliation to Public Sector Current Budget Deficit

A.12 Public Sector Current Budget Deficit is also calculated from the National Accounts and the government's preferred measure excludes public sector banks. Total net expenditure in WGA is higher than the Public Sector Current Budget Deficit primarily because it includes expenditure on long-term liabilities. By comparison, net expenditure on public services in WGA is in line with the Public Sector Current Budget Deficit.

Public sector current budget deficit

	2015-16 £bn	**2014-15 restated £bn**	**2013-14 restated £bn**
Public sector current budget deficit (National Accounts)[1]	**40**	58	71
Add expenditure on liabilities excluded from National Accounts:			
Increase in provisions	-	18	9
Adjust expenditure calculated differently from National Accounts:			
Depreciation and amortisation	(8)	(10)	(10)
Impairments and revaluations of assets	9	15	21
Net losses on sale of assets	(6)	(2)	(4)
Capital grants	7	8	11
Research and development	3	3	3
Other adjustments including eliminations	4	2	(17)
Net expenditure on public services (WGA)	**49**	92	84
Financing costs of long-term liabilities, including discounting	187	65	57
Revaluation of financial assets and liabilities	8	(5)	5
Total net expenditure (WGA)	**244**	152	146

A.13 The reconciling amounts included in the table above are calculated as the difference between the value of a transaction in WGA and the value of the same transaction in the National Accounts. These amounts are therefore not directly comparable to the amounts included in the Financial Statements in Chapter 5.

[1] ONS Statistical Bulletin, Public Sector Finances, January 2017

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