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The Committee of Public Accounts

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Summary

The Government's high level of debt leaves little room for manoeuvre in public spending. The as yet unknown costs of Brexit place a further limit on the Government's ability to react to further economic shocks. As the Government looks to reduce borrowing and debt to meet its fiscal targets, decisions affecting the public finances will need to be sufficiently visible to Parliament and the public. The UK Debt Management Office's and National Savings & Investments' ability to respond to any financial crises and possible need to increase borrowing levels significantly may be more difficult in the future; because of the increasing exposure to rising inflation and the eventual unwinding of the Bank of England's quantitative easing programme.

The Whole of Government Accounts (WGA) provides us with a clearer picture of all public sector finances than ever before. It is particularly useful in highlighting future liabilities such as pension costs. We are encouraged by the improvements that the Treasury has made to the WGA, but its value remains limited by the delays to publication and the lack of information in key areas. We welcome the steps that the Treasury is taking to strengthen the understanding and management of the Government balance sheet but, to have a lasting effect, the Treasury will need to embed best practice in routine decision-making across government to ensure we are both harnessing the assets and managing down the risks from our increasing liabilities in the longer-term.

There is still work to be done to ensure that the WGA is a useful and useable document for Parliament and ultimately the individual citizen and taxpayer.

Introduction

Government's annual spending has exceeded its income for the last 15 years. To fund the deficit, government borrows by issuing government bonds, known as gilts, through the UK Debt Management Office (DMO) to large investors in the capital markets, or by encouraging savers to invest in National Savings & Investment (NS&I) retail products such as Premium Bonds. The Government has a significant amount of debt outstanding from financing past annual deficits and it has targets to reduce levels of borrowing and debt by 2020–21. Public sector net debt (PSND), government's preferred measure for reporting on the public finances, was around £1.7 trillion at March 2017. By comparison, the latest Whole of Government Accounts (WGA), which provides a financial reporting view of the public finances, reports that total debt from borrowing was £1.3 trillion at March 2016: around £47,000 for each UK household. Interest on debt cost government £222 billion in the period 2009–10 to 2015–16. As government's economic and finance ministry, HM Treasury has overall responsibility for government's financial strategy and fiscal policy. The Treasury published WGA 2015–16 in July 2017, 16 months after the financial year end.

Conclusions and recommendations

1. **UK government debt remains too high relative to economic performance, potentially reducing government's capacity to respond to future shocks and uncertainty.** At £1.7 trillion and 86% of gross domestic product at March 2017, the Government recognises that public sector debt is too high. We are also concerned about the rising level of personal debt which could have a significant impact on the economy and public finances in the longer term. In November 2017, the Office for Budget Responsibility (OBR) revised down its forecasts for UK productivity and economic growth, estimating that the Government has £14 billion headroom to meet its borrowing target in 2020–21. The Government recognises that productivity growth over the last few years has been disappointing. It has now increased the amount it expects to borrow by £55 billion between 2018–19 and 2021–22 but this estimate will be affected by economic performance, the terms agreed for exiting the EU and significant changes to government's balance sheet. The DMO has proven it can raise funds quickly and cost-effectively, with its annual remit (the amount Treasury tells them to borrow) increasing from £80 billion in 2008–09 to £220 billion in 2009–10. However, it may be more challenging for the DMO to meet government's borrowing needs in the future given the already high level of debt, the uncertainty in the public finances arising from the UK's exit from the EU, and the eventual unwinding of the quantitative easing programme. Index-linked gilts now make up 34% of the gilt portfolio, increasing the exposure to inflation risk, which could raise the cost of borrowing considerably. In July 2017, the OBR published its first Fiscal risks report which provides an independent view of risks to the public finances, and the Government has committed to responding formally to the first report in summer 2018.

   Recommendation: ***In its formal response to the OBR's report, the Treasury should ensure it sets out its assessment of the key risks to the public finances, and explain how it will measure and report on the impact its investment is having on the economy.***

2. **NS&I faces an inherent tension in balancing the differing interests of the taxpayer, savers, and the wider retail savings market at the same time as delivering specific policy objectives for the Government.** NS&I must offer a fair return for savers in order to be able to successfully raise funds to meet government's borrowing needs. But it must also minimise finance costs to taxpayers, and maintain market competition and stability. For example, after 2008–09 NS&I had to reduce returns offered to savers, thus reducing demand, following the 'flight to safety' response to the financial crisis when investors sought the security of its government-backed investments. Around 9% of the £1.7 trillion UK retail savings market is held with NS&I currently. In 2016–17, NS&I's measure of cost-effectiveness showed that borrowing through the NS&I had saved £74 million compared to borrowing through gilts, although this has fallen from £1.4 billion saved in 2009–10, largely due to government bond rates falling faster than the interest rates on NS&I products. For some products, NS&I faces the challenge of balancing wider policy objectives with the need to provide cost-effective borrowing. For example, its 65+ Guaranteed Growth Bond, introduced by the Government in 2015 to reward a specific group of savers, offered market beating rates, and we are told became the "biggest selling

retail financial product in Britain's modern history". The estimated costs of such products are set out alongside the relevant Budget when they are launched, but the costs are excluded from NS&I's measure of cost-effectiveness.

Recommendation: ***The Treasury and NS&I must find a way to communicate to Parliament and the public how future products with specific policy objectives strike an appropriate balance between meeting government's wider policy aims and delivering value for money.***

3. **It is not yet clear how the move to one annual fiscal event in the autumn will work in practice to enable greater Parliamentary scrutiny.** In Autumn Statement 2016, the Chancellor abolished future autumn statements and spring budgets in favour of just one Autumn Budget each year. This change was in response to the International Monetary Fund's recommendations to enhance the UK's fiscal transparency and aims to allow greater external and Parliamentary scrutiny of new tax and spending measures before they are introduced in the next financial year. The OBR is legally required to publish two forecasts each year and until now has published these forecasts alongside the Spring Budget and Autumn Statement. The Government will respond to the OBR's March forecast in a Spring Statement in 2018. Although the Treasury assures us that Parliament will still have the information it has available today, it is considering how it will respond to the OBR's spring forecasts and communicate changes to the budget in subsequent years.

Recommendation: ***By March 2018, the Treasury should set out how and when it will provide Parliament with the opportunity to scrutinise and debate decisions affecting the public finances.***

4. **The Treasury has made progress in improving the WGA but the time it takes to produce, and the limited information included in some areas, continue to restrict its use as a tool for decision-making and accountability.** In the 2015–16 WGA, the Treasury has provided more insightful narrative information on government finances and on significant movements in major assets and liabilities than it did previously. The Treasury recognises that there is still more to do to develop the narrative in the WGA to meet the recommendations of the previous Committee, in particular on pension liabilities and regional spending. The Treasury published the 2015–16 accounts 16 months after the financial year-end, despite its goal to publish within a year. To produce the WGA more quickly, the Treasury will need to address bottlenecks in the consolidation process. While the Treasury is increasingly using the WGA to analyse trends and long-term risks to the public finances, it must rely on other, more timely information to make decisions in the short term. For example, alongside public sector net debt (PSND) and its fiscal targets, the Treasury has begun using a further statistical measure, public sector net financial liabilities, to assess the impact of decisions on government's balance sheet. It is important that these measures are used consistently. As we prepare to leave the EU, disclosures in the WGA which show the impact and related risks will be particularly important for transparency.

Recommendation: ***By March 2018, the Treasury needs to set out its plans and timetable for producing the WGA more quickly after the year end, and for improving the disclosures, as recommended by the previous Committee.***

5. **Unless actions to maximise the value from assets and reduce liabilities are embedded in routine financial management across departments, any gains from the Treasury's balance sheet review are likely to be short term.** In response to recommendations from the previous Committee as well as the International Monetary Fund and the NAO, the Treasury has been building its understanding and analysis of government's balance sheet and working with the OBR to improve its oversight and analysis of fiscal risk. However, this work is at an early stage and will need to be embedded in routine decision-making and its existing oversight arrangements with departments. The Treasury has now announced plans to carry out a review of government's balance sheet to ensure it is getting the best return from its assets while monitoring and reducing the cost of liabilities. The Treasury expects the review will help to release resources for future investment in public services and improve the sustainability of the public finances. As part of the review, the Treasury will look for further income-generating opportunities and we are keen that it harnesses the value from intangible assets, such as intellectual property, in particular. The Treasury expects to report on its review at Budget 2018.

Recommendation: ***The Treasury needs to ensure that its review has a long-term impact on the cost-effective management of government assets and liabilities. It should report to us on its progress by June 2018.***

1 Borrowing and the public finances

1. On the basis of a report by the Comptroller and Auditor General and the Whole of Government Accounts for the year ended 31 March 2016, we took evidence from HM Treasury (the Treasury), the UK Debt Management Office (DMO) and National Savings and Investments (NS&I) on government borrowing and debt.[1]

2. Government borrows by issuing government bonds, known as gilts, through the UK Debt Management Office (DMO) to large investors in the capital markets, or by encouraging savers to invest in National Savings & Investment (NS&I) retail products such as Premium Bonds. As government's economic and finance ministry, the Treasury has overall responsibility for government's financial strategy and fiscal policy. Drawing on the independent forecasts produced by the Office for Budget Responsibility (OBR), the Treasury decides each year on the total amount of borrowing it needs and how much the DMO and NS&I need to raise.[2]

Levels of borrowing and fiscal risks

3. Government's annual spending has exceeded its income for the last 15 years and, because of this, the Government has a significant amount of debt outstanding from financing past annual deficits. Public sector net debt (PSND), government's preferred statistical measure for reporting on the public finances, was around £1.7 trillion at March 2017.[3] By comparison, the latest Whole of Government Accounts (WGA) provides a financial reporting view of the public finances, which takes into account a broader range of assets and liabilities. The latest WGA reports that total debt from borrowing was £1.3 trillion at March 2016: around £47,000 for each UK household. Interest on debt cost government £222 billion in the period 2009–10 to 2015–16.[4] Government recognises that public sector debt is too high relative to the UK's economic performance, and it has targets to reduce levels of borrowing and debt by 2020–21.[5] Figure 1 shows that PSND as a share of gross domestic product (GDP) has risen from around 65% in 2009–10, immediately after the banking crisis, to 86% in 2016–17. In November 2017, the OBR published a forecast that showed it expected PSND as a share of GDP to peak in 2017–18, however it also revised down its forecasts for UK productivity and economic growth.[6]

4. Private debt as a share of GDP has remained persistently high since the banking crisis, and stood at around 230% at the end of 2016.[7] We are particularly concerned about the impact that rising levels of household debt could have on both individuals and the public finances, especially interest-only mortgages.[8] Recent media reports suggest that around a fifth of outstanding residential mortgages in the UK are interest-only, and the Council of Mortgage Lenders estimates around 1.9 million borrowers are simply paying off the

1 Report by the Comptroller and Auditor General, Evaluating the government balance sheet: borrowing, Session 2017–19, HC 526, 7 November 2017; HM Treasury, Whole of Government Accounts: year ended 31 March 2016, HC 254, July 2017
2 C&AG's Report, para 2–3
3 Office for National Statistics, Public sector finances, UK: March 2017, April 2017
4 C&AG's Report, para 5–6
5 Q 4
6 Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 9530, November 2017
7 C&AG's Report, Figure 6
8 Qq 101–104

interest on their debts.[9] Risks arising from consumer debt are identified and monitored by the Bank of England's Financial Policy Committee (FPC), which is responsible for protecting and enhancing the resilience of the UK financial system. The FPC's most recent Financial stability report, which sets out the FPC's view on the stability of the UK financial system, concluded that "the level of household indebtedness in the United Kingdom has fallen but remains high relative to incomes". However, the FPC noted that highly indebted households may still pose risks to UK financial stability, either by amplifying economic downturns (as spending is cut back to meet mortgage payments) or through failing to meet debt repayments which leads to losses for lenders.[10] In written evidence provided to us after the session, the Treasury stated that mortgage arrears and repossession are at "historically low levels" and that the Financial Conduct Authority, which regulates financial services firms, continues to monitor lenders' treatment of borrowers with interest only mortgages.[11]

Figure 1

Growth in government borrowing since 2009–10 using a range of measures

Debt measure	2009–10	2010–11	2011–12	2012–13	2013–14	2014–15	2015–16	2016–17
Public sector net debt (PSND)	1,007	1,152	1,247	1,358	1,460	1,548	1,602	1,727
PSND as a % of gross domestic product (GDP)	64.6	71.4	75.1	78.6	80.5	82.9	82.6	85.6
Whole of Government Accounts borrowing and financing	782	908	966	996	1,096	1,175	1,261	Not available
Public sector net financial liabilities (PSNFL)	857	975	1,108	1,235	1,321	1,398	1,462	Not available

Source: Office for National Statistics, Public Sector Finances; HM Treasury, Whole of Government Accounts

5. The Government recognises that productivity growth over the last few years has been disappointing.[12] In Budget 2017, the Government announced its plans to "expand the National Productivity Investment Fund (NPIF) to support innovation, upgrade the UK's infrastructure and underpin the Government's modern Industrial Strategy". However, the OBR currently forecasts future growth will be slower than previously forecast, and now estimates that the Government has £14 billion headroom to meet its borrowing target in 2020–21. The Government has increased the amount it expects to borrow by £55 billion between 2018–19 and 2021–22 but this estimate may be further affected by economic

9 Financial Times, Ticking time bomb of interest-only mortgages, 21 July 2017
10 Bank of England, Financial Stability Report, Issue number 42, November 2017
11 Correspondence with Treasury, 7 December
12 Q 103

performance, the terms agreed for exiting the EU and significant changes to government's balance sheet. For example, if planned assets sales are delayed or generate less income than expected, more borrowing will be needed.[13]

6. In addition to its regular forecasts, in July 2017 the OBR also published its first Fiscal risks report which provides an independent view of risks to the public finances. The OBR prepared this report in response to a recent recommendation from the International Monetary Fund that government should "publish a comprehensive fiscal risk report combining the analysis of macroeconomic risks, the modelling of the fiscal impact of severe shocks, and a discussion of the magnitude and likelihood of specific fiscal risks."[14] In its report, the OBR highlighted the biggest potential risks that would affect the whole economy, including: shocks like recessions and financial crises; sustained productivity weakness; and risks that would affect large parts of public spending (such as shocks affecting debt interest).[15] We asked the Treasury how it monitored these and other fiscal risks, and in particular risks arising from government's exposure to specific sectors of the economy. The Treasury told us it had two standing groups, a Fiscal Risk Group and a Balance Sheet Group, that bring together information from across government to get a sense of fiscal risks that might be emerging. When asked to provide a specific example of a significant fiscal risk it was paying close attention to, the Treasury highlighted a number of risks relating to the tax base, for example, the trend for people to incorporate and work as self-employed rather than employees. Government has committed to responding formally to the OBR's first report in summer 2018.[16]

7. We also asked the Treasury and the DMO how confident they were in their ability to adapt and respond to unexpected or uncertain changes in borrowing needs. The Treasury noted that the DMO has proven it can raise funds quickly, citing the dramatic increase in the DMO's expected borrowing requirement at the onset of the banking crisis in 2008. In this case, the DMO's annual remit (the amount Treasury tells them to borrow) increased from £80 billion in 2008–09 to £220 billion in 2009–10. The Treasury noted that it may be more challenging for the DMO to meet government's borrowing needs in the future given the already high level of debt, and that government would be better placed to respond to future recessions and shocks once the debt is lower. However, it views the institutional arrangements in place as very strong, and observed that the DMO is highly respected and trusted in the market. Similarly, the DMO was confident in the arrangements in place, and suggested that the market response to the large increase in the DMO's remit in 2009 showed that such increases were both operationally possible and that there was flexibility in the market.[17] However, future risks and uncertainties remain, such as the uncertainty in the public finances arising from the UK's exit from the EU, and the eventual unwinding of the quantitative easing programme.[18] In addition, the proportion of index-linked gilts in the gilt portfolio (where interest payments are adjusted in line with the UK Retail Prices Index) has increased from 24% in March 2009 to 34% in March 2017 (excluding gilts held by the Bank of England), increasing government's exposure to inflation risk and

13 HM Treasury, Autumn Budget 2017, HC 587, November 2017; Office for Budget Responsibility, Economic and fiscal outlook, Cm 9530, November 2017
14 International Monetary Fund, United Kingdom: Fiscal Transparency Evaluation, November 2016
15 Office for Budget Responsibility, Fiscal risks report, July 2017
16 Qq 25, 27–32
17 Qq 10, 33–36, 71
18 C&AG's Report, para 24

potentially higher interest costs on its future borrowing.[19] The OBR attempts to anticipate the impact of such events through its forecast assumptions; however, the reliability of these assumptions will only be tested over time.[20]

Cost-effective borrowing through NS&I

8. To deliver its remit, NS&I must balance the interests of savers by offering a fair return and the interests of the taxpayer by minimising finance costs. At the same time, it must also maintain an appropriate competitive position in the retail savings market. Currently, NS&I holds around a 9% share of the £1.7 trillion UK retail savings market, with a debt portfolio at March 2017 of £148 billion.[21] We asked NS&I how challenging it was to meet its annual remit (the amount Treasury tells them to borrow) without distorting the market. NS&I told us it managed this challenge by being clear with the market how much it is planning to raise overall, by monitoring its market position and considering its potential impact on competitors. NS&I explained it would only take action to change its market position following careful evaluation, and in order to balance the interests of the market, savers and the taxpayer.[22] For example, after 2008–09 NS&I experienced a considerable inflow of funds following the flight to safety response to the financial crisis when investors sought the security of its government-backed investments. NS&I took action to reduce the inflow by reducing the returns offered to savers, reducing the demand for NS&I products and responding to concerns about the health of the market.[23] Similarly, in February 2017 NS&I reduced the interest rates on four of its variable rate products, in order to balance the need to meet its 'annual remit' with the interests of stakeholders.[24]

9. We asked NS&I how cost-effective it was compared to other means of borrowing. NS&I said it saw itself as very cost-effective and highlighted that its indicator of cost-effectiveness, the Value Indicator, implies that NS&I borrowing is competitive relative to gilt borrowing. However, this indicator has fallen from £1.4 billion in 2009–10 to £74 million in 2016–17, largely due to government bond rates falling faster than the rates NS&I can offer on its products. NS&I noted that its ability to provide cost-effective borrowing is constrained to some degree by needing to balance the interests of multiple stakeholders. For some products, NS&I faces the further challenge of balancing wider policy objectives with the need to provide cost-effective borrowing. For example, we are told that its 65+ Guaranteed Growth Bond, introduced by the Government in 2015 to reward a specific group of savers, offered market beating rates, became the "biggest selling retail financial product in Britain's modern history". As these policy products often offer rates of return above market rates, they are generally excluded from NS&I's indicator of cost-effectiveness.[25] The estimated costs of such products are set out alongside the relevant Budget when they are launched; for example Budget 2014 and Budget 2015 set out costs relating to the 65+ Guaranteed Growth Bonds of £295 million.[26]

19 C&AG's Report, para 18
20 Qq 12–13
21 C&AG's Report, para 4.2, 4.15
22 Qq 91–93
23 Q 94
24 C&AG's Report, para 4.17
25 Qq 85–87; C&AG's Report, para 4.6, 4.13
26 HM Treasury, Budget 2014, HC 1104, March 2014; HM Treasury, Budget 2015, HC 1093, March 2015

Announcing future changes to the public finances

10. In Autumn Statement 2016, the Chancellor abolished future autumn statements and spring budgets in favour of just one Autumn Budget each year. The Chancellor announced that this change would "allow for greater Parliamentary scrutiny of Budget measures ahead of their implementation."[27] This change was in response to the International Monetary Fund's recommendations to enhance the UK's fiscal transparency and allow for greater external and Parliamentary scrutiny of new tax and spending measures before they are introduced in the next financial year.[28]

11. The OBR is legally required to publish two forecasts each year and until now has published these forecasts alongside the Spring Budget and Autumn Statement. The Government will respond to the OBR's March forecast in a Spring Statement in 2018. We asked what effect the move from two fiscal events to one would have on the Treasury's presentation of key financial information, in terms of Parliament's accountability and transparency. The Treasury assured us that, following the change, Parliament will still have the information it has available today. For example, the estimates process, by which Parliament authorises government's spending plans, would continue as before and the timing of OBR publications would be unaffected. The Treasury indicated that the change may lead to a higher degree of consultation on future Budget measures than has been possible in the past. However, it is still considering how exactly it will respond to the OBR's spring forecasts and communicate changes to the budget in 2018 and beyond.[29]

27 Oral statement to Parliament by the Chancellor of the Exchequer, 23 November 2016
28 International Monetary Fund, United Kingdom: Fiscal Transparency Evaluation, November 2016
29 Qq 14, 24

2 Analysing and managing the Government Balance Sheet

12. The Whole of Government Accounts (WGA) brings together the financial activities of more than 6,000 organisations across the public sector, including central and local government as well as public corporations such as the Bank of England. There is no more complete record of what the Government owns, owes, spends and receives. HM Treasury (the Treasury) published the 2015–16 WGA in July 2017. It is the seventh WGA to be published.

13. In its 2016 evidence session on the Government balance sheet and 2014–15 WGA, the previous Committee asked the Treasury to make the WGA clearer and more useful to the reader by providing a better understanding of the regional distribution of public money and what is causing significant movements on the balance sheet. The previous Committee also recommended that the Treasury needs an enforceable plan to produce WGA more quickly after the year-end.[30]

Progress in improving the WGA

14. In response to recommendations by the previous Committee and the National Audit Office (NAO), the Treasury said it had made an effort to focus on the key risks, issues and movements in the accounts–particularly the pension obligations–in the performance report at the front of WGA 2015–16.[31] In the latest WGA, the Treasury has provided comparative information showing how major income, assets, liabilities and financial risks have changed and explained the main movements in assets and liabilities, particularly the major impact of the discount rates used to value assets and liabilities in today's prices. For example, the Treasury sets out in the WGA that £125 billion (96%) of the increase in provisions (liabilities which government will probably need to pay in the future but where the timing or amount is uncertain) was due to a change in the discount rate. The Treasury recognised there was more to do and committed to continuing to improve the report and build in more information that is available elsewhere. For example, the WGA still lacks detail on the distribution of spending by region or by government activity. The Treasury explained that it would be a large undertaking to get this level of information on a financial reporting basis from each organisation which feeds into the WGA.[32] Instead, it committed to include in the WGA information from the Treasury's annual publication on the Public Expenditure Statistical Analyses (PESA) which provides a breakdown of annual expenditure by objective based on National Accounts definitions.[33]

15. The Treasury explained that it has a target to publish the WGA within one year of the financial year-end, but it hopes to bring this deadline forward to nine months in the future. It said that the 2015–16 WGA was published 16 months after the year-end mainly because of the impact of the general election. The Treasury told us that the key areas affecting the timeliness of publication were the later deadline for local authorities to publish their

30 Committee of Public Accounts, The Government Balance Sheet, Nineteenth Report of Session 2016–17, HC 485, October 2016, conclusion 1

31 Q54–55

32 Q 79; HM Treasury, Whole of Government Accounts: year ended 31 March 2016, HC 254, July 2017, note 22, para 6.4–6.5

33 Qq 79–80; HM Treasury, Public Expenditure Statistical Analyses 2017, Cm 9467, July 2017

annual accounts and the time taken to produce the sector report for Academy schools. Currently, local government bodies have a deadline to publish their accounts by end of September compared to July for central government, although this is coming forward to July in 2017–18 which the Treasury said should enable them to bring forward the WGA timetable.[34] The Department for Education produced the first consolidated accounts for the Academy Schools Sector in England 2015–16 in October 2017, 14 months after the academic year they are reporting on.[35] The Treasury said that now the sector report was established, it hoped to work with the Department to get the information into the WGA on a more timely basis and make staged improvements to bring forward publication, potentially publishing the 2018–19 accounts by the end of December 2019, although it recognised this would be a "stretch target".[36]

16. The Treasury told us that whereas it uses the National Accounts, which provides a statistical, monthly view of the public finances, for in-year budgeting, it uses the WGA to provide a view of fiscal risks. In WGA 2015–16, the Treasury has improved on the reconciliation between the national accounts and WGA.[37] In 2016, the Treasury began using a further statistical measure, public sector net financial liabilities (PSNFL), which is a more comprehensive measure than PSND. PSNFL includes all financial assets and liabilities in the National Accounts which is helpful when considering the broader impact on the public finances of selling assets. For example, selling government-owned shares would reduce PSND regardless of the profit or loss made on the sale, whereas PSNFL would reflect the loss of the value of the asset sold as well as the income gained. Responding to our concerns that different measures could be misleading if used inconsistently, the Treasury acknowledged the challenge of explaining these complex figures to the Government, Parliament and the public.[38]

17. We challenged the Treasury over how the WGA could inform decision-making given it is reporting out-of-date numbers long after the year-end. In response, the Treasury highlighted the broad and unique view of the public finances that it feels the WGA provides which it said had been valuable in identifying risks, such as foreign exchange liabilities, that may not have been picked up elsewhere. The Treasury also gave examples such as clinical negligence where the exact number of the liability being considered was less important than the trend over time when determining the response needed.[39] It said there had been a greater focus within the Treasury and in Departments, as a result of WGA, on risks attached to significant items on the balance sheet such as liabilities arising from clinical negligence and nuclear decommissioning.[40] We asked whether the WGA will set out clearly how much it costs to leave the EU, particularly in terms of the money given to those departments most affected by the need to prepare to exit. The Treasury told us that a significant impact would not be seen in the 2016–17 WGA but that future funding allocated would be voted by Parliament in the usual way. In some cases the relevant department may need to spend money to prepare to take on another function in March 2019 but will not have legal or parliamentary authority to do so until the European Union (Withdrawal) Bill is passed. In this event, the Treasury explained that it has asked

34 Qq 74–75
35 Department for Education, Academy Schools Sector in England: consolidated annual report and accounts for the year ended 31 August 2016, HC 425, October 2017
36 Qq 75–77
37 Qq 54–61; HM Treasury, Whole of Government Accounts: year ended 31 March 2016, HC 254, July 2017
38 Qq 60–63
39 Qq 48, 70
40 Qq 61, 70

Accounting Officers to seek a ministerial direction: a formal instruction from a minister to an Accounting Officer to proceed, where the Accounting Officer has expressed concerns that the spending involved does not meet the tests of regularity, propriety, value for money or feasibility.[41]

The Treasury's approach to balance sheet management

18. The previous Committee recommended in 2016 that the Treasury do more to analyse its balance sheet and develop contingency plans while also getting a grip on specific liabilities, such as clinical negligence.[42] Similarly, the International Monetary Fund's evaluation of the UK's fiscal transparency recommended the Treasury increase controls over off-balance sheet commitments such as guarantees and publish a report setting out risks to the balance sheet.[43] In response, the Treasury has created balance sheet and fiscal risks analysis teams to develop its fiscal risk modelling and stress testing of the public finances, and bring together analysis carried out by teams across the Treasury. This work is at an early stage. Both teams support the newly-established Balance Sheet Group, Fiscal Risk Group and executive management board's view of risk.[44] The fiscal risks branch will be responsible for responding to the OBR's report on fiscal risks in summer 2018. The Treasury has also strengthened its budgetary and approvals process around any newly-created contingent liabilities which might exceed £3 million and which are either novel, contentious or could impact other parts of the public sector.[45] Around 24 new contingent liabilities had gone through the revised process as at November 2017.[46]

19. We asked how the Treasury was going to make sure its balance sheet analysis informs decisions made so that we harness the value from our assets and manage down our liabilities. The Treasury told us that its Balance Sheet Group and Fiscal Risk Group already brings together directors from across the Treasury, so everybody has the same information and the groups are fully integrated into the work of the department. In addition, the Treasury explained that it had announced a balance sheet review in Autumn Budget 2017 which, drawing on the information in WGA, aims to make more effective use of assets, improve the return of investments and reduce the cost of liabilities. The Treasury will report on progress at Budget 2018. The Treasury told us it hopes to find considerable savings from this review which can be invested in public services.[47] We stressed the importance of getting value from intangible assets such as software and intellectual property, and the Treasury confirmed that intangible assets would be part of the review.[48]

41 Qq 114–118
42 Committee of Public Accounts, The Government Balance Sheet, Nineteenth Report of Session 2016–17, HC 485, October 2016, conclusions 4 and 5
43 International Monetary Fund, United Kingdom: Fiscal Transparency Evaluation, November 2016
44 Q 66; C&AG Report, para 16
45 HM Treasury, Contingent liability approval framework: guidance, July 2017
46 C&AG Report, para 16
47 Qq 60, 64–66; HM Treasury, Autumn Budget 2017, HC 587, November 2017
48 Q 64

Formal minutes

Monday 22 January 2018

Members present:

Bim Afolami
Heidi Allen
Sir Geoffrey Clifton-Brown
Caroline Flint
Layla Moran
Gareth Snell

In the absence of the Chair, Sir Geoffrey Clifton-Brown was called to the chair.

Draft Report (*Government borrowing and the Whole of Government Accounts*), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 19 read and agreed to.

Introduction agreed to.

Conclusions and recommendations agreed to.

Summary agreed to.

Resolved, That the Report be the Sixteenth of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Wednesday 24 January 2018 at 2.00pm

Witnesses

The following witnesses gave evidence. Transcripts can be viewed on the inquiry publications page of the Committee's website.

Wednesday 29 November 2017

Question number

Ian Ackerley, Chief Executive, National Savings and Investments, **James Bowler**, Director General, Public Spending, HM Treasury, **Ian Bulmer**, Deputy Director Government Finance, HM Treasury, **Sir Tom Scholar**, Permanent Secretary, HM Treasury and **Sir Robert Stheeman**, Chief Executive, Debt Management Office Q1–118

Published correspondence

The following correspondence was also published as part of this inquiry and can be viewed on the inquiry publications page of the Committee's website.

1 Correspondence with HM Treasury

List of Reports from the Committee during the current session

All publications from the Committee are available on the publications page of the Committee's website. The reference number of the Government's response to each Report is printed in brackets after the HC printing number.

Session 2017–19

First Report	Tackling online VAT fraud and error	HC 312 (Cm 9549)
Second Report	Brexit and the future of Customs	HC 401
Third Report	Hinkley Point C	HC 393
Fourth Report	Clinical correspondence handling at NHS Shared Business Services	HC 396
Fifth Report	Managing the costs of clinical negligence in hospital trusts	HC 397
Sixth Report	The growing threat of online fraud	HC 399
Seventh Report	Brexit and the UK border	HC 558
Eighth Report	Mental health in prisons	HC 400
Ninth Report	Sheffield to Rotherham tram-trains	HC 453
Tenth Report	High Speed 2 Annual Report and Accounts	HC 454
Eleventh Report	Homeless households	HC 462
Twelfth Report	HMRC's Performance in 2016–17	HC 456
Thirteenth Report	NHS continuing healthcare funding	HC 455
Fourteenth Report	Delivering Carrier Strike	HC 394
Fifteenth Report	Offender-monitoring tags	HC 458
First Special Report	Chair of the Public Accounts Committee's Second Annual Report	HC 347

HOUSE OF COMMONS

Public Accounts Committee

Oral evidence: Government Borrowing, HC 463

Wednesday 29 November 2017

Ordered by the House of Commons to be published on 29 November 2017.

Watch the meeting

Members present: Meg Hillier (Chair); Bim Afolami; Geoffrey Clifton-Brown; Martyn Day; Chris Evans; Caroline Flint; Luke Graham; Shabana Mahmood; Bridget Phillipson; Gareth Snell.

Sir Amyas Morse, Comptroller and Auditor General, Adrian Jenner, Director of Parliamentary Relations, National Audit Office, Elaine Lewis, Director, NAO, and Richard Brown, Alternate Treasury Officer of Accounts, HM Treasury, were in attendance.

Questions 1-118

Witnesses

I: Ian Ackerley, Chief Executive, National Savings and Investments, James Bowler, Director General, Public Spending, HM Treasury, Ian Bulmer, Deputy Director Government Finance, HM Treasury, Sir Tom Scholar, Permanent Secretary, HM Treasury and Sir Robert Stheeman, Chief Executive, Debt Management Office.

HOUSE OF COMMONS

Examination of witnesses

Witnesses: Ian Ackerley, James Bowler, Ian Bulmer, Sir Tom Scholar and Sir Robert Stheeman.

Chair: Welcome to the Public Accounts Committee on Wednesday 29 November 2017. We are here to look at the fascinating issue of the Whole of Government Accounts and how Government manage their borrowing. We are considering that on the back of the NAO Report on last year's accounts, "Whole of Government Accounts 2015-16", which came out this summer. We have been looking at this issue as a Committee since at least 2011 and it is fair to say that how well our Government deal with producing this document is world-breaking. No other Government does it as well as we do, if at all. It is a great and exciting document to look at that explains and helps us to understand how Government manage their finances across the piece.

That said, of course, we have a lot of questions today. We are aware that the debt built up from borrowing to plug the gap between what the Government get and what they spend has increased by 61% since 2009-10; that, at £1.3 trillion, Government debt is now equal to about £47,000 per household; and that interest paid on that debt has cost £222 billion since 2009-10. We are talking in more-than-telephone-number figures here. It is important that we do not get lost in those figures, but that we ask the questions—as we will be today—about the liabilities on the balance sheet, the impact of Brexit and other risks and uncertainty that make it harder to predict borrowing. We are excited to be looking at that today.

Before we get into the main hearing, I will introduce the witnesses and then I will bring in Caroline Flint to ask a few questions about the Budget proposals to tackle VAT fraud, if I may—just to give you a moment's warning on that, Sir Tom. The witnesses, from my left to right, are: Ian Ackerley, the chief executive of National Savings and Investments—welcome to you, Mr Ackerley. Sir Robert Stheeman, chief executive of the UK Debt Management Office—welcome to you. Sir Tom Scholar, the permanent secretary at the Treasury—I remember, Sir Tom, we met the day after Brexit, so you have chosen a very interesting time to become permanent secretary at the Treasury. Ian Bulmer, head of financial reporting policy at HM Treasury—Mr Bulmer is the man responsible for the Whole of Government Accounts and bringing it together, so congratulations on progress so far.

Ian Bulmer: Thank you.

Chair: That's the best it gets—drink it up while you can. And then we have James Bowler, director general for public spending at the Treasury. I am sure we will be directing a lot of questions at you, Mr Bowler. First of all, Caroline Flint on VAT fraud.

Q1 **Caroline Flint:** Sir Tom, you can imagine how excited we were when we heard there would be a new measure to tackle online VAT fraud by, from what I understand, ensuring that online marketplaces have better, more connected responsibility for the VAT being paid. But, as our Committee has found and the OBR has pointed out, the amount that could be raised by tackling this sort of VAT fraud has been overestimated in the past and has had to be downgraded several times. How confident are you that this measure can produce better results? How much have you banked on it pulling in?

Sir Tom Scholar: This is an area that has obviously become of increasing concern in recent years, as more and more goods and services are sold online and also increasingly sold cross-border online. So working out what tax is due in each country, very much including the UK, is a much more complicated task than it has been in the past. I think that is probably one of the explanations for why various estimates made at previous points have subsequently had to be revised: it is quite a difficult thing to get a handle on.

We are very determined to tackle this. It is—we think—one of the growing elements in the tax gap: the gap between the tax owed and the tax actually paid. That in part has to be an international effort, because we need to have, both in the EU and through places like the OECD, agreed rules on how we do this. We are taking action there, but we are also taking action directly through HMRC. I must say, I cannot recall exactly the figure that the OBR have scored for it in their fiscal forecast—

Q2 **Caroline Flint:** From what I know, they say that the amount this second attempt will raise is subject to "very high" uncertainty.

Sir Tom Scholar: I think that is a reasonable thing to say. What I would like to say to you and the Committee is that, through HMRC, we will do everything we can to make sure that that number is as high as possible.

Q3 **Caroline Flint:** Do you have any sense of when you will be able to make more public what the estimation might be of what the measure might pull in?

Sir Tom Scholar: Perhaps I can offer you a note on that, because I would need to talk to the relevant experts at HMRC. I do not have the answer at my fingertips.

Chair: We are constantly on HMRC's back on this, and particularly on how they are tackling the fulfilment houses and online marketplaces. Clearly it is potentially an important chunk of Exchequer money, so we will be coming back to you. If you could get us that note, that would be great.

Q4 **Luke Graham:** An opening question for Sir Tom Scholar: a balance sheet is often seen as a snapshot of the health of an organisation, so, reviewing the accounts as they are just now, what would be your diagnosis?

Sir Tom Scholar: The first thing to say is that the Government believes that the level of debt in the economy is too high and it is committed to bringing it down. One of the fiscal rules is to get debt falling in 2021, but the Government intends to bring it down for many years to come. Looking at the financial health of a Government is a bit different from looking at the financial health of a company, not least because there is a major asset which is not recorded under accounting standards, and that is the Government's future ability to raise revenue through taxation. So we look at a number of things, but two things in particular, when we consider the financial health of the Government and the country. One is definitely the Whole of Government Accounts, which, as the Chair said, is the most comprehensive statement available of the balance sheet. We also look at long-term fiscal projections that the OBR provides, which take account of things such as future tax revenues. Those projections are all published—you will have seen them. They show that, in the absence of corrective policies to address the various drivers of debt, debt is projected to rise significantly in the decades ahead. We see a lot of work to do to ensure that debt is on a sustainable path.

Q5 **Luke Graham:** Obviously, we have seen a lot of economic performance re-forecasts, bringing down the deficit and reducing debt. In your opinion, are the Government's current plans going fast enough to reduce that deficit and bring it under control?

Sir Tom Scholar: When setting fiscal policy you always have to make a judgment and balance competing objectives. In particular, when you are looking at a fiscal consolidation—bringing debt down—which many countries are doing at the moment, you need to strike a balance between, on the one hand, doing it quickly enough that you can get it down within a reasonable time to give you protection against future shocks, and, on the other hand, not doing it so quickly that you end up doing damage to the economy in the meantime. There is no science to that. The course that the Government have set strikes a pretty reasonable balance between those two objectives. Some people would criticise it for being too quick and some people will criticise it for being too slow. There is no scientific answer to that, but it seems to me to set out a sensible course for the years ahead.

Q6 **Bim Afolami:** Sir Tom, you said that the Government think that the debt level is too high—that is clear. But too high relative to what? Some may say that our overall debt-to-GDP ratio isn't excessive in comparison with lots of other Western countries. On what basis do the Government believe that it is too high? Ten years ago, we would probably say that where we are is far in excess of where Government would have conceived we would ever go.

Sir Tom Scholar: The main metric that we look at for that is debt as a share of GDP, which is currently higher than it has been at any point in the last 50 years and has more than doubled in the last 10 years, obviously as a result of the banking crisis and then the recession. So it is high by historical levels. Looking internationally, certainly it is true that there are countries with higher levels of debt. There are others with lower levels, too. Most countries feel that their debt level is too high and will be trying to get it down, making the same judgment that I referred to earlier on, about the correct path to do that.

One thing that we take very seriously when looking at this is the information that we get from the Whole of Government Accounts that talks about future liabilities, and from the work of the Office for Budget Responsibility. One thing that the OBR does, very valuably, is look at the public finances and try to work out how they would look if there were some shock or series of shocks to them—for example, a future recession. What that work shows very clearly is that a future recession would make the public finances very considerably worse and could, under certain circumstances, make servicing the debt, through debt interest, quite a challenge.

We look at all that and we think that it is prudent to plan on the basis of creating a buffer that is there to absorb the shock, if the shock comes, as it did in 2008 to 10. It is not a simple one-off look at one measure that gives you an automatic answer. It is a balanced judgment, looking at a range of indicators.

Chair: We will delve into some of that more in our questioning.

Forgive me, I forgot to welcome our visitors from South Africa, and we are also delighted to welcome the Public Accounts Committee from St Helena, who managed to get here on an aeroplane, and we think that's a minor miracle—some of you may have followed our work on St Helena. Welcome to you, and we hope that you can get back okay and land safely back on St Helena.

Q7 **Geoffrey Clifton-Brown:** Following on from my colleague's question on debt as a share of GDP, out of interest, in 2008 it was 36%; today it is 89%. Are you confident that it has peaked at 89% this year and next, as the Chancellor indicated in his Budget?

Sir Tom Scholar: The Office for Budget Responsibility, who do the forecast, show it peaking this year and falling thereafter. Admittedly, in the first few years it is falling very slowly—it is, broadly speaking, flat, slightly coming down. Now, that forecast, like any forecast, is subject to uncertainty—things could turn out better or worse—but what you do see, by the end of the forecast period, is debt on a clearly falling path, including in 2020-21, which is the year at which the fiscal rule operates.

Q8 **Geoffrey Clifton-Brown:** To what extent have you left yourself enough headroom to meet the Chancellor's fiscal targets by 2020-21?

Sir Tom Scholar: Again, the Budget documents show the Government meeting them with some margin—slightly less margin than was there was at the spring Budget six months ago. When we looked at the position and the Chancellor looked at the position, the overall judgment, again looking at the trade-off—the balance of risks I was referring to earlier—the path we set out is one that both provides a small degree of extra support to the economy over the next couple of years and is still consistent with the medium-term objectives on the public finances.

Q9 **Geoffrey Clifton-Brown:** Could you give the Committee an indication of why the margin has come down since the spring Budget?

Sir Tom Scholar: Principally because the OBR is now expecting a slightly weaker economy and a slightly lower path for growth, which in turn is principally driven by a weaker assumption on productivity, which in turn reflects their judgment, looking at the data of recent years.

Q10 **Geoffrey Clifton-Brown:** The Chancellor made a big play in his Budget about needing to reduce the level of debt to deal with the level of economic shock. What reassurance do you have that the Government has the capacity and flexibility to respond to a future recession or economic shock?

Sir Tom Scholar: First of all, we will be better placed once the debt is lower. That is without doubt the case, and that is why the Government has that objective. But secondly, compared to other countries, as I was saying earlier, we are not in any sense an outlier. If you look at what happens when there is a turndown, these things quite often tend to be correlated across countries. On the question of, "Could the Government absorb this on borrowing?", the question there is, "Will there be people who want to lend the Government money? Will people want to buy our debt?" Investors buying Government bonds typically are comparing the relative merits of bonds issued by different countries.

We have shown in the past that we have been able to absorb a very large increase in borrowing—that was certainly the case in 2008—and I am confident that, because of the strength of our framework, we would be able to do so again. But I repeat where I started: the Government does think that the level of debt is too high, and it is committed to bringing it down.

Q11 **Geoffrey Clifton-Brown:** I gave the figure of 89% for next year as a percentage share of GDP, and even by 2021 the Government are only bringing it down to 83%. So it is only coming down very slowly. Are the Government bringing it down fast enough? Is the notion still at risk by the fact that it is so slow?

Sir Tom Scholar: There are two ways that you bring debt down. One is by getting an economy growing faster, and the other is through action on the fiscal front. So a large amount of the policy measures of the Budget is all about improving future productivity and getting the economy growing faster. Obviously, that is not going to happen overnight or even in the next couple of years, but that is an important part of the strategy.

On the fiscal front, of course, it would be possible to make the judgment that we should have a tougher fiscal policy with some mixture of higher taxation or lower spending. You would then begin to question whether that was an appropriate macro fiscal stance for an economy that is currently growing at about 1.5% and projected to slow a little bit over the next couple of years.

I think a much more aggressive fiscal stance would not be the right thing, given that cyclical position at this point. Again, it is a difficult set of trade-offs, especially with debt at the level it is, but I think the approach the Government have set out is a sensible one.

Q12 **Geoffrey Clifton-Brown:** How far might Brexit negotiations throw your figures off course?

Sir Tom Scholar: The OBR have had to make an assumption about that. They have quite deliberately and explicitly not tried to predict the outcome of the UK's negotiation with the EU27, because that is not possible to do at this stage. Instead, what they have done is try to take a set of assumptions on trade, migration and productivity that represent a bit of a mid-point of the possible range of outcomes. Of course, there is no great science to this.

The answer to your question is that it depends what the agreement we reach is and what its impact on the economy is. The Government have said very clearly they are looking for a deep and special partnership with very strong economic links. That might well prove to be something that would be a surprise on the upside, compared with what the OBR are assuming. But of course we do not know what will happen in this negotiation. If—to the extent that that is not achieved and the outcome is less positive, there is clearly downside risk as well.

The simple answer is, we can't say with any certainty at this point in time but what the OBR have tried to do is plot a middle path, with risks on either side.

Q13 **Geoffrey Clifton-Brown:** I detect a little bit of optimism in that reply, which is a good thing. I used in my Budget speech the example of the American war reparations debt, which we took 50 years to pay. Presumably, you will be making representations that we should pay this EU debt off over as long a period as possible.

Sir Tom Scholar: On the direct question of the financial settlement, that is all still being negotiated. I think the Chief Secretary gave an answer to an urgent question on this in the House earlier this afternoon. There are many elements to that negotiation, one of which will be the precise nature of the commitment that we are going to honour and what that means in financial terms and the timeframe over which it will be paid. We don't yet know what that would be.

I would say, though, that the fiscal projections are robust to this financial settlement. They don't incorporate it explicitly because the OBR don't know what it would be. What they do make is what they describe as a neutral fiscal assumption, in that they assume that the money that we currently transfer to the EU as a net contribution is still spent somehow or other by the Government, without specifying how. It could be spent on domestic priorities. Clearly, to the extent that there is a financial settlement, there is money assumed in the Budget there that would be available for that use as well.

Q14 **Geoffrey Clifton-Brown:** My final general, trend-setting question concerns your move from two financial events to one Budget. What effect has that had on your presentation of financial numbers, in terms of Parliament's accountability and transparency and your presentation of these debt figures?

Sir Tom Scholar: It won't have any effect on that at all because, although we won't have a fiscal event in the spring, we will have another forecast prepared and published by the OBR, because there is a legal requirement that they should do two of those a year. All of the information that is currently provided, including through the process of Estimates, by which Parliament votes money, and the various OBR publications, is going to continue as before. The difference is that there will not be a fiscal event with new policy and new measures. We are currently considering what exactly we will do in response to the forecast. We are thinking about that at the moment. It may be, for example, that we would introduce a higher degree of consultation on future Budget measures than has been possible in the past. Parliament will still have the information it has today.

Q15 **Chair:** Obviously, there is not an event in the House—a presentation by the Treasury or Treasury Ministers about what will happen next spring—but we have heard from numerous Departments that they are hitting a stress period in their Brexit preparations. They have to make decisions about what they do next spring and summer. How are you going to make sure those Departments are resourced so we can move out of Europe without things like customs services falling over, given the restraints in the Budget? How are you going to make sure you have got enough resource to do that? What are you going to stop funding to make sure the Brexit transition moves smoothly and the country keeps working? Maybe Mr Bowler wants to come in on that as well.

Sir Tom Scholar: Let me start. In the Budget, we set aside £3 billion—£1.5 billion next year and £1.5 in 2019-20—for use for Brexit preparation in one way or another. That is not yet allocated. That is our forecast of how much we think will be needed across the Government. We will be looking at bids from Departments in the usual way. We will treat them very much as we do claims on the reserve at the moment. Departments that have a need, such as HMRC, will come to us with their assessment—

Q16 **Chair:** Most of them have a need. I think DCLG is one of the handful that doesn't.

Sir Tom Scholar: Yes. I am sure there will be plenty that come to us. Of course, we will first explore the possibility of reprioritisation within their own budget, before looking at calls on this extra money. We will, as you would expect, challenge the level of funding required. We will have a proper process of scrutinising this, as we always do with reserve claims.

Q17 **Chair:** How fleet of foot can you be on this? Maybe this is to you, Sir Tom, or to James Bowler. Some of these Departments have said that they are really up against it. We have had HMRC being very candid with us in this room saying that they need £7.3 million, I think it is, to keep CHIEF—the old customs system—going before they bring in the new one. That sort of money needs to be drawn down now or very soon. These processes—of course there have to be proper checks and balances—can take some time. Have you got the capacity to deal with that? Have they got the capacity, as well as making sure the money arrives at the right moment?

Sir Tom Scholar: I will turn to James in a moment. This year, we have already allocated £700 million to the five most affected Departments, including HMRC. We are confident that we can turn things around quickly. We have done it in the past and we can do it again. We are particularly committed, in the case of Brexit-related spending, to doing that. James, perhaps you would like to add to that.

James Bowler: We ran two allocation processes for 2017-18 in June and September. We turned departmental asks round very quickly indeed. We based our assumptions on the DExEU model of what people need to do to be ready for day one, and we linked the funding to that. Departments bid into a Chief Secretary-led process in the Treasury. As I say, money has been allocated twice in 2017-18, and the process for the £3 billion—the £1.5 billion and £1.5 billion—for future years is under way already for an early set of allocations next year. We are turning things around very quickly indeed. The quid pro quo on that is not to lose sight of value for money, which the Committee will be rightly concerned about. We are doing a streamlined process to allocate the money, but business cases will still be needed to ensure that the large amounts of spending are spent sensibly. The Chief Secretary, as she does for departmental pressures generally, is looking, as Mr Scholar said, at reprioritisation in two ways. First, can the Department absorb any of these funding pressures already? She does that day in, day out, with departmental colleagues. Secondly, there is a bandwidth question that fits with that: does the Department have the capacity to do this and other things too? We will basically be going through our third process on that, on top of setting up DExEU and DIT, which we funded in the autumn statement 2016.

Q18 **Chair:** So Mr Bowler, so far, have you told a Department that it can't do something else? Have you had that conversation where they have agreed to drop another priority? Some of the priorities we have been looking at are quite long in gestation. You cannot just stop a big IT project, for example.

James Bowler: The good news for Departments is that there is additional funding to help them do more. There is a question about whether they can absorb any of that funding and we have those discussions all the time. It is not a Brexit example, but with DFE earlier this year we reprioritised £1.3 billion towards frontline schools, so that is the kind of conversation the Chief Secretary is used to having. But there is also an issue about straight bandwidth in Departments to do those things, and we are having very sensible conversations about that. Much of the £250 million over and above the money we have given to DExEU and DIT in 2017-18 was really about departmental capacity to be ready. It was a lot of staff costs and some IT. It is clearly a huge priority across Whitehall.

Q19 **Chair:** You have given a full answer, but can you give a precise example of something a Department is now not going to do because of the conversations they have had with you about getting funding for something that they need to do, with Brexit looming?

James Bowler: I can't give you an exact answer on that. I would probably say some of those questions are for answering in the future, because much of the spending to date has been additional capacity in Departments to get ready to answer these questions. They probably aren't at that stage yet.

Q20 **Chair:** So when would be a good time for us to ask you the question about what has been deprioritised as a result of those extras?

James Bowler: The Chief Secretary will allocate the first round of 2018-19 funding, as set out in the Budget—that first £1.5 billion—in early 2018. That will have gone through a process of the Department saying what they need and the Chief Secretary asking whether they can do any of that already and whether they have the bandwidth to do that, so there will be a decision there.

Q21 **Chair:** And I am right that you will be reporting that to the Public Accounts Committee as well? That will be our cue.

James Bowler: Okay.

Q22 **Chair:** I think on the written statement it said you would be reporting to the Public Accounts Committee. I am right, aren't I?

James Bowler: On the allocations?

Chair: Yes, and when the money is drawn down.

James Bowler: Yes.

Chair: We will be watching those dates and we will be coming back and asking you and Departments.

Q23 **Geoffrey Clifton-Brown:** Can I just stick with this subject just for a second and ask you a question, Mr Scholar? If there is something that needs to be done in order to make crucial preparations for us leaving the EU, will the money be available? We have heard about CHIEF going to CDS—the IT system in Customs and Excise. Whether it is roads to Dover or whatever is really necessary, will the money be available so that this country is completely ready in March 2019 for our leaving the EU?

Sir Tom Scholar: Yes, that is correct.

Q24 **Geoffrey Clifton-Brown:** Can I just come back to your previous answer about the two fiscal events going into one and the two OBR forecasts? You said you were thinking about how to present that. Can we take it from that answer that there may well be some form of statement in the House in the spring from the Chancellor to respond to the next half-yearly OBR forecasts?

Sir Tom Scholar: That would be a matter for the Chancellor, of course. The forecasts and the OBR productions are always presented to the House. That has normally been done alongside a Budget statement or an autumn statement; of course, in theory, that could be done through a written ministerial statement, but it would be for the Chancellor to decide how he wants to do that. I am sure we will want, though, to find a means of setting out what we make of the forecasts and not just release them without any kind of commentary or Government view on them, but that is something that, as I said, we are thinking about now and that the Chancellor will need to decide in due course.

Q25 **Bim Afolami:** I'd like to switch tack a little, Sir Tom. How does the Treasury monitor the risks that arise from the Government's direct exposure to specific sectors of the economy such as housing or student debt?

Sir Tom Scholar: We have two standing groups in the Treasury that bring together the relevant directors to consider these things. One is what we call the fiscal risk group and the other is the balance sheet group. The fiscal risk group is most relevant to your question, I think. They have a regular, monthly process of looking right across spending and, indeed, tax. That is informed by the work of all the Treasury spending teams, who obviously are in constant touch with the finance departments in all Government Departments. The purpose is precisely to get a sense of fiscal risks that might be emerging.

Q26 **Bim Afolami:** Is there a formal time period that they look at? Is it one year, three years or five years, or does it just depend on what the issue is?

Sir Tom Scholar: Obviously, some risks are long term and others may materialise much more quickly.

Q27 **Bim Afolami:** Let's take student debt. We often think about student tuition fees from the consumer perspective, but if you think about it from a Government fiscal perspective, how do you see the fiscal risk now, looking out 10, 15 or even 20 years' time?

Sir Tom Scholar: I think you are referring to the risk that the loans are not repaid in full. That is driven by the employment prospects of graduates over that time period, their earnings and, of course, Government policy, because that can change and increase—or more likely reduce—the repayment burden. We look at those things internally. The Office for Budget Responsibility also looks at them. The fiscal risks report that they published in July is a very comprehensive analysis and looks specifically at balance sheet issues and student loans. It does a very rigorous analysis every couple of years. We are committed also to publishing a formal response to that, which we will do some time in the first half of next year. We have now created and are entering into a regular cycle, where there is a rigorous and independent analysis of fiscal risks and then a Government response on their view and what they are doing about them.

Q28 **Bim Afolami:** If you look at the Government's direct exposure to particular sectors of the economy—I picked up tuition fees but there are others—what do you see as something that is a particularly big fiscal risk but may not get sufficient attention? I talked about student fees, but everybody is focused on that. Has the Treasury has identified anything as being of potentially significant fiscal risk in the future?

Sir Tom Scholar: There are some future risks that get a lot of air time, such as an ageing population or the demands of extra healthcare. If I had to identify one where more public debate would be welcome, it would be the risks to the tax base. There are number of risks, which the OBR goes through. One example is the increasing trend for people to incorporate and work as self-employed, rather than employees. Other things being equal, that tends to reduce the tax take. Cars getting more fuel efficient tends to reduce the tax take; people giving up smoking tends to reduce the tax take; global competition on corporation tax—

Chair: Sorry—it sounds like you are looking for new things to tax!

Sir Tom Scholar: We are cheerful in the Treasury, as you know.

Q29 **Chair:** You are very welcome to suggest alternatives to us.

Sir Tom Scholar: The question that we started on—the digital economy, which is an extremely important issue—is a risk to the tax take.

Q30 **Chair:** I have to say it must be very gloomy being in your position. If people smoke less—a good thing—it is a bad thing for the Treasury. If people drive less—a good thing—it is a bad thing for the Treasury. I hadn't quite seen your job in such a gloomy light.

Sir Tom Scholar: It is something we share with actuaries.

Q31 **Luke Graham:** On the point about corporation tax and competition, am I right in saying we have been lowering corporation tax? Is it correct that we actually had record corporation tax receipts last year? I understand the point about smoking and the others, but I want to ensure that we are clear on that point about corporation tax.

Sir Tom Scholar: I can't quite remember, but I think that's correct. My point was not about a specific policy measure; it was that there is great tax competition against the world to attract mobile businesses to set up. The tax environment is a constantly moving one. Other countries, by the way, face exactly the same challenges, and I know they are thinking about them. That is an area that, for me, has had less attention in the public debate than some of the spending issues.

Q32 **Caroline Flint:** It is interesting to hear about the nudges in different directions to improve the outcomes of what comes in, but on something like corporation tax, how much are you able to qualify that the amount you are taking is due to reductions in corporation tax as opposed to tightening up the procedures to collect it in the first place? For example, this Committee conducted an investigation into companies like Google. I am not sure that it was a lowering of corporation tax that led to them paying the bill that they had not paid for 10 years; it was to do with public focus on the fact that, regardless of what the level of corporation tax was, they weren't paying it. How do you manage and balance those different pushes and pulls within the system?

Sir Tom Scholar: We have to do all those things. There is the design of tax policy, there is the enforcement of policy and ensuring that the tax due is paid, and then there is a third angle, which is every bit as important: the question of global co-operation, in particular through the OECD. We will only be able to make sure that companies globally are paying the tax that they owe where they owe it through co-operation. Otherwise, we have the situation that we have seen, where companies are able to move profits from one jurisdiction to another and avoid paying tax as a result—perfectly legally, I should say. Tax evasion is a different thing.

Chair: We could get drawn into the tax thing very happily, but we will resist the temptation.

Q33 **Bim Afolami:** Thank you for that response about what does not get covered in terms of this debate. That was genuinely interesting. In terms of how the Treasury is looking at longer-term risks, you have these two committees that look on a monthly basis at the OBR stuff, but how confident are you in the controls you have in place in the event you get something unexpected or uncertain? I am talking not so much about fiscal risk but about the borrowing needs in the market and being fast enough to be able to adapt to things that may change. How confident are you in that context?

Sir Tom Scholar: We have experience of that. If you go back to 2008 and the onset of the banking crisis and the recession, the expected borrowing requirement—the level of borrowing needed week in, week out—increased very dramatically in a very short time.

Q34 **Bim Afolami:** Out of interest, what was your job at that time?

Sir Tom Scholar: At that time I was the director general in the Treasury looking after the financial services sector.

Q35 **Bim Afolami:** So you were pretty closely involved.

Sir Tom Scholar: I can't remember the exact figures, although my colleague Robert Stheeman certainly will, but the increase in borrowing in that year—2008-09—and again in 2009-10, compared with what had originally been planned, was very significant. That said, we have very strong institutional arrangements. The Debt Management Office is a highly respected and competent operation that is well trusted in the market. Because of all that, the market was able to absorb that extra level of gilt issuance and we were able to borrow the extra money we needed despite things changing very quickly.

Q36 **Bim Afolami:** So can I take it from your answer that you are pretty confident, basically, in the systems you have in place? You do not think any institutional changes are needed.

Sir Tom Scholar: We are not at all complacent, and the level of debt is higher than it was then, which is clearly an issue, but I think we have got a very robust set of institutional arrangements.

Q37 **Bim Afolami:** That is helpful. Obviously we are talking about the risk to the Government balance sheet. If you look at the private sector, I think in the NAO Report it says that our private sector net debt is something like 230% of GDP, which is at the upper end internationally. Those are harder risks to monitor, because they are in the private sector. How confident are you about the Treasury's monitoring of those risks, bearing in mind that if something really blows up in the private sector, the public sector might have to assume some of that debt anyway?

Sir Tom Scholar: The way we look at those risks is through the FPC—the Financial Policy Committee—at the Bank of England, which, as you know, we established a few years ago. That is the body charged under statute with financial stability and monitoring that sort of risk. A senior Treasury official sits on the committee, so we have full information through that route.

The FPC published their latest report earlier this week. They note the level of debt in the private sector is quite high and has risen quite high by historical standards. They also stress-test it, and they find that there is no immediate cause for alarm, not least because debt servicing costs are so low at the moment. They do discuss a particular area, unsecured consumer credit, which they have been looking at for some time. In fact, I think it was in October that they encouraged the prudential regulator, the PRC, to tighten up underwriting standards, which it did. And this week they have increased their countercyclical capital buffers again just to dampen down a bit on it. So they are set up to do this, they have got the tools to do it, and that is where—

Chair: We might come back to consumer debt in a moment.

Q38 **Bim Afolami:** Talking about borrowing, if interest rates went to 2%—I always think it is helpful to come up with an absolute number—what would the impact be on demand for British Government gilts, both index-linked and conventional? Would it be significantly affected?

Sir Tom Scholar: Let me say a little bit and then I will turn to Robert. Of course, in part it would depend what was happening to other Government bond yields. You tend to have global movements up or down, and then of course within that you sometimes have specific or relative movements. But we have seen quite large shifts over recent years and demand has remained very solid. Robert, perhaps you would like to elaborate on that.

Sir Robert Stheeman: Just to give you a very brief idea, at the moment, 10-year yields on UK Government bonds are just over 1.3%. If they were to move up to 2%, the reason that they are moving up is in itself nothing more than the market effectively demanding a higher yield—

Bim Afolami: A higher premium.

Sir Robert Stheeman: Absolutely—a higher yield for our debt. Behind your question, to answer that properly, about demand, what is absolutely critical is that that price adjustment process actually works smoothly. You can argue—I am taking this to an extreme—that there is a price for anything, also in terms of supply, but it may not be a price that Government would want to pay. However, critical from where we sit is that the market can adjust and reprice as necessary. Demand would fall away if that price adjustment process did not work smoothly. So, from our perspective, we need—

Q39 **Bim Afolami:** So everything is about the execution of that, as opposed to the decision making per se.

Sir Robert Stheeman: Absolutely.

Q40 **Bim Afolami:** If I take up the different types of gilts, obviously you have the conventional fixed and then the index-linked. Over the last few years—I think I saw this in the NAO Report—we have gradually been increasing the percentage of index-linked rather than conventional. What will you and your team do if rising inflation, which is not a negligible risk at the moment, means that index-linked gilts are less cost-effective but the market continues to demand them, and they seem to sell more easily?

Sir Robert Stheeman: If the market demands them the chances are that they will remain, none the less, cost-effective. Because, if you think about it at the moment, there is not a single inflation-linked gilt out in the market that has a positive real yield. It is heavily negative. The reason for that is that the market is willing to buy this at prices that are cost-effective for the Exchequer, and that enables us to fund cheaply.

I am not trying to downplay the risk of rising inflation and its consequences but I think the key issue, which the Report correctly highlighted, as did the OBR in their fiscal risk report, is fundamentally around the quantum of inflation exposure in the portfolio compared with the conventional nominal exposure, and the need to try to ensure that that balance is got just right.

Sir Tom Scholar: Just to add one thing to that. We said in the Budget last week that we would be looking at the appropriate balance between index-linked and conventional gilts. As Sir Robert said, the NAO highlighted that, as have others. We are also alive to it and will look at it with that risk exposure in mind.

Q41 **Bim Afolami:** That is helpful. If we go on to who holds this debt—obviously somebody has got to hold it—roughly how much of UK Government debt is held by members of the European Union and other nations at the moment?

Sir Robert Stheeman: We do not, unfortunately, have a specific breakdown in terms of the European Union. The statistics and numbers we have we get from the ONS. In their latest publication, the ONS suggest that 27%—just over a quarter—of all gilts are held by international investors across the world.

Q42 **Bim Afolami:** Forgive me, but it seems a bit odd that we don’t know. Is it not possible to know who holds our debt?

Sir Robert Stheeman: To some extent, that is true.

Q43 **Bim Afolami:** So, it is tradeable? Is that the issue—that, once it is traded out, you have no idea who holds it?

Sir Robert Stheeman: Effectively, all gilts are in registered format but a high number of those gilts—the vast majority—are held in what are known as nominee accounts, and those accounts can be anywhere. The actual final identity of all holders is not always known. As I say, the statistics that we have we get from the ONS.

Q44 **Bim Afolami:** Where do they get them from?

Sir Robert Stheeman: They rely on a number of things, in particular on so-called bank-flow statistics, which come from the Bank of England. All that can be seen is in terms of national and international flows. Unfortunately, precise breakdowns are not available.

Q45 **Geoffrey Clifton-Brown:** What are the factors that worry you about the cost of providing finance to the Government to service its debt? Is it inflation, interest rates, the exchange rate, the perception of the UK economy? What are the factors that are worrying you at the moment?

Sir Robert Stheeman: Probably a mixture of all of those. Those are always the ones that are most important. Ultimately, the gilt market trades, as does any other major market of its kind, on confidence. The currency plays a key point in that. It is interesting to note that, where questions have been raised, also about Brexit, over the past 15 or 16 months, in general that plays itself out much more obviously in the currency markets than it does in the gilt market. But clearly the gilt market and the currency are very closely linked.

What is key—I referred to confidence—is in particular in relation to international investors. It is important to note that international investors are not only but quite significantly influenced by official institutions—overseas central banks, sovereign wealth funds—all of whom, in many cases, have an interest in holding gilts, and that that confidence should be maintained. That is not necessarily totally within the gift of the Debt Management Office.

Q46 **Bim Afolami:** Okay, so we cannot know who holds all the external debt, as you have set out. Presumably we know the amount that the British Government effectively owes to itself through QE—in other words, the Bank of England. Presumably we know that number and the percentage of total GDP owed to ourselves.

Sir Robert Stheeman: The total holdings of the Bank of England currently are £435 billion, and that is conventional gilts only. They are not involved in the inflation-linked market.

Sir Tom Scholar: That is about 22% of GDP or something like that. It is a quarter of the outstanding stock, which is nearly £90 billion.

Q47 **Bim Afolami:** Indulge me if this is an odd idea, but is it not true that that is of a different quality in terms of fiscal risk from debt we hold with other nations, because ultimately it is owed to ourselves? I was wondering whether we distinguish between that when we are thinking about these overall debt GDP numbers, as you were talking about earlier, Sir Tom. If 20% of that is owed to ourselves, does it really matter as much as the other debt?

Sir Tom Scholar: The answer is, yes it does. Although at a national level it is held within the UK and within the UK public sector, it is not held by the Government; it is held by the central bank for monetary policy purposes. It has occasionally been put to me, "Why don't you just cancel that debt?"

Bim Afolami: I was about to ask that.

Sir Tom Scholar: I think that would not be a good thing to do, because it would amount to monetary financing. That would, in effect, be the central bank directly financing the Government, and we have seen from many episodes around the world that that takes you on a very dangerous course, possibly even to hyperinflation.

When we look at these two large operations—one being the process of selling debt and borrowing money by the Government, and the other being the operation by the Bank of England to provide support to the economy through its monetary policy—they are two entirely separate operations with entirely separate governance and accountability structures. It is quite right that they should be kept separate.

Q48 **Chair:** I want to pick up on the issue of exchange rates. One thing we have picked up—particularly with the MOD; we are looking at the F-35 as part of carrier strike—is the impact of Brexit on exchange rates. Have you had any thoughts about whether you will change the way you measure the hit on Departments' finances when they are dealing with these big international deals where the exchange rate has a material impact on the financing of that project?

Sir Tom Scholar: I should say that one of the things that has interestingly come out of the preparation of the Whole of Government Accounts is that you can see, on the balance sheet, the foreign exchange liability, which has prompted us to do quite a lot of internal work, looking across Departments at the different ways in which they handle it. Some hedge and some don't; some do for a shorter period, and some do for a longer period.

Obviously, there are very differing degrees of exposure. The Ministry of Defence, which has lots of contracts denominated in dollars, clearly has that exposure. It is one of the examples of things that have come out of this work and then been mainstreamed into the work of our spending teams. As you would imagine, we are talking to the Ministry of Defence about that specific issue at the moment.

Q49 **Chair:** Has anyone in the Treasury done a calculation of what the extra costs of the Brexit bill will be because of the exchange rate problems since we voted to leave?

Sir Tom Scholar: I don't know that—do you mean the direct exchange-related impact?

Chair: Yes, so whether it is £40 billion or £50 billion, what would it have been if the pound had been stronger against the euro?

Sir Tom Scholar: I don't know the answer to that, and I am not sure whether we have done the calculation. You really need to look at the impact on the whole of public finances, which will include a number of things pointing in different directions. What the ultimate net effect would be, I don't know.

Q50 **Chair:** It goes back to the point about how quickly we will pay the bill to Europe. If it is one hit, it hits at a particular point, but if it is spread over time, that will reduce the risk of exposure to the exchange rate. Are you feeding into the negotiations about the rate at which we pay the bill to Europe?

Sir Tom Scholar: That is all part of the negotiations.

Q51 **Chair:** So Treasury is feeding into that.

Sir Tom Scholar: In the negotiation on the financial separation agreement, the Treasury is leading that.

Q52 **Bim Afolami:** Bearing in mind the international context we have already talked about, we have seen what is happening in the United States with attempts to unwind QE and the impact that has had on both the economy and Government borrowing. What do you think the effect of unwinding QE would be on the cost of Government borrowing here in the UK, assuming it is done in a broadly staggered, slow way, as opposed to an abrupt halt?

Sir Tom Scholar: The first thing to say is that it will be the Monetary Policy Committee that decides when and how to do that, because it will be a monetary policy action. They have said on various occasions that they would only start to think about doing that once interest rates got back to what you might regard as a more normal level. A couple of years ago, they said 2%. That is clearly some way off at this point.

You raised the example of the Fed. That is very instructive. It is the first major central bank that has started to back out of these operations. The way they have chosen to do so is by setting out very clearly and transparently to the market ahead of time what they intend to do: basically they are allowing maturing US treasuries to run off without reinvesting the proceeds, and they have set a monthly limit and expect to raise that over time. That is the way they have chosen to do it.

The Bank will have to decide how they want to do it, but it is important, as I said earlier, to keep these two operations separate. The market needs to know both what is coming at it in terms of supply from the DMO and also the impact that the Bank's actions are going to have more broadly. Quite what the impact of that will be would depend on so many other things happening at the time that it is not really possible to say. I think transparency is the key concern here.

Q53 **Geoffrey Clifton-Brown:** Following on from that answer, doesn't the fact that we are still not really unwinding QE demonstrate that there are still significant structural weaknesses in the UK economy?

Sir Tom Scholar: The reason we have QE is because of the extremely low interest rate environment and the inability of conventional monetary policy to do its job under the inflation targeting regime when interest rates are basically on the floor, at the zero bound. That is not just a UK phenomenon, but very much a developed economies phenomenon, although I would agree it is not a normal state of affairs and central banks, just like finance ministries around the world, are hoping to see a more normal financial and fiscal landscape emerging.

Q54 **Luke Graham:** I want to move the conversation on to assessing and managing some of the risks. The NAO Report highlights the growing number of ways to measure and report Government debt and borrowing. That obviously adds to the complexity and produces transparency for a lot of our constituents. With so many sources of information, how confident are you that the Whole of Government Accounts capture the overall risk picture for the Government?

Sir Tom Scholar: First, I agree that it is complicated. There are lots of measures. They all measure slightly different things and they are used in slightly different ways. The reason it is complicated is because it is complicated! It is a complicated business.

What we have tried to do this year in the Whole of Government Accounts, through the opening chapter, is something we had not previously done. I should say that we did it very much in response to the recommendations of the Committee and the NAO. We have tried to add that first chapter to bring it alive and to explain to people what it is telling us at a point in time, about trends over the last few years and what we can expect in the future.

We would be very grateful for any feedback or suggestions of ways in which we could improve that and make it more accessible to people. As the Chair said at the beginning, the Whole of Government Accounts is not just the most comprehensive presentation that we make of the Government's financial position, it is the most comprehensive that any Government anywhere in the world makes. We really want people to use it and inform themselves through it, because that leads to better public debate.

As I said, we have tried to set out the different measures and how they are used. At the very back of the document, we have set out a table and some numbers that reconcile the numbers on the accounting standards basis with the numbers on a national accounts basis. It is all very complicated but we have explained it to the best of our ability.

Q55 **Chair:** Mr Bulmer, is there anything you wanted to add, as the person who draws this together?

Ian Bulmer: Tom's right, in that we made a real effort on this set of accounts to really look at the performance—

Chair: Could you speak up? We are a long way away from you.

Ian Bulmer: Sorry, I am fighting a cold. We made a real effort on the 2015-16 set of accounts to look at the performance report and streamline it, to make it focus on what we thought were the key risks, issues and movements that we should talk about. Perhaps just as importantly, we tried to draw in some of those wider metrics that Tom talked about around the fiscal measures and how the data relate to the figures that are in WGA, just so that, when somebody is reading that report, they get that much more rounded view of what the different metrics are telling them.

I don't think we have the perfect report; there is more work we can do. As Tom said, any suggestions from the Committee would be most helpful. One of the areas we have really tried to focus on is around the pension obligation. We have had a lot of feedback about how we explain what is going on with the pension liability, and we have hopefully met some of the Committee's concerns on that front.

We will continue to improve that report over the years to try to build in more of the information that is available elsewhere without necessarily duplicating everything—that is an important point—but actually cross-referencing with information that is available elsewhere and reconciling those numbers to build that understanding. That is the important bit.

Q56 **Chair:** So in a way, it is looking at UK plc, not just the Government?

Ian Bulmer: Exactly.

Q57 **Geoffrey Clifton-Brown:** On that very answer, Mr Bulmer, how are you using the Whole of Government Accounts to bring together other sources of information that the Government have? For example, the ONS says net liabilities were £1.5 billion, but your Whole of Government Accounts says it is £2.5 billion, because you included pension liabilities, and equally with OBR and affordability, excluding the discount on the long-term liabilities you were talking about. How are you using the Whole of Government Accounts to bring together all those sources of information?

Ian Bulmer: That's a question for my colleague.

James Bowler: The way I put it is that there are national accounts and Whole of Government Accounts. The national accounts is a very timely measure—it is updated every month—and we use it to budget. We can use it to budget because you can work out what is going to happen and when, and it is comparable with how you compare the UK to lots of other Governments and countries around the world—public sector net borrowing, flow and the stock of public sector net debt.

The Whole of Government Accounts is less timely—you might come to that; we are trying our hardest—but it gives you a lot more information, particularly on assets and liabilities. We use that less for the in-year budgeting framework and more for fiscal risks. We also use that more for looking at some of the questions that Sir Tom has been discussing about what is coming down the track and what we should do to make sure we are insulated as far as possible from fiscal risks in the future—are we using our balance sheet and assets correctly? What are we doing about our liabilities and, indeed, our contingent liabilities? It is complicated, but it is horses for courses. I hope that helps to explain it.

Luke Graham: To return to that point, Mr Bulmer, having worked as a management accountant in my previous life for a corporate, I can only imagine the challenge you have had, so all credit to you for that.

Chair: The compliments are flowing today. Other Departments will get jealous.

Q58 **Luke Graham:** Are you linking with other public and private bodies to help to explain the Whole of Government Accounts to the general public and other interested parties, so they can use the information effectively to interpret Government data and performance?

Ian Bulmer: Yes, we are. I think it is kind of in two halves. There is what we are learning internally within Government from best practice accounts—from what some of the other Departments are saying in their own performance reports—and how we can reflect that in the Whole of Government Accounts. We recognise that this is an area that we need to do a lot more work on, but we are also starting to learn a lot more from the private sector, in terms of how it explains what is also a complex business for it in a relatively summarised way.

The answer is that internally we are doing a lot more learning from our own departmental reports, and there is a little bit more that we can do to work with external companies in terms of getting best practice from there.

Q59 **Luke Graham:** So am I right in saying that there is an internal process taking place at the moment where you are trying to standardise a lot of the internal management reporting as well, so information can be pulled in on a much more timely basis?

Ian Bulmer: Absolutely.

Q60 **Luke Graham:** Okay, great. This question is for Mr Bowler. We have the introduction of the newer measure of public sector net financial liabilities, in addition to public sector net debt and net borrowing. How can you make sure those measures will be used consistently? Certainly, one of the biggest challenges we have as politicians is that when debating and discussing financial measures and budgets, you are constantly undercut by other politicians—or you may undercut them—using different measures. How can we ensure we have a bit of consistency so that we can give the public some assurances about the measures that are being used, and make sure that it is true news and not fake news?

Q61 **Chair:** There's a challenge: stop politicians misusing numbers.

James Bowler: I'll try. There are two things that people mainly focus on, and there is a handy chart on page 3 of the Whole of Government Accounts, if you have it in front of you, which goes through them. There are two ends. One has the national accounts, which would have public sector net debt. The other has the full WG Accounts and net liabilities. The addition of public sector net financial liabilities that you mentioned adds illiquid financial assets—things like student loans and some of the things that we cannot immediately cash in. That gives us a slightly wider definition. It shows you, for example, that if you have just sold a load of shares, that helps public sector net debt, but it might not help public sector net financial liability. I would suggest you focus on either end—either national accounts or Whole of Government Accounts.

The one thing I would say, not least through the auspices of this Committee, is that the balance sheet—the end with everything in; the Whole of Government Accounts—is just much more part of the discussion on financial and fiscal sustainability. If you look at your reports on clinical negligence, on nuclear decommissioning and so on, Departments in their own accounts are taking much more of a view now of that. The Whole of Government Accounts has driven that and I think it is a move for the good. But yes, there are different definitions.

Q62 **Luke Graham:** What I am trying to get to is that, to change behaviour and better inform decision making within Departments and in the political sphere, you think the public sector net financial liabilities measure would be a more comprehensive measure when looking at all our liabilities? You mentioned student loans; that obviously becomes an active part of the political debate. I say this to you in terms of making sure that these things are taken into account so we get a true picture and the public does, too.

James Bowler: It is a more comprehensive measure. There is no question about that. But we measure our fiscal rules on public sector net debt, which is the slightly less comprehensive one. That is the one that is internationally comparable. If you said, "How is the UK doing vis-à-vis France on debt levels?" that is what you would use. I would not move off public sector net debt to public sector net financial liabilities and cast public sector net debt aside, if you see what I mean.

Q63 **Luke Graham:** Understood. Are there any moves for international benchmarking on the public sector net financial liabilities? I am sure some other states would have some very interesting information within those, if they collect those figures.

James Bowler: Yes. There are some pretty big numbers in Whole of Government Accounts. It is interesting that we are the country that publishes it all and points out that there are liabilities of trillions of pounds here. I think transparency is really important. We have had the IMF tell us recently that on fiscal issues we are probably one of the most transparent Governments around.

I take your point that we have the challenge not just to produce lots and lots of complex figures but to explain them to Government, the public and Parliament, and we need to rise to that challenge.

Q64 **Luke Graham:** To add another complexity, we have obviously seen the rise of value being held in intangibles worldwide, especially with the development of the economy. I know that at the moment you are compliant with the international accounting standards on intangibles.

Considering that, by some estimates, about 80% of the S&P 500 value is held in intangibles, and a lot of that is not being captured within current accounting standards, are there any moves happening in your Department, or are you doing any work internationally, to try to capture that value, to ensure that we are not missing out anything on the Government's accounts?

James Bowler: That was the perfect tee to ensure that I mentioned to you that we announced in the Budget a balance sheet review. That is using the data in Whole of Government Accounts precisely to ensure that we are getting the best value for the balance sheet that we hold.

That includes more traditional things such as estate rationalisation and perhaps pooling investments. One thing we particularly want to look at is those intangibles. The Government, for example, itself produces a lot of software. As you say, in the private sector that would be of very large value, so we want to look at that. That balance sheet review—

Q65 **Chair:** You can see that by looking at the intellectual property aspect of that can you?

James Bowler: Yes. That balance sheet review is a very good example of not just publishing something but doing something with it.

Q66 **Luke Graham:** Just to move this on a little. The NAO Report identified some of the Treasury's work in strengthening the approach to evaluating the balance sheet, as we have all complimented today. Sir Tom, how will the Treasury embed the balance sheet group into the routine business and ensure that the work of that group is going directly to inform decision making?

Sir Tom Scholar: We are doing that now. The first way is through the balance sheet review that Mr Bowler just talked about. That is going to inform decisions over the next year, we hope across a range of Departments, and we hope to find considerable savings from that exercise.

That is one way; the other way is simply through the exercise of the balance sheet group and the fiscal risk group that I mentioned earlier. That brings together all of the relevant directors—not just directors of the fiscal and economic groups but the public spending directors and the tax directors. Everybody has the same information. It is fully integrated into the work of the Department. They produce a monthly summary of fiscal risk that goes to the management.

Q67 **Chair:** If I can follow up on that, earlier Mr Bowler raised clinical negligence and nuclear decommissioning. These are liabilities that are looming pretty large. Are there any Departments where there are liabilities that you think they are not yet really understanding or taking into account, where you want to nudge them harder and faster to understand the wider financial picture?

Sir Tom Scholar: As you know, we have got a new system this year on contingent liabilities. In the past, more or less, a Department that wanted to enter into a contingent liability, entered into it, informed Parliament and informed the Treasury. Unless there was something particularly special or, in the jargon, novel and contentious about it, it did not require Treasury approval. That has changed. Now, any contingent liability has to be put to the Treasury first. We stress-test it. We look at, first, is it necessary to take it on? Could we could avoid or reduce the size of it in some way? How is the Department going to manage it? How is it going to forecast it? How are we going to keep a handle on it? We have been through 24 or 25 such cases in the course of this year. In some cases, they have either been considerably modified or withdrawn as a result.

Q68 **Chair:** Can you give any examples of ones that have been withdrawn?

Sir Tom Scholar: I don't have any examples at my fingertips, and it may be the case that I won't be able to give them because they relate to negotiations of commercial contracts.

Chair: I thought you might say that, but it was worth a try.

Sir Tom Scholar: I did ask.

Q69 **Chair:** What about ones that you have modified?

Sir Tom Scholar: Again, can I come back to you? If we can find some good examples, we would like to give them to you.

Chair: It would be good to have some concrete examples. This goes back to the point about people understanding this, including us. It helps us to have some concrete examples to pinpoint what the benefits are of having Whole of Government Accounts and this approach.

Q70 **Luke Graham:** It was great to hear about the monthly summary of risk analyses coming through from the Departments. To put that against Mr Bulmer's comments about the inconsistency in the management accounts being produced on a monthly basis, how far do you think Departments have to go to get truly accurate risk information that you, at the centre, will be 100% happy with? What is the percentage of accuracy in the information you are getting at the moment, in terms of helping to inform decision making?

Sir Tom Scholar: Let me give an overview, and then Mr Bowler might want to add a bit. Just as we in the Treasury have devoted much more attention to balance sheet issues over the last couple of years, not least as a result of finding out more about it through the whole process of preparing Whole of Government Accounts, I think it is fair to say that Departments were devoting less attention in the past than they are now. Of course, in our discussions with them at spending reviews and so on, we require them to make provisions for liabilities, which leads naturally to that conversation. What we are really hoping to do in the year ahead through this whole exercise we have been talking about is to shine a much stronger light on all this and challenge Departments further to improve their ability to manage both their assets and liabilities. This is going to be quite a big exercise over the next year.

Chair: It sounds like that is going to be a lot of work. It will be interesting for us when we see you next year.

Sir Amyas Morse: I am very much in favour of that exercise, but given that you are looking at Whole of Government Accounts that are for the year finishing April 2016, just how much actual decision making can possibly be based on such out-of-date numbers? We are all sitting saying how great they are and how much use you are making of them, but can you explain a little more why they are actually useful to you if they are so out of date?

Sir Tom Scholar: Some things change quickly in Government finance, and some things change slowly.

Sir Amyas Morse: That sounds like a Nick Macpherson remark.

Sir Tom Scholar: I'm not sure whether that is a compliment. I will take it as such.

Clearly some large liability that has emerged since then is not captured, and there may be things that are changing or growing rapidly since that date that we are not yet completely on top of and will find out more about. We are going through the preparation now of last year's accounts. A lot of these things develop over time, and a snapshot, even if it is 18 months ago, is pretty valuable. In particular, because it pulls together information from right across the public sector—it gives us a look across the board at things we might not have otherwise picked up. I mentioned earlier the question of foreign exchange and currency liability. Another example would be the use of the estate—property rationalisation and so on. That probably does not change rapidly, but that is an example of where even out-of-date information is valuable.

Chair: James Bowler has something to add.

James Bowler: I have two examples of that. We have been in court with Littlewoods on a tax liability case for 13 years. We won the case at the Supreme Court at the start of November. I think HMRC estimated that, with the immediate exposure and follow-on cases, that was a £17 billion potential liability. That has been something on our risk register that our fiscal risk group has been looking at for 13 years. On clinical negligence, we saw the Secretary of State for Health's welcome announcement earlier this week about maternity safety. I think about 80% of clinical negligence costs, at least for the Department of Health, are maternity-based, so you can see that the exact number does not necessarily need to be exactly up to date to know that you need to take great steps forward in those kinds of areas.

Q71 **Luke Graham:** Just one point. Obviously, cash holdings and the balance sheet are quite significant. We had the illustrative forecast for central Government net cash requirement, as provided by the NAO, which saw a significant change from the spring 2017 Budget to the autumn 2017 Budget. The cash requirement is up 17.7% for 2020 and 24% in 2021—billions of extra cash required because of, as has been previously mentioned, the fall in productivity forecast. What kind of stress is that putting on the Department, Mr Stheeman? Are we 100% confident that we will be able to meet those cash obligations?

Sir Robert Stheeman: I suppose I have to say that you can never be 100% confident, because ultimately it is down to the market and not down to us. Having said that—Tom referred to this earlier—if you think about some of the increases that we saw 10 years ago, exactly this time 10 years ago we were in a position where we had started the financial year with a gilt remit of £80 billion. That was revised in October to £110 billion. It was subsequently revised in November to £146 billion. We ended that year with £146 billion in March 2009 and started the following year borrowing £225 billion. So if you think how within six months we had to go from £80 billion to £225 billion, that gives you a sense of a couple of things. One, which is critical for what we do, is that it is operationally possible, although under pressure, and we were under pressure then. Secondly and more importantly, it tells you something about the elasticity of demand in the market, the flexibility of the market, has necessary to respond. We cannot be 100% confident, but it is fair to say that, based on past experience, you can draw some comfort from that.

Please see footnote.

Q72 **Chair:** I just want to go back to the issue about the relevance of the Whole of Government Accounts. What resource would you need, Mr Bulmer, to make sure you could get this together more quickly so it could be more timely? Is it resource or is it just kicking the other Departments into a speedier reaction?

Sir Tom Scholar: May I say something first? The two things that make the preparation particularly complicated and affect the timetable are, first of all, the need to incorporate all the local authority accounts and, secondly, academy schools, of which there are a large number. They are both currently on a financial reporting timetable of end of August/beginning of September, so their accounts by definition are not available until the autumn.

Q73 **Chair:** They have been brought forward from where they were.

Sir Tom Scholar: In the case of local authorities they are moving forward.

Q74 **Chair:** Schools have moved forward.

Sir Tom Scholar: Schools are where they are. As far as I know, there is no plan to change that. That is just a fact. It is very important that the accounts are comprehensive in their coverage. That is the whole purpose of them. Our intention, as you know, is to publish within a year, so we would hope that the accounts for 2016-17 would be ready by the spring of next year. Obviously this year we were a little late: we published in July. The principal reason for that was the general election. Without that, we would have been ready to go in April. We are targeting the end of the financial year. We would like to improve on that in the future and get it by the end of the calendar year. That is probably about as good as we are ever going to be able to manage, but we are dependent on, first, local authorities and, secondly, the Department for Education, which have this very difficult task—

Q75 **Chair:** So how long will it take before we can get them by the end of December for the previous financial year?

Ian Bulmer: Sir Tom just set out the two remaining issues. There is a point about whether we can just become a bit more efficient in the Treasury, and I think we have probably reached the limit as to how quickly we can do these accounts internally, so it is precisely those two issues that are preventing the earlier publication. On the local government side, their statutory deadline is the end of September, which is coming forward to July in 2017-18. So from 2017-18 their accounts will get published three months earlier, and that will enable us to bring forward the timetable.

Secondly, with academies, the Committee will be aware that this is the first year that academies produced their sector report, with an August year-end for 2015-16. That is still 13 months after their academic year-end, which is an issue that we still need to deal with at WGA, but we are hopeful that over the next year or two, now that we have the sector report established, we can work with DFE and get that information into WGA on a more timely basis. I cannot really give you a precise date, but we will make staged improvements over the next couple of years, and by 2018-19, assuming local government—

Q76 **Chair:** So assuming all those things, it could be by the end—

Ian Bulmer: Assuming they happen, 2018-19 could be an aspiration for—

Q77 **Chair:** That is a stretch target.

Ian Bulmer: It is a stretch target, yes.

Q78 **Chair:** Do you need any powers to get academies and local authorities to fall in line? Is it about that or is it just practical?

Ian Bulmer: We have the legal powers already. It is more about the practicalities of dealing with 5,500 or 4,500 academies.

Q79 **Chair:** What about using the accounts to break down spending by region or nation? Is that something you are looking to do?

James Bowler: You asked about that last time, and you challenged us to do it. What we have done is make a link to the public expenditure statistical analysis, which does break spending down by region. We have reconciled—I think it is on page 8—the categories in PISA into that. We have done a reconciliation between Whole of Government Accounts and PISA, which publishes things by region and country. To be honest with you, if we actually got all 6,000 of these accounts to tell us all the information they do regionally—each academy tells us where they purchase all their things from by region—that is a very large undertaking.

Q80 **Chair:** Short of that, surely you could get more broad-brush information at least?

James Bowler: I think that is a fair challenge. What we should do for the next time is show spending by region, which is what we publish every September, and try to reconcile between those two, which I hope would be a step forward.

Chair: I think you get a sense from around the table that we think that would be a good idea, but you will have to wait for our report before we make it a final—you are halfway there.

Q81 **Luke Graham:** I have one quick question, which I may have missed when you were speaking earlier. Mr Bulmer, on the timeline to bring the internal management accounts and the internal risk analysis up to the standard that Sir Tom was talking about earlier, what is the deadline for that? We heard it for the Whole of Government Accounts and their production, but for the internal information, to help with the decision making—

Ian Bulmer: You mean for departmental accounts?

Luke Graham: Yes.

Ian Bulmer: For central Government, they have an administration deadline of July. For local authorities, as we said earlier, it is September.

Q82 **Luke Graham:** Is that the same for the internal management accounts—the monthly risk assessments that were referred to—to get their accuracy up? Is there a deadline? You said there is quite a big programme of change taking place. Is there also a deadline to deliver that?

Ian Bulmer: There is a whole monthly programme of data, management information returns, from the Departments. I do not know the exact date, but it is something like working day five or six of a month that we get that information in.

Q83 **Luke Graham:** So it is performing to working day five or six already?

Sir Tom Scholar: Can we check that? I cannot recall, so let me check that and come back to you.

Q84 **Luke Graham:** Absolutely, that is fine. One final observation from me. From the NAO Report, we saw some quite big differences between the UK's performance and our comparable neighbours. On public debt, Germany's is about half of ours; on private debt, Ireland's is considerably higher than ours—I think it is 422% of their GDP. The question may be to you, Mr Bowler: what does "good" look like for us? Are we looking at a floor and a ceiling on public and private debt respectively, because they are between comparable nations? As we go through the Brexit discussion and the UK is put more into a European and broader international context, it would be great to be able to say where we are performing and what good looks like, for our country at least.

James Bowler: I would say two things. I think those two examples reflect the housing market in each of those countries—certainly on the private side. On the public side, I think the permanent secretary has set out what we want to do, and the Government's position is that debt is too high and they want to reduce it. On the private side, the key thing to look at is unsecured debt—debt that isn’t backed by an asset—and we have a mechanism to do that. I cannot give you a band. We have a target to reduce public sector debt; I am not aware of a target level for private sector debt.

Chair: Okay, we will come back to some of those issues.

Bim Afolami: Mr Ackerley, you have been very patient over there.

Chair: You thought you were getting away with it!

Ian Ackerley: Yes I did, actually. I was rather hoping I would get a free run, but there we go.

Q85 **Bim Afolami:** How cost-effective do you think NS&I is?

Ian Ackerley: I think we are very cost-effective. I would point, first of all, to two tables in the Report that show the effective interest rates comparing gilts to NS&I. I think you see a comparison there over the last three years of about 3% on gilts and about 1.5% for NS&I. I think that shows one measure of it. There are a couple of other things to look at, one of which is our value indicator. We have to be very careful with the value indicator. It is an indicator—an indicative measure. The objective of that is to try to compare the cost of raising debt financing through ourselves as opposed to through the gilts market. You will see from that that last year it was £74 million, and over the last few years we have successively raised significantly more than that. I think that gives you an indication that we can do it. We are obviously constrained to a degree by needing to balance the interest of the taxpayer, offering a fair return to our savers, but also the general stability of the sector.

Q86 **Bim Afolami:** Is that not the difficulty when you look at your organisation? Because the better a deal the investor gets, on some level the worse deal the taxpayer gets, albeit recognising the obvious point that the investor is a taxpayer too. Is that not the tension at the heart of your organisation?

Ian Ackerley: Absolutely.

Bim Afolami: Do you think that you have the right balance? Are you in the right spot? The reason I ask is because the 65-plus guaranteed growth bond—I have a few years before I get to do this—was “the biggest selling retail financial product in Britain’s modern history". Something would tell me that if it was such a big hit, maybe it was too good a deal.

Q87 **Chair:** Mr Ackerley, I think you were at Virgin Money before, is that right? It would be interesting to know if Virgin Money would have delivered such a product.

Ian Ackerley: I will leave that to Jayne-Anne Gadhia and the Virgin management team to answer that question. The answer is that we have to distinguish here between a few different activities that NS&I does. We have a core remit, which is raising cost-effective financing for

Government, and we very carefully monitor the value we are adding, et cetera. There is another activity, which is delivering what we call policy products on behalf of the Treasury, and 65-plus was a good example of that. That was a product developed in response to a request from the Treasury. The Chancellor explicitly wanted something that would reward savers who were aged over 65, and therefore its policy objective was about rewarding those people and providing them with an attractive product. To be very explicit, that didn't appear in the value indicator score for NS&I, because it was such an attractive product for the consumer. In those situations, we are balancing a slightly different equation.

Bim Afolami: How much influence—

Sir Tom Scholar: Sorry, could I just add something? It was explicitly scored in the Budget as a policy measure with the expected cost to the Government, so it was taken outside NS&I's remit in that way.

Q88 **Bim Afolami:** I see. So it had a spend next to it. Is it in that table in the Budget?

Sir Tom Scholar: It's in the table in the Budget, yes.

Q89 **Bim Afolami:** What was the cost of it in the Budget? I can't remember what it was.

Chair: You might not be able to remember right now. If you can't—

Ian Ackerley: I do not have the number to hand, but I can let you have it.

Chair: If you want to write to us—

Ian Ackerley: We'll write to you with that number.

Chair: Well, we can probably look it up.

Q90 **Bim Afolami:** That's fine. I'll probably look it up. It's okay.

What you are saying, if I am right, is that there are two types of NS&I product. You get the ones that are the real policy ones and then the normal ones. Is that right?

Ian Ackerley: Yes, broadly speaking, that is the way it works. We have a suite of established products, such as premium bonds, which have been around for 60 years, and the other side of it is the policy products. Most recently, this year, we are delivering the investment guaranteed growth bond, which is another policy product, on behalf of the Treasury.

Q91 **Bim Afolami:** On that, to what extent does it pose a challenge to you to stay within your remit and not distort the market? Being a good Conservative, I don't like things that distort markets. To what extent does that pose a challenge?

Ian Ackerley: We are very explicit at the start of each year in publicising how much we are planning to raise overall. It is publicised usually as part of the April Budget. It will get released again as part of some event in the spring. So we flag that to the market. That enables our competitors to be very clear on how much we are looking to raise in the next 12 months. So we try to manage that, and we monitor constantly where we sit in the market and keep very aware of what we might do to others.

Q92 **Bim Afolami:** Let me take what you have said in the round. Would you see it as a success or a failure if, for example, in five years' time we were sitting here and NS&I occupied a much larger share of the retail market?

Ian Ackerley: That is very difficult to say, because so many factors come into it. It is worth saying that in 2000 our market share was over 12%; today our market share sits at less than 9%, so our market share has fallen quite considerably during that period.

Q93 **Bim Afolami:** Say that went up to 15%, not necessarily as a deliberate policy aim—say, it was just where you were after five years of various things going on. Do you think that would be a success or a failure for you?

Ian Ackerley: Obviously, in terms of growing the business, it would be a success. I think the critical thing here, though, is that we would be doing that only if we felt it was the right thing for the market, as well as for the customers, as well as for the taxpayer. We would get to that stage only through a very careful process of evaluation, so it would be done very deliberately. We would not allow that to happen on an accidental basis.

Sir Tom Scholar: May I just add one thing? My recollection is that in 2008-09, National Savings saw a very considerable inflow of funds without doing anything to its interest rate—

Q94 **Bim Afolami:** That makes sense—it was a flight to safety.

Sir Tom Scholar: Because it was a flight to safety and it was guaranteed. If I remember correctly, we did get plenty of complaints at the time, particularly from smaller savings institutions—building societies, co-operatives and the like—and National Savings took action to reduce the inflow, precisely because of its concern for the health of the market overall.

Q95 **Chair:** I want to pick up on a couple of points. Earlier, permanent secretary, you referred to the OBR's "no Brexit" counterfactual, which is that if money is not going to Europe, it is going to be spent on other things. How confident can you be about making that assumption prior to the final deal being hammered out in Brussels?

Sir Tom Scholar: To clarify, are you referring to what the financial settlement might be? Well, let me try to answer and then you will tell me whether I have answered the right question. What they are doing is to say, first of all, they do not know what the financial settlement will be. Secondly, they do not know what the future relationship will be and whether it will involve any future financial relationship. You can easily give examples of where it would, and you can easily give examples of where it would not and they do not know. I think—it is slightly presumptuous of me to speak for them, but they are not here—that it is a neutral assumption, in that that is money we are currently paying. In the future, it seems almost completely certain that we will be paying less than we currently are because we will not be a member of the EU.

Q96 **Chair:** Yes, but we might be paying more to do certain things because we are having to change our procedures, trade arrangements, customs systems and so on to deal with Brexit. How confident are you in the assumption that the money being spent on Europe now could be spent directly on other services, rather than just on the new things we might have to do as a result of Brexit?

Sir Tom Scholar: They are trying to do a slightly different thing, which is to look at a medium-term assumption. They are not trying to forecast how much it will cost to—

Q97 **Chair:** So what would you say is the point at which we might get that Brexit dividend, where money that would have gone to Europe is instead coming into the Exchequer and being spent on public services or whatever the Government of the day decide to do with it, rather than being absorbed by the changes that will need to take place to deal with Brexit?

Sir Tom Scholar: The main thing that will decide that will be, first, the level of the financial settlement and, secondly, the timetable over which it is to be paid, which we were discussing earlier.

Q98 **Chair:** So no dividend in the next three years. Would you hazard that?

Sir Tom Scholar: It depends what—I am sorry to keep going back, but this is being negotiated right now in Brussels.

Q99 **Chair:** Well dodged. We shall be watching. I suspect it is not in the next three years at least, but we will leave that, and our sister Committees will be following that too. One of you mentioned intellectual property and in particular IT projects. Is intellectual property generally something you are looking at analysing more effectively through your work, to persuade Departments to analyse more effectively? That is a huge potential benefit to Government. I remember the Home Office science team doing a lot of innovative work, and that is sort of lost to the Exchequer. If it was a private company, they would be holding it tight and getting the value.

James Bowler: The answer is yes, and that is one of the areas that the balance sheet review we announced as part of the Budget is going to look at, particularly where there is a set of software issues.

Q100 **Chair:** Particularly software. Is anything else being developed in MOD or Home Office?

James Bowler: MOD certainly has a whole set of those intangibles. Let us do the review and come back to see where we get to.

Chair: We will earmark it as a question for next year.

Q101 **Caroline Flint:** The NAO Report focuses on Government borrowing, but it notes that private borrowing is also very high, with consumer debt rising at 10% per year, while household incomes have only been rising at 2% per year. That is quite interesting, given that we are almost at full employment levels. You would think that would put a pressure on bringing wages up and people having more in their pocket, to not rely on personal debt. How worried are you that higher private indebtedness poses a greater risk to the economy than Government borrowing?

Sir Tom Scholar: We have set up a body—the Financial Policy Committee—at the Bank of England to look precisely at that and other financial stability risks. They are the people who primarily are looking at this. A Treasury senior official is a member of it, so we get full visibility, and you get visibility because they publish their reports after each meeting. Their conclusion is that yes, it is high; it is high historically and quite high compared with other countries. They have been concerned in particular by the growth in unsecured consumer lending and have taken various actions in the last few months to try to dampen that down a bit. They do not see it as an immediate cause of alarm, in part because of the very low debt servicing costs in a very low interest rate environment, but if it continues to grow, we would expect them to take further action, and they have a number of tools at their disposal to do that.

Q102 **Caroline Flint:** It is quite worrying that some measures of private debt have risen back to pre-crisis levels. It is a sign of an unhealthiness in the economy that, although we have more people in work, which is a good thing, the income that they are getting does not meet what they expect to have as consumers in terms of a decent way of life. Add to that the number of people who are in work but increasingly reliant on Government back-up support while they are in the workplace, on going to food banks and everything else they might be doing, and on possibly taking out loans elsewhere that add to their insecurity, and it is a worrying picture, isn't it, against the background of low levels of productivity that we continue to have.

Sir Tom Scholar: It is certainly the case that real incomes are suffering a squeeze at the moment, not least because of the rise in inflation. We hope and expect that that will now start to come down, but because inflation is higher than wage increases, that is putting a squeeze on people's disposable income. I am sure that that is one of the explanations for what is happening here. The central message of the Budget was the need to improve productivity—precisely to improve real earnings. We completely recognise the urgency of that.

Q103 **Caroline Flint:** What would be the top two changes that you would make, or think should be made through the Budget, to increase productivity? We borrow money and part of that borrowing is to invest in areas like infrastructure or whatever it may be, but it seems so far that Government borrowing over the last seven years or so has not contributed to changing that picture. Now borrowing will increase again.

Sir Tom Scholar: It is certainly true that the poor performance of productivity in the last few years has definitely been one of the most disappointing features of the UK's economic performance. In the Budget, in the industrial strategy, we set out the areas where we think we need to focus: infrastructure, investment, long-term capital to support new technologies, skills and transport. They are all things that we think will change the productivity position, if we can make a sustained effort on them. But as I said earlier, that is not something that will happen immediately; it is bound to take some time.

Q104 **Chair:** We will no doubt delve into that further. On the issue of personal indebtedness, will the WGA begin to analyse the risk of the interest-only mortgage? For many people, it is the only way they can afford a home but it means that once people reach the end of the mortgage term, they have no asset—no home. That will potentially put demands on all sorts of parts of the public sector. Is that on your horizon and in your planning?

Sir Tom Scholar: In terms of the financial stability issue, it would be done through the machinery that I have described before. In terms of its impact on living standards and the public sector more broadly, that is something that we would certainly look at. We would also want to talk to our colleagues at the DWP because often—

Q105 **Chair:** It is a looming liability that there are people who only pay the interest on their mortgage. They will never have somewhere to live afterwards and they will then go to the DWP, as you rightly highlight, needing support at that point. Has anyone quantified that risk?

Sir Tom Scholar: I am not aware of any figure or study to quantify that, but it is something we should certainly be looking at.

Q106 **Chair:** Will you be looking at that?

Sir Tom Scholar: Yes, and again, I can come back to you on that.

Q107 **Chair:** Okay. If you can come back to us with more detail, we will be very pleased to see it. Before I move on to Geoffrey Clifton-Brown, on maternity safety, which you mentioned Mr Bowler, we have looked at clinical negligence on this Committee for some time now. Was the announcement on maternity safety a direct result of the issues around clinical negligence? It was very much focused on the needs of parents, which is absolutely right, but was that a driver in formulating that policy and was the Treasury involved in that at all?

James Bowler: No, I don't think it was. The Treasury has been involved with clinical negligence and the Department of Health for a number of years. There is a cross-Government group and a £250 million maternity fund. The answer is that greater maternity safety is a core measure of a good health service. They have a target to reduce stillbirths, and it was brought forward from 2030 to 2025 by the Secretary of State. That is a good example of how investment in that kind of area will also reduce clinical negligence. I am not sure about the figure, but I think about 80% of the Department of Health's clinical negligence costs are maternity-based, so it was not that the Treasury forced the Department of Health to do it.

Q108 **Chair:** So there is a double dividend: a better deal for the parents, but also potentially for the public purse.

James Bowler: Correct.

Q109 **Geoffrey Clifton-Brown:** Sir Tom, may I ask you a couple of questions on growth, which is a fairly critical element of the economy? The Budget numbers show that the trend of reduction in growth is continuing, unfortunately. The OBR forecast evaluation report in October stated at paragraph 1.16 that "business investment has been very weak since the crisis. Business investment today is just 5 per cent above its pre-crisis peak almost a decade ago; in contrast, a decade after the 1980s and 1990s recessions, investment was 63 and 30 per cent higher than the pre-recession peaks respectively." Does this structural weakness of the economy worry you, in terms of the rates of growth?

Sir Tom Scholar: Yes, we are very concerned. As I said, a major feature of the Budget was a set of measures to address the UK's productivity performance. I suspect that one of the reasons—perhaps even the main reason—for the difference in performance in recovery between the recession now and those in the '80s or '90s is that the last recession was caused by a major crisis in the financial sector and banking. It has also been the experience in other countries that investment recovers particularly slowly from that kind of episode. Having said that, it clearly needs attention and we will do what we can to address that.

Q110 **Geoffrey Clifton-Brown:** Private sector investment is very low and Government investment is also fairly low: we invest about 2% of GDP, or £90 billion, which is much less than many of our main rivals. Has austerity meant that we have cut spending in the wrong areas—things like investment and infrastructure? Has that had an effect on growth?

Sir Tom Scholar: During the period of fiscal consolidation, of course there were effects on budgets across the board. I cannot remember the run of figures on Government investment, but we certainly set out plans in this Budget and in last year's autumn statement to increase it in the years ahead. That includes quite an ambitious target for increasing spending on research and development, another area in which historically we have tended to lag behind others. Thinking back, my sense is that Government spending, both on investment in general and on research in particular, has tended to be lower than in other major economies over a run of decades; it is not particularly a phenomenon of the last few years.

Q111 **Geoffrey Clifton-Brown:** No, but could one of the factors that explains why the trend in growth is declining be because Government is not spending enough on investment? As you indicated, investment takes quite a long time—sometimes many years—to have an effect.

James Bowler: The only thing I would add is that Government investment capital spending is at a historic high—the highest level for quite some years. The Chancellor has made an intervention with NPIF—the National Productivity Investment Fund—and they are actively trying to change that situation.

Q112 **Geoffrey Clifton-Brown:** The final question is whether, given the trend of slowing growth, the figures you started with at the beginning of this session for repayment of total debt are achievable over the period to 2021.

Sir Tom Scholar: In the best view of the OBR, those figures for the public finances are based on that projection for the economy. Any forecast is uncertain and things can turn out differently, but their view is that, given the growth of projection that they are expecting, that is where they see the public finances going. I think what the Government will try to do, and has set out the industrial strategy this week, is improve on that and surprise on the upside by taking a range of measures that will strengthen productivity, improve growth and bring the debt down more quickly.

Q113 **Geoffrey Clifton-Brown:** Do you think this slowing of growth is a temporary phenomenon possibly caused by Brexit, or do you think it is now a more permanent feature of the economy?

Sir Tom Scholar: In the report prepared by the OBR, they are quite clear in saying that this is driven by productivity. They have a rather good chart in the report—it is very interesting—that shows productivity growth pre-crisis and since crisis, and then the successive projections they have made every six months in that time. They kept expecting—they were not the only ones; plenty of people did—productivity to pick up its previous trend, and it has not happened. They have now made the assumption, which I think is a prudent one, that that is not about to happen. They still have some recovery pencilled in, but it is very much a structural medium-term phenomenon, rather than a temporary or cyclical one.

Q114 **Chair:** I have one final question about the Brexit funding packages that are available to Departments. In some circumstances, Departments may have to request a ministerial direction to get the money. In what circumstances would you at the Treasury require a ministerial direction for that money to be spent?

Sir Tom Scholar: This is an important issue but quite a technical one, and it all relates to proper authority for spending money. A Department can only spend money if it has been voted by Parliament and if it has legal authority to spend it. Then of course there are questions of value for money and so on. This is explicitly not a value-for-money issue; it is about the proper legal or parliamentary authority.

There are a few areas of spending where a Department is, in the future, going to need to take on a function that is currently taken on by somebody else—for example, some European agency. A Department might need to start spending money now in order to ensure they are ready by March 2019 but do not currently have legal or parliamentary authority. In a number of cases, they will get that authority once the EU (Withdrawal) Bill is on the statute book, but that is some months down the track, and they might need to spend the money now.

We wrote round to all accounting officers to set this out. In those quite limited circumstances, the solution is a direction from the Secretary of State in which there is a transparent exchange of letters where the accounting officer says, "I need to spend this money on this service, but I don't have legal authority to do so," and the Secretary of State says, "Yes, you do need to."

Q115 **Chair:** Those narrow circumstances—we heard this from Clare Moriarty at DEFRA—are the only ones in which you would accept a ministerial direction.

Sir Tom Scholar: Yes, and DEFRA is one of the Departments most affected.

Chair: With so much of its business in Europe.

Q116 **Caroline Flint:** I understand that earlier on today, the head of HMRC, Jon Thompson, told the Exiting the European Union Committee that it will cost HMRC more than £1 billion over the next five years because of the 5,000 new staff who will have to be hired in preparation for Brexit. Do you concur with that assessment? In the light of the Chair's earlier question, given that HMRC seems to be quite clear about what it will have to do to prepare for Brexit and how much it will cost, how quickly will we have the information I just outlined from other Departments on the costs for them and what that will mean in real terms, in terms of staff or other resources they will have to find?

Sir Tom Scholar: I have not seen his precise remarks, but it sounds, from what you quote, like he was making his assessment of what the cost will be over a number of years. I have no reason to think he is wrong about that, but that is not the nature of the discussion we are now having. With HMRC and other Departments, we have already assessed what they need in terms of additional funding this year, 2017-18, and we have allocated £700 million to the Departments most concerned, including HMRC. Now that the Budget is done, we are starting immediate discussions with them about what they are going to need in 2018-19. There is £1.5 billion available for that, and I am quite sure HMRC will be one of the Departments that needs additional funding, because as he said, they have a big job on their hands. We are in a constant round of discussions with the spending Departments most affected by the need to prepare for EU exit, and we will make sure they have the funding they need when they need it.

Q117 **Chair:** Will the next Whole of Government Accounts have a line that explains, so that we can all see transparently, how much Brexit is costing in terms of money being put into Departments to deal with it?

Sir Tom Scholar: First of all, the next Whole of Government Accounts will cover the year 2016-17, so that will be a rather small number. In terms of transparency, we are just entering the usual round of supplementary estimates, which will include the money agreed for this year for reserve claims, including those related to Brexit, which obviously will be voted by Parliament in the usual way. We would expect a very high degree of parliamentary interest in the money to be allocated in 2018-19 and beyond, and I am sure we will be disclosing it one way or another well ahead of the Whole of Government Accounts.

Q118 **Chair:** It would be very helpful to have a line in the WGA that clearly lays that out. We talked earlier about this being more easily understandable by the general public. I am sure the National Audit Office will be crawling over all this, but it would be helpful if it was offered up in a spirit of openness by the Treasury.

Sir Tom Scholar: I am not sufficiently nimble to know exactly how the application of the standards would then—can I appeal to the Comptroller and Auditor General, who is very expert in how Government accounts are prepared?

Sir Amyas Morse: Let's wait and see what happens, and I will do my best.

Chair: We won't let this one go, and nor will our sister Committees.

Thank you all very much for your time. We are well aware that we have just had 10 hours of highly paid Treasury officials' and other finance officials' time. We appreciate that and your preparation. We think the Whole of Government Account is an extremely useful tool for Government. You have heard our concerns about it, and I think you share a number of those. We will publish our uncorrected transcript on the website in the next couple of days, and our report will be out in due course; I cannot give you an exact time. We look forward to seeing you again, no doubt very soon.

Footnote –Q71: Clarification made by witness. In answering Q71 Sir Robert Stheeman said "If you think about some of the increases that we saw 10 years ago, exactly this time 10 years ago"…when referring to the increase in the borrowing requirement following the bank bailout operations conducted by the Treasury.

He meant – "exactly this time of year", as the increase came at the autumn fiscal event in 2008. That was of course nine years ago (not 10 as he may have said).

Witness would like the clarification to be "If you think about some of the increases that we saw around 10 years ago, exactly this time of year [9 years ago]".