

EXPLANATORY NOTE: TREASURY SPENDING DATA

1. This note provides a full commentary on the departmental expenditure data presented in Annex B of the Treasury's May 2003 departmental report. It explains how spending by the core Treasury – the organisation now wholly based in 1 Horse Guards – and other Government bodies are included in the spending statistics for the departmental group. It also provides full details of the cost of core Treasury administration. The note highlights and explains the effect that changes to the nature of departmental financial reporting and the public expenditure framework, as well as changes to the structure of the Treasury departmental grouping for reporting purposes have had on the presentation of expenditure data in the Treasury's departmental report.
2. The data presented describe a stable core Treasury that has seen a rise in administrative spending, mainly incurred as a result of moving from obsolete accommodation and the filling of vacancies.

Scope of the Treasury's Accounts

3. As with all departments, since the financial year 2001-02 the Treasury's accounts have been prepared in accordance with United Kingdom generally accepted accounting principles (UK GAAP), modified as necessary for the public sector following advice from the independent Financial Reporting Advisory Board (FRAB). These are reflected in the resource accounting manual (RAM), (available at www.resource-accounting.gov.uk).
4. The accounting rules set out in the RAM determine the range of entities consolidated into the Treasury's accounts and the investments shown on its balance sheet. As a result of these accounting rules, the Treasury's accounts and balance sheet includes:
 - a. the core departmental Treasury, now entirely based in 1 Horse Guards;
 - b. the Office of Government Commerce (OGC), including the properties of the former Property Advisers to the Civil Estate;
 - c. the Debt Management Office (DMO);
 - d. the value of the Bank of England, which is reflected in the accounts as an investment on which a dividend is received and on which a

cost of capital charge is payable (the RAM requires a cost of capital charge to be levied on the department's net assets to reflect the opportunity and financing costs of capital);

- e. monies separately voted by Parliament for the supply of coinage;
 - f. other costs include a variety of spending not directly relating to the business of a finance and economics ministry. Examples include the Civil List, the salaries and pensions of UK members of the European Parliament, grants-in-aid to certain Parliamentary bodies such as the Commonwealth Parliamentary Association, and the costs of issuing UK honours.
5. Costs and credits associated with non-core Treasury entities such as the Bank of England result in significant year-on-year changes in the total departmental public spending numbers. HM Treasury's annual resource accounts, which have been laid before Parliament with a clean audit opinion from the Comptroller and Auditor General, the head of the National Audit Office, give a full account of the costs relating to these entities.
6. The need for greater disaggregation in published tables has already been noted by the Treasury's Audit Committee, which, in line with best practice, was reconstituted earlier this year. The Audit Committee now has an independent Chairman from the commercial accountancy sector.

What the data show for the core Treasury and other entities

The core Treasury

7. Table 1 provides a breakdown of the figures presented in Table B5 of the departmental report for core or central¹ Treasury's administration costs from 1998-99 and ending in 2005-06, when the current spending review period ends.

Table 1: Core Treasury administration costs – an analysis (1)

¹ In this note, unless otherwise specified, 'core Treasury' refers to the costs associated with the staff, building and other operations for the organisation now wholly based in 1 Horse Guards. 'Central Treasury', the term used in the departmental report, is wider as it reflects asset holdings in the Bank of England on the Treasury's balance sheet, which, as noted elsewhere in the note, give rise to additional and substantial charges.

£ million	1998-99 Outturn	1999-00 Outturn	2000-01 Outturn	2001-02 Outturn	2002-03 Estimated Outturn	2003-04 Plan	2004-05 Plan	2005-06 Plan
Central Treasury net administration costs								
Ongoing costs								
<i>Paybill</i>	35	36	38	41				
<i>Other costs (2)</i>	28	23	26	25				
Total ongoing costs	63	59	64	66	73	76	80	84
Write-down of GOGGS		23						
Recurring costs of 1 Horse Guards Road					11	16	16	17
Fit-out costs					2			
Reclassification from capital					4	1	1	1
Disposal of Allington Towers					3			
Total central Treasury admin costs	63	82	64	66	93	92	96	101

NOTES

- (1) Excludes the Debt Management Office and the Office of Government Commerce
- (2) The rise in ongoing costs from £66 million to £73 million between 2001-02 and 2002-03 reflects the costs of filling vacancies (£5 million) and general inflation (£2 million). Full details are given in paragraphs 9 and 10 of this note.

8. Between 1998-99 and 2001-02 total Treasury administration costs were broadly flat at around £60 million to £65 million. The spike in administration costs in 1999-2000 is due to the writing down to zero of the value of the Treasury's former Parliament Street accommodation (Government Offices, Great George Street or GOGGS). This write down followed an independent valuation of the building's market value, in line with accounting standards (in particular, Financial Reporting Standard 11).
9. Total spending on Treasury administration costs increased by **£27 million** between 2001-02 and 2002-03. Of this £27 million, **£16 million is costs related to the move to new accommodation, both recurring and non-recurring:**
- the **recurring cost** is the unitary payment to the Treasury's Private Finance Initiative (PFI) partner. This comes to **£11 million** in 2002-

03, and rises in future years because the costs in 2002-03 relate only from the period when occupancy began, which was August 2002;

- the **non-recurring costs** relate in part to a **£3 million** charge paid to the Home Office in relation to the lease on the Treasury's former secondary accommodation in Allington Towers, Victoria. This reverse premium was largely determined by the cost of the works needed to bring it back into its original condition. The Treasury also faced costs of removals, and of fitting out the new accommodation of around **£2 million**.

10. The Treasury did not pay any rent on its GOGGS accommodation and its market valuation of zero meant that no depreciation or cost of capital charge was payable, in line with best accounting practice. The small total cost of accommodation for the Treasury – reflected in a charge for the secondary accommodation in Allington Street – did not represent a sustainable position for the Treasury. The GOGGS building was in very poor condition – its valuation at zero reflecting its obsolescence. The capital cost of essential works to bring the GOGGS building to an acceptable standard (as estimated independently in 1999) was well above £50m. Such works would simply have made the existing building safe for occupation, and would have done nothing to modernise the Treasury's working arrangements. In short, under the new arrangements and best practice financial disclosure, the Treasury's accounts now reflect the full economic cost of its accommodation.

11. The National Audit Office have examined in detail the value for money aspects of the refurbishment project. In its report of November 2001 it noted the success of the innovative competitive funding scheme which produced savings of £13 million over the lifetime of the PFI deal – a view subsequently also recorded by the Committee of Public Accounts.

12. Another set of costs relate to the increase in core Treasury **staffing**, following the filling of vacancies. These costs increased by **£5 million** in 2002-03 as against 2001-02. As reported to the Committee the Treasury is now fully staffed for the first time in a number of years.² Staff numbers are expected to

² At the time of the publication of the Departmental report, the split between pay and non pay costs in Table B5 of Annex B had not fully taken account of this.

remain at current levels until the end of the present spending review period in 2005-06, but remain around or below the level following the completion of the Treasury's fundamental expenditure review in 1995, when the Treasury employed over 1,100 people, and below the annual average of around 1,150 in the 1990s as a whole.

13. There is also an additional factor which is a **£4 million** reclassification to administration costs from the capital budget. The reason for this is that some expenditure previously counted as capital is now classified as administrative expenditure because the threshold under which certain payments are defined as administration has been increased, in line with revised accounting policy agreed with the National Audit Office. This has no effect on total Treasury spending.
14. The staffing costs, along with a general rise in costs not separately identified in this note in line with the rate of inflation, account for the **£7 million** rise – from £66 million to £73 million – in ongoing costs at the beginning of Table 1.
15. In the years following 2002-03, the Treasury's administration costs continue at broadly the same level or slightly above. This is because although some of the costs associated with the new accommodation do not recur, the unitary charge increases to around **£16 million** to reflect its full year cost, rather than simply the period August to March as in the 2002-03 period. There is also the ongoing cost associated with the new staff recruited to fill previous vacancies and provision for further modernisation of the department.
16. All the expenditure incurred or planned for the period covered by the data is within the Departmental Expenditure Limit (DEL) for the Treasury, and expenditure incurred to date has been voted by Parliament.

HM Treasury total public spending and the resource and capital budgets

17. Table 2 provides a breakdown of the resource budget for the Treasury group – both the core Treasury and other entities – found in Tables B1 and B2 of the departmental report. It also provides a reconciliation between central Treasury administration costs presented in Table B5 and the central Treasury resource budget from Table B2.

Table 2: The Treasury group resource budget

Resource budget, £ million		1998-99 Outturn	1999-00 Outturn	2000-01 Outturn	2001-02 Outturn	2002-03 Estimated Outturn	2003-04 Plan	2004-05 Plan	2005-06 Plan
Central Treasury admin costs	B5	63	82	64	66	93	92	96	101
Plus									
Bank of England capital charge and dividend			52.5	-15.5	48	109	90	90	90
Exceptional charge on 1 Horse Guards						69			
Other		-3	-10.5	-1.5	3	15	8	10	11
Central Treasury resource budget	B2	60	124	47	117	286	190	196	202
Bank of England services	B2	13	13	12	13	13	13	13	13
Other services	B2	50	47	69	31	22	24	23	23
Debt Management Office	B2	1	4	5	7	6	7	13	14
Coinage	B2	14	38	40	35	36	36	37	39
Office of Government Commerce	B2	-49	-33	-12	45	47	39	40	40
<i>of which</i>									
OGC admin costs	B5	13	12	18	30	37	39	41	42
OGC other (mostly civil estate)		-62	-45	-30	15	10	0	-1	-2
Total budget	B2	88	192	161	248	410	309	322	331

Central Treasury Resource Budget

18. The starting point in this table is the core Treasury's administration costs, the changes in which have been described in paragraphs 7 to 13 of this note. Beyond this, the main factors affecting the **central Treasury resource budget** over recent years have been:

- costs arising from the Treasury's status as sole shareholder in the Bank of England and credits resulting from the Bank's annual payments to the Treasury in lieu of a dividend;
- a one-off charge arising from the balance sheet treatment of the new building.

19. In line with accounting rules on investments (set out in section 3.10 of the RAM), the Bank of England is treated as an investment in the Treasury's

accounts. A cost of capital charge on the Treasury's sole shareholding in the **Bank of England** is charged to the Treasury's accounts at the rate of 7 per cent. The latest valuation of the Bank is some £1.5 billion, resulting in a capital charge of around £100 million. Table B4 on page 83 of the departmental report illustrates that investments – i.e. the Treasury's shareholding in the Bank of England – is by far the most significant item of the balance sheet of the departmental group. In addition, the Bank is required to pay the Treasury, in lieu of dividend, a sum agreed between the Bank and the Treasury in respect of each financial year, normally 50 per cent of its net operating surplus. This is credited to the central Treasury budget as a receipt but is then surrendered by the Treasury. These items taken together can have a very profound effect on the Treasury's resource budget, rising from a net credit of £15 million in 2000-01 to a cost of some £48 million the following year. The reasons for this volatility are the magnitude of the investment, which mean that any shift in the valuation of the Bank can have a significant impact on the charge, and the fact that the dividend depends on the Bank's financial statements, which, as with any organisation, will vary from year to year.

20. The £69 million charge in 2002-03 reflects the **revaluation of the new Horse Guards Building**, in line with more transparent disclosure under best practice accounting standards (in particular, Financial Reporting Standard 11). Broadly speaking, this charge reflects the market value of the office space, as independently valued in line with accounting standards, as against the full capital costs incurred by the private sector partner in refurbishing and upgrading an historic Grade II listed building for the purposes of modern office accommodation. This charge was reflected in a supplementary Estimate presented to Parliament earlier this year and is shown in Table 2 as an exceptional charge relating to 1 Horse Guards. A full explanation of this charge is given in section 14.2 of the Treasury's audited accounts (pages 38 and 39).

Total Resource Budget

21. The profile of the **total resource budget** (for the departmental group) between 1998-99 and 2002-03 also reflects developments outside the core

Treasury, in particular those arising from the creation and development of the Office of Government Commerce.

22. Established in 2000, the **Office of Government Commerce (OGC)** is responsible for a wide-ranging programme that focuses on improving the efficiency and effectiveness of central civil Government procurement. The OGC inherited functions carried out by the Property Advisers to the Civil Estate (PACE) and the Central Computer and Telecommunications Agency (CCTA). Its Spending Review 2002 target of making £3 billion of value for money gains in Government procurement replaces its Spending Review 2000 target of £1 billion. As reported in the Departmental report, the OGC has already reported gains of £815 million in the first two years of its Spending Review 2000 target.
23. OGC administration costs increased by £24 million between 1998-99 and 2002-03 reflecting its growing role, following the initial start-up phase and a planned reduction in administrative income. Increasingly, OGC's income-earning activities are transferring to its trading fund, OGC buying solutions, with OGC concentrating on supporting high risk, high value projects in line with its agreed medium term strategy.
24. In addition to its administration costs, there are programme costs included in the resource budget for the OGC, which relate to the disposal of the residual civil estate and the management of the Whitehall District Heating and Distribution Systems. The disposal of the civil estate – down from 384 properties in 1996 to 33 in March 2003 – has provided both resources and cash benefits in the last few years of the last decade and the first two years of this one. This led to the significant credits to the resource budget (as well as to the capital budget, which is explained in the next section). The credit to the resource budget occurs because the OGC's balance sheet contained liabilities for costs of surplus properties on the estate. As the estate was disposed of, surplus liabilities were released, which count as a credit to the resource budget. As the residual estate decreases in size, the value of these releases becomes smaller.
25. In addition to the OGC, the total resource budget includes costs associated with the **Debt Management Office (DMO)**, which has been a considerable success in terms of generating financial gains for the Government overall, has led to an increase in costs over the period covered by the table, from £4

million in 1999-2000 to £7 million in 2003-04, rising to £14 million in 2005-06. These reflect expenditure required to review (and possibly replace) the DMO's dealing and management information systems, to re-engineer business processes following the merger with the National Investment and Loans Office, to further develop the DMO's risk management capabilities, and further involvement in wider activities surrounding the management of the Government's balance sheet.

26. Other costs include a variety of spending not directly relating to the business of a finance and economics ministry. Examples which are charge to the total spending numbers for the Treasury include:

- the supply of UK coinage;
- the Civil List;
- the salaries and pensions of UK members of the European Parliament;
- grants-in-aid to certain Parliamentary bodies such as the Commonwealth Parliamentary Association; and
- the costs of issuing UK honours.

The Treasury's capital budget

27. In a similar manner to table B2, table B3 of the departmental report provides a further breakdown of the department's capital budget.

Table 3: The Treasury group's capital budget: an analysis

£ million	1998-99 Outturn	1999-00 Outturn	2000-01 Outturn	2001-02 Outturn	2002-03 Estimated Outturn	2003-04 Plan	2004- 05 Plan	2005-06 Plan
Core Treasury	3	4	23	7	145	1	3	3
<i>of which</i>								
<i>Routine</i>	3	4	3	7	4	1	3	3
<i>Exceptional</i>			20		141			
DMO	1	2	1	2	1	2	2	1
OGC	-47	-29	3	-41	3	4	3	2
Total capital budget	-44	-23	26	-32	149	8	9	7

28. The capital spend of central Treasury is normally between £3 million and £7 million. For the Debt Management Office, spending is normally £1 million to £2 million per year. There have been two notable exceptions over the period:

- in 2000-01 the Treasury floated Partnerships UK as a public private partnership. Capital expenditure of £20 million was incurred in the form of investment in 45 per cent of PUK shares. Receipts from sale of the shares – some £45 million – were remitted directly to the Consolidated Fund, and did not score against Treasury's resource budget.
- In 2002-03, 1 Horse Guards was brought onto the Treasury's balance sheet in line with professional advice about the balance of risk. More detail on this issue is in note 14.2 to the Treasury's accounts, which are available on the Treasury's website and are attached to this note. This did not involve additional cash outlays from the Treasury. But to represent the creation of the building as an asset in the Treasury's balance sheet, the Treasury's capital spending included a non-cash element of £141 million, matching the value of the asset.

29. The OGC's negative capital spend in the early years of the period is a result of the sale of the freeholds within the residual estate. The -£41 million in 2001-02 is largely made up of the sale of 1 Marsham Street. Most proceeds are surrendered automatically to the Consolidated Fund and are not spent either by the OGC or by any other part of the Treasury departmental group.

There are now no more large freeholds left. For the forward years, the capital spend is designed to underpin the modernisation of the OGC (as outlined in the OGC's Departmental Investment Strategy – see the OGC's website for details).

Explanatory notes – Annex B Tables

30. The terms used in the data annex of the departmental report require additional explanation for a full understanding of the data.

31. It is important to note the key budgetary concepts of Departmental Expenditure Limits (DEL) and Annually Managed Expenditure (AME):

- **Departmental Expenditure Limits (DEL):** this is the budgetary aggregate for spending on programmes by Departments. Expenditure within DEL is subject to firm and fixed three-year limits set during the Spending Review process. It can be viewed as discretionary or controlled spending – that is to say it is within the control of departments;
- **Annually Managed Expenditure (AME):** this is the forecast for non-discretionary spending. AME spending is that which can not reasonably be subject to firm multi-year limits. It is re-forecast every six months in the Pre-Budget Report and the Budget. The main components of AME are demand-led or non-discretionary expenditure such as state pension payments, unemployment benefits and debt interests. However, many departments will have AME charges.

32. Critically, whether or not expenditure is classified as DEL or AME, or whether it is cash or non-cash, it must normally be voted by Parliament. As the departmental report must account for all the resources voted by Parliament, the guidance on departmental reports issued by HM Treasury requires departments to use as the total public spending measure a number that includes DEL and AME expenditure. Consistent with both the independently set accounting framework, and the Government's fiscal framework, this means that the data are reported in the format set out in Annex B, which is explained in more detail below.

Table B1 total public spending (page 80)

33. Table B1 is designed to show the full resources consumed and capital spending by the department. Crucially, “the Department” in this context means the range of entities incorporated in the Treasury’s accounts:

- The **consumption of resources** means the full economic costs associated with the delivery of public service, measured on an accruals basis, and including depreciation and a cost of capital charge.
- broadly speaking **capital spending** covers the net acquisition of assets by the department (or gross expenditure on assets less the proceeds from the sale of fixed assets) plus new loans or investments undertaken by the department.
- **total public spending** is the sum of resource consumption and capital spending less depreciation and impairments. Depreciation is excluded to avoid double counting capital investment – once when a new investment is made (i.e., in capital spending) and again as it is consumed/depreciated over its useful life (i.e., in resource consumption). Total public spending represents the best measure of total annual spending under resource budgeting by capturing the costs of delivering services as well as net investment.

Table B2 Resource Budget (page 81)

34. This table provides a further breakdown of the department’s resource budget by expenditure area. The resource budget broadly aligns with the department’s operating cost statement and, for control purposes, is divided into the Resource Departmental Expenditure Limit (DEL) and Resource Departmental Annually Managed Expenditure (AME), as set out above in paragraph 31.

Table B3 Capital Budget (page 82)

35. In a similar manner to table B2, this table provides a further breakdown of the department's capital budget. The capital budget generally reflects additions to the department's balance sheet and is divided into DEL and AME by applying the same principles set out in the previous paragraph.

Table B4 Capital Employed (page 83)

36. This table summarises the capital employed by the department in the delivery of its outputs and is based on audited departmental accounts for outturn data and internal financial data (where audited accounts are not available).

Table B5 Administration Costs (page 84)

37. Administration costs are the part of the resource budget that capture the resources consumed by the department that are not directly related to the delivery of services to the public. More specifically, administration costs include: employee costs (notably pay and pensions), operating expenditure on accommodation (such as rent and maintenance), office services (including postage and telecommunications), comparable contracted-out services and non-cash costs (mainly depreciation and cost of capital charges) on the assets used to manage spending not directly related to the delivery of frontline services.

Table B6 Staffing numbers (page 85)

38. This table illustrates staff numbers in line with Cabinet Office classifications to allow comparisons between departments on a consistent basis.

HM TREASURY

15 September 2003