National Audit Office

HM Treasury: Certificate and Report of the Comptroller and Auditor General

Whole of Government Accounts 2013-14

This report has been prepared under Section 16.1 of the Government Resources and Accounts Act 2000

Contents

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

I certify that I have audited the financial statements of the Whole of Government Accounts (the Account) for the year ended 31 March 2014 under the Government Resources and Accounts Act 2000. These comprise the Consolidated Statements of: Revenue and Expenditure, Comprehensive Income, Financial Position and Changes in Taxpayers' Equity; Cash Flow Statement; the related notes; and Annexes 1 to 4. These financial statements have been prepared under the accounting policies set out within them.

Respective responsibilities of the Accounting Officer and auditor

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

Scope of the audit of the financial statements

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

Basis for qualified opinion on financial statements

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

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

However, in Note 1.22 to this Account, HM Treasury defines the accounting boundary for the Account by reference to those bodies classified as being in the public sector by the Office for National Statistics. I consider that it would be more appropriate to assess the accounting boundary with reference to the accounting standards. By applying such accounting standards, I consider that the Account should include Network Rail.

I also consider that HM Treasury's accounting policy has not been applied consistently in 2013-14 as a number of significant bodies, including Royal Bank of Scotland, have not been included in the Account, even though they are classified by the Office for National Statistics as being in the public sector and which I also consider should be included in the Account in line with applicable accounting standards.

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

- Network Rail which has gross assets of £53.9 billion and gross liabilities of £45.7 billion;
- publicly-owned banks which have gross assets £1,027.9 billion and gross liabilities of £968.7 billion; and
- other bodies which have estimated gross assets of £16.6 billion and gross liabilities of £5.9 billion.

Qualification arising from disagreement relating to inconsistent application of accounting policies

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

- bodies in the local Government sector follow the Code of Practice on Local Authority Accounting in the UK for 2013-14;
- bodies that follow either pure IFRS or UK GAAP; and
- bodies that follow the Charities Statement of Recommended Practice.

Accounting standards require that, where the effect of such inconsistent accounting policies are material, adjustments should be made on consolidation. HM Treasury has undertaken an assessment of these differences and identified one material inconsistency, but has not been able to adjust for this in 2013-14. This inconsistency is where infrastructure assets included in the Account are valued on an inconsistent basis. Assets held by local authorities are valued at historic cost, whereas those held by central Government bodies are valued at depreciated replacement cost. HM Treasury's estimate of the understatement of assets due to the difference in valuation between historic cost and depreciated replacement cost for local authority assets could be at least £232 billion (Note 13 to the accounts). I do not have the information to fully quantify the effect of all inconsistent applications of accounting policies.

Qualification arising from disagreement in the accounting for 3G and 4G licences

In April 2000, the Government issued licences to access the 3G telecommunications spectrum. Each licence was awarded for 20 years and the total raised was £22.5 billion. This was recognised as £22.5 billion of income in 2000-01. In March 2013, the Government issued further licences to access the 4G telecommunications spectrum. As with 3G, each licence was issued for 20 years and the total payments were £2.4 billion which was recognised as income in the 2012-13 financial statements. In respect of both sets of licences I consider that it would be more appropriate to recognise this income over the life of the licences as the licence holders have the right to access the spectrum for 20 years and the Government has an on-going obligation to ensure that the spectrum remains available to licence holders, exercised by the Office of Communications. The impact of this difference is that income would be £1.3 billion higher; liabilities would be £8.9 billion greater (£10.2 billion in 2012-13); and the value of the general fund would be £8.9 billion less (£10.2 billion in 2012-13).

Qualification arising from limitation of audit scope due to lack of evidence supporting the completeness and valuation of schools' assets included in the Accounts

Local authority maintained schools are required to be included in the Account. There is insufficient evidence over the completeness and accuracy of the valuation of assets held by these schools. Local authority maintained schools' assets, which are estimated to be up to £21.8 billion (2012-13: £23.0 billion) of assets from voluntary aided and foundation schools and £7.7 billion (2012-13: £8.1 billion) of assets from voluntary controlled schools, have been omitted from these Accounts.

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

The external auditors of the financial statements of 4 bodies that are consolidated into this Account qualified their audit opinion. Of these, two are of material significance to this Account, qualifications of the Departmental Accounts of the Ministry of Defence and the Department for Education.

- **Ministry of Defence Resource Accounts:** The Department has not complied with the Financial Reporting Framework as it has not accounted for the expenditure, assets and liabilities arising from certain contracts in accordance with International Accounting Standard 17, Leases. Consequently, I have concluded that the Department has omitted a material value of leased assets and lease liabilities from its Statement of Financial Position as at 31 March 2012, 31 March 2013 and 31 March 2014. This has also led to a material misstatement of the Statement of Comprehensive Net Expenditure for 2012-13 and 2013-14; and Statement of Parliamentary Supply for 2012-13 and 2013-14. I am unable to quantify the impact on the financial statements because the Department has not maintained the records or obtained the information required to comply with International Financial Reporting Standards in this respect.

In 2012-13, I qualified my opinion in respect of the valuation of inventory and certain non-current assets in the form of capital spares recorded in the financial statements. During 2013-14 the Department performed an adequate impairment review and charged impairments of £860 million to the Statement of Comprehensive Net Expenditure. I have therefore been able to obtain sufficient, appropriate audit evidence to support the valuation of £6.4 billion of non-current asset Capital Spares and £3.3 billion of non-explosive inventory, held on inventory systems subject to previous qualification, at 31 March 2014. My opinion on the financial statements is qualified in respect of the corresponding figures for the asset values at 31 March 2013.

- **Department for Education Resource Accounts:** The Department consolidated 3,905 academies using a number of data sources with different reporting periods. This has resulted in a level of misstatement and uncertainty that I consider to be material and pervasive to the group financial statements.

  In addition, the Departmental Group has recognised academy trust land and buildings of £31 billion in its Statement of Financial Position. The audit evidence available to me was limited in respect of this balance because the Group was unable to demonstrate that these all met the recognition criteria for a non-current asset under International Accounting Standard 16 Property, Plant and Equipment.

Qualification arising from limitation of audit scope due to lack of evidence supporting the completeness of the elimination of intra-Government transactions and balances

Accounting standards require that balances and transactions held and made between bodies consolidated into this Account shall be eliminated in full. HM Treasury has a process in place to identify intra-Government balances and transactions between bodies consolidated into the Account, and most balances and transactions have been eliminated. However, there remain significant values of intra-Government transactions and balances which have not been eliminated and the effect of not adjusting for these could lead to a potential overstatement of up to £7.3 billion (£9.1 billion in 2012-13) in gross income and expenditure and up to £2.2 billion (£3.7 billion in 2012-13) in gross assets and liabilities.

I have reviewed the impact of this uncertainty and have assessed that the maximum uncertainty resides within the gross figures in the individual primary statements rather than on the net deficit or net liabilities. The totals reported for the net deficit and the net liabilities are subject to a maximum uncertainty of some £0.5 billion (£1.3 billion in 2012-13). This information is derived from where only one body has reported an intra-Government transaction or balance or there is a mismatch on the amounts reported.

There is also uncertainty about whether there are amounts which both bodies involved in a relationship have not reported, leading to further overstatement.

Qualified opinion on financial statements

In my opinion, except for the effects of the matters described in the Basis for Qualified Opinion paragraphs above:

- the financial statements give a true and fair view of the state of the affairs of the Whole of Government Accounts as at 31 March 2014 and of its net deficit for the year then ended; and
- the financial statements have been properly prepared in accordance with the Government Resources and Accounts Act 2000.

Emphasis of matter – nuclear decommissioning provisions

In forming my opinion on the truth and fairness of these financial statements, I have considered the adequacy of the disclosures made in areas where there is significant uncertainty in the values reported in Note 1.22.5 to the financial statements, which concerns the uncertainties inherent in estimating the likely costs of the liabilities of the Nuclear Decommissioning Authority. As explained in the Note, the lengthy timescales, final disposition plans for waste and spent fuel, timing of final site clearance and the confirmation of site end states mean that the ultimate liability will vary as a result of subsequent information and events, and may result in significant adjustment over time to the value of the provision, which currently stands at £64.9 billion (£58.9 billion in 2012-13).

Opinion on other matters

In my opinion, the information given in the Foreword, Performance Report, Comparison to National Accounts, Remuneration Report and Governance Statement, for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception

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

- the financial statements are not in agreement with the accounting records or returns; and
- I have not received all of the information and explanations I require for my audit.

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

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

My Report on pages 9 to 41 includes more details of the matters leading to my qualified opinion.

Amyas C E Morse
Comptroller and Auditor General
23 March 2015

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

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

Summary

1 The Whole of Government Accounts (WGA) is a single set of accounts consolidating the financial activities of the UK public sector. The WGA for 2013-14 is the fifth such set of audited accounts to be published by HM Treasury (the Treasury).

2 The WGA consolidates the financial activities of over 5,400 organisations from across the public sector into a single set of audited accounts showing the overall public sector financial position. It includes both central and local Government bodies as well as public corporations such as the Bank of England.

3 The WGA is now a key part of the Treasury's framework for improving public financial management and accountability to Parliament for the Government's financial position. The WGA is increasingly being used within and outside of the Treasury to inform decisions which affect public finances. As such, improvements to the quality and timeliness of the WGA help to increase its value to the Treasury in its own management of the public finances; and improve accountability to Parliament and the public.

4 Since the 2009-10 WGA was first published, the Treasury has made continuous improvements to its processes for compiling these accounts, to data quality and to its commentary published alongside the accounts. As a result, the Treasury has been able to reduce the publication time after the year end from 20 months in 2009-10 to producing the 2013-14 WGA within one year of the reporting date, meeting a major milestone in its aim of delivering WGAs within nine months of the year end.

Scope of my financial audit

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

6 I applied the concept of materiality in planning and performing my audit; and in evaluating the effect of misstatements on my audit opinion and on the financial statements. This approach recognises that financial statements are rarely absolutely correct, and that an audit is designed to provide reasonable, rather than absolute, assurance that the financial statements are free from material misstatement or irregularity. A matter is material if its omission or misstatement would reasonably influence the decisions of users of the financial statements. Part 2 provides more detail on my approach to determining materiality and the materiality levels applied to my audit of the WGA

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

8 The main risks for my audit of the WGA relate to the past qualifications, which are set out in Part 2 of this report. These relate to four broad themes: the boundary of the WGA and its application; areas of inconsistency in accounting treatments; disagreement over accounting treatments; and the quality of the data that forms the financial statements. I am also required to consider the following by International Standards on Auditing:

- The risk of material fraud arising from the approach to recognising revenue, which I addressed through my understanding and assessment of the Government's approach to recognising the main revenue streams via my audit of HM Revenue and Customs; and

- The risk of management using its influence to override the embedded controls that support the production of the financial statements and manipulate the financial results within the WGA. This risk is a particular challenge for the WGA, due to the range of sources of figures that constitute the accounts and level of adjustments that the Treasury processes to produce the consolidated figures. I addressed this through my audit of these adjustments and my assessment of how the transactions streams and balances within the underlying accounts that form the WGA are reflected within the consolidated financial statements.

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

Conclusions

10 I completed my audit in line with my planned audit approach. I have qualified my audit opinion on six counts this year, relating to: the application of the WGA accounting boundary; inconsistencies in the underlying accounting treatments within the WGA; disagreement on the accounting treatment of 3G/4G mobile licences; lack of evidence in support of the completeness and valuation of school assets; underlying material qualifications of the Department for Education and Ministry of Defence accounts; and inaccuracies in the elimination of intragroup transactions and balances.

11 In reaching these opinions I am satisfied that I have obtained sufficient appropriate evidence in relation to these qualification areas and the additional risks related to the risk of fraud in revenue recognition and the potential for override of the accounts production process controls by management.

12 My Report covers:

- In **Part 1**, the context for my audit of the 2013-14 WGA; and the progress the Treasury has made in taking forward recommendations made in previous years by the National Audit Office and the Committee of Public Accounts; and
- In **Part 2**, why I qualified my audit opinion on the 2013-14 WGA, and the progress made by the Treasury in resolving my qualifications.

Key findings

13 The WGA shows the UK public sector's overall financial position, as defined by accounting standards. In 2013-14, the WGA net expenditure (the shortfall between income and expenditure) decreased by £30.1 billion to £148.6 billion largely due to an increase in taxation revenues and stabilisation of overall expenditure. Direct expenditure (monies incurred in the direct delivery of the Government’s policies) fell for the first time since 2010-11, by £2.2 billion in 2013-14 to £663.6 billion, mainly due to a reduction in provision expenses offset by increases in the purchase of goods and services. Within this overall expenditure, the overall cost of benefits has fallen for the first time to £213.4 billion from £215 billion and staff salaries have also fallen to £146.2 billion from £147.6 billion.

14 The Government's net liabilities (the shortfall between asset and liabilities) increased to £1,851 billion as at 31 March 2014 from £1,627.9 billion at 31 March 2013, largely due to increases in public sector pension liabilities of £130 billion and Government borrowing of £99.9 billion.

15 The 2013-14 WGA is a true and fair account of the use of public resources, but my opinion remains qualified. My audit opinion on the 2013-14 WGA is similar to that for 2012-13 and previous years as significant issues remain with the boundary of the financial statements and quality and consistency of the data. However, the Treasury is progressing with its plans to address the issues that have led me to qualify my audit opinion, particularly with regard to eliminations of intra-Government transactions. If these plans are successful, I may be able to remove a number of my qualifications within the next four years.

16 The Treasury published the 2013-14 WGA within one year of the reporting date for the first time, which is a significant achievement. This will allow for more effective transparency and accountability for how public finances are

managed. The 2013-14 WGA was published 12 months after the reporting date compared to 20 months for the 2009-10 WGA. This improvement is part of the Treasury's aim of delivering the WGA within nine months of the year end. It also reflects the fact that the data collection and accounts production processes supporting the WGA have become much more embedded and better controlled since it was first published. To achieve further improvements in delivery, the Treasury needs to work with the bodies that provide data to support the accounts to improve the timeliness and accuracy of the information that it receives.

17 WGA is one part of a wider set of processes which the Treasury uses to manage risks to the public finances. The Treasury has improved its analysis of the trend data within WGA, which is starting to reveal the impact of the process of reducing the budgetary surplus and improvements in the performance of the economy. For example, the 2013-14 WGA shows the effect of increases in revenue flowing through from the emerging economic recovery; the process of restructuring the benefits regime; and reductions of public sector staffing on salaries. The Treasury's analysis of trends in the Government's assets and liabilities can, however, still be enhanced to demonstrate the full financial impact of changes in the delivery of public service in the next Parliament

18 The Treasury is taking steps to make disclosures in WGA more detailed and transparent. However, there is more to be done in this regard, particularly in relation to the disclosures on: the purchase of goods and services; the risks related to borrowing; and fraud and losses across Government. Enhancing disclosures in these areas will help the reader to see how Government spends taxpayers' money; assess the impact of the Government's management of the economy on borrowing; and understand the main sources of financial loss.

Recommendations

19 Although responsibility for the underlying transactions lies with the various bodies included in the WGA, my recommendations are aimed at the Treasury, because it has ultimate responsibility for preparing the WGA. The Treasury should:

- **Continue its work in improving the quality and timeliness of the data within the WGA so that it is a true and fair account in all respects**. The Treasury should review the causes of late and erroneous data within the component bodies making up the WGA and set out an action plan for resolving them at an individual component level.

- **Build on developments in financial management across Government to improve the consistency of accounting and financial reporting across the public sector.** This will improve the comparability of data within the WGA and the Treasury's ability to analyse trends across Government.

- **Continue to raise the profile of the WGA within Government and embed it in the routine monitoring of risks to public finances.** As use of the WGA within Government increases, the Treasury should seek to provide greater insight into the continued process of reducing the budgetary surplus, termed fiscal consolidation, within the next Parliament and monitor the risks to the delivery of this programme. As the process of fiscal consolidation evolves, the Treasury should build on its analysis of in year spend to demonstrate the impact of Government policy on the assets and liabilities it is responsible for, to illustrate its approach to managing the increasing net liability position.

Part One: The context for my audit of the WGA

The Whole of Government Accounts

1.1 The Whole of Government Accounts (WGA) is a single set of audited accounts consolidating the financial activities of over 5,400 bodies, representing most of the UK public sector. It is the largest consolidation of public sector accounts in the world and includes central and local Government and public corporations such as the Bank of England; but not independent public sector organisations such as Parliament, the Crown Estate or the National Audit Office (**Annexes 2** and **3** to the WGA set out entities that have not been consolidated). The WGA sets out what the Government owns (assets), owes (liabilities), spends (expenditure) and receives (revenue).

1.2 The Treasury compiles the WGA and has overall responsibility for delivering it as a “true and fair” representation of the financial position and performance of Government as a whole. It has also provided a detailed Performance Report (**Chapter 2**) which sets out the Government's financial performance for 2013-14.

The context for my audit of the 2013-14 WGA

1.3 Statistics on the Government's financial position are routinely published in the *National Accounts*, monthly *Public Sector Finances Report*, the *Public Expenditure Statistical Analyses* and other sources. These produce two main measures which HM Treasury use for fiscal management: C*urrent Deficit* and *Public Sector Net Debt*.

1.4 The WGA provides a broader view of public finances based on accounting standards. The Treasury sets out the key differences between the two approaches and the reported financial position in **Chapter 3** to the WGA. Between 2009-10 and 2013-14, net expenditure as shown in the WGA has fluctuated whereas the ONS's Current Deficit fell year on year[1]. The WGA also shows that the Net Liability has fluctuated over the same time period whereas Public Sector Net Debt has increased[2].

WGA Net Expenditure

1.5 The WGA shows that net expenditure, the shortfall between income and expenditure as defined by accounting standards, was £148.6 billion in 2013-14

[1] Paragraph 3.28 and Public Sector Current Budget Deficit Table in Chapter 3

[2] Paragraph 3.14 and Public Sector Net Debt Table in Chapter 3

(**Figure 1**). This compares to £178.7 billion reported in 2012-13. The reduction is largely due to increases in revenue against broadly stable overall expenditure.

Figure 1

Key elements of the Whole of Government Accounts 2013-14

	Examples	**2009-10**	**2010-11**	**2011-12**	**2012-13 (restated)**	**2013-14**
Assets	Land and buildings, student loans, taxes due.	1,249.5	1,234.3	1,270.6	1,297.5	1,337.3
Liabilities	Public sector pension schemes, Government borrowing.	2,477.4	2,420.0	2,617.5	2,925.4	3,189.1
Net Liability		**1,227.9**	**1,185.7**	**1,346.9**	**1,627.9**	**1,851.8**
Revenue	Taxation, rental from local Government housing.	(583.4)	(614.0)	(616.6)	(620.7)	(648.5)
Direct Expenditure **(Paragraph 1.6)**	Benefit payments, staff costs, grants, contributions to the EU.	619.5	663.3	647.8	665.8	663.6
Other Operating Expenditure	Pension scheme costs and impairment of assets.	47.7	(38.4)	67.3	51.5	54.4
Net Financing Cost	Interest paid on borrowing.	78.6	83.2	88.1	79.4	78.8
Other assets	Revaluation of financial and liabilities and net loss on disposal of assets.	0.3	0.3	(1.3)	2.7	0.3
WGA Net Expenditure for the year		**162.7**	**94.4**	**185.3**	**178.7**	**148.6**

All figures are in £ billions

Sources

2009-10 - NAO analysis of restated prior year values in 2010-11 WGA

2010-11 - NAO analysis of restated prior year values in 2011-12 WGA

2011-12 - NAO analysis of restated prior year values in 2012-13 WGA

2012-13 - NAO analysis of restated prior year values in 2013-14 WGA

2013-14 - NAO analysis of 2013-14 WGA

1.6 In the 2011-12 WGA, the Treasury introduced a new way of explaining the trend in public spending, called Direct Expenditure. The Treasury's definition of Direct Expenditure is monies incurred in the direct delivery of the Government's policies. This uses items in the WGA's Consolidated Statement of Revenue and Expenditure but excludes those that result from the revaluation of assets or are actuarially determined, as these are outside the direct control of individual entities within the WGA, and finance costs. Performance using this measure shows that in 2013-14, Direct Expenditure fell to £663.8 billion from £665.8 billion last year[3]. This reflects falls in:

- provision expenses to £19.7 billion from £29 billion;
- social security benefits to £213.4 billion from £215 billion;
- depreciation to £28.2 billion from £29.2 billion; and
- staff costs to £146.8 billion from £148.4 billion.

1.7 These reductions were offset by:

- increases in grants to £59.8 billion from £56.3 billion; and
- the costs of goods and services and other costs to £189.8 billion from £182.3 billion.

The WGA Net Liability

1.8 Since the WGA was first produced covering 2009-10, the net liability has increased to £1,851.8 billion from £1,227.9 billion (Figure 1). Over this five year period, the most significant factor was the issuance of £314.3 billion of Government debt to finance the deficit. An increase of £167.2 billion to public sector pension liabilities was mainly due to actuarial assumptions, current service costs and financing costs, offset by a significant decrease caused by increasing payments in line with the consumer price index instead of the retail price index in 2011-12.

1.9 In 2013-14, the Government's net liability increased by £223.9 billion to £1,851.8 billion. The mainly was due to a £130 billion increase to public sector pension liabilities and £99.9 billion increase to Government borrowing. This increase in the overall net liability position is likely to continue in the coming years due to continued deficits in the public finances.

Improvements made since the 2012-13 WGA

1.10 The Treasury continues to improve the WGA and take forward recommendations made by both the National Audit Office and the Committee of Public Accounts. Since I last reported, the Treasury has taken forward a number of initiatives which aim to improve the robustness, timeliness and quality of the WGA, and use the WGA to help inform the Government's financial position.

[3] (**Figure 1** above**, Table 2.4 in the WGA Performance Report**).

Reflecting the Government's fiscal consolidation measures within the trend analysis in the Performance Report section of the WGA

1.11 The 2013-14 WGA shows the initial financial impacts of the Government's major fiscal consolidation and growth programmes during this Parliament. This demonstrates the valuable contribution the WGA can make to the transparency agenda and in demonstrating the overall impact of this consolidation.

1.12 There are three areas where economic growth and fiscal consolidation measures can be seen within the WGA: increases in taxation revenue; revisions to the social security benefits regime under the control of the Department for Work and Pensions; and reductions in the employment in the public sector. These are set out below.

Taxation revenue

1.13 The WGA shows a significant increase in the Government's revenue arising from taxation to £555.8 billion from £524.4 billion[4], which represents 6 per cent of revenue. This increase is broad based but mainly arises from: increases in income tax receipts of £11.2 billion, which is the first increase in such receipts in the WGA since 2010-11 and reflects the improved employment position since the 2012-13 WGA; VAT of £9.1 billion reflecting an increase in consumer spending; and stamp duties of £3.4 billion, reflecting the increased activity in the housing market since the 2012-13 WGA.

1.14 The only major taxation stream that has not increased is local taxation, which fell to £52.8 billion from £55.9 billion, mainly due to the effect of changes to the benefits regime which impacted on council tax and changes to the regime for non-domestic rates.

Social security benefits

1.15 Total social security benefits have fallen in the WGA for the first time this year, to £213.4 billion from £215 billion[5].

1.16 This reflects:

- increases to state pension payments, which are the largest benefit stream, to £85.0 billion from £83.8 billion, reflecting the uprating of pensions by 2.5 per cent;
- increases in the Employment Support Allowance to £10.9 billion from £6.7 billion;
- falls in housing and local Government benefits to £27.3 billion from £28.5 billion, reflecting the revisions to the housing benefit regime;

[4] Note 3 to the *Whole of Government Accounts 2013-14*.

[5] Note 6 to the *Whole of Government Accounts 2013-14*

- falls in child benefit to £11.5 billion from £12.2 billion, reflecting the removal of the benefit from higher rate tax payers;
- falls in income support payment to £4.0 billion from £5.7 billion, reflecting the revisions to the benefit regime; and
- falls in incapacity benefit to £1.3 billion from £3.5 billion reflecting the revisions to the benefit regime.

Reductions in public sector wages and salaries

1.17 Public sector wages and salaries have fallen to £146.2 billion from £147.6 billion[6], reflecting the initial impact of the reduction in public sector staff numbers which can be seen in the WGA this year. Overall staff numbers within the public sector have fallen to 4.454 million from 4.615 million, a reduction of some 161,000 staff. This reflects the transfer of employment from the public to private sector, arising mainly from the sale of Royal Mail in October 2013, and the balance of changes in staffing rates across the public sector.

1.18 The WGA, in note 7.3, shows 72,445 compensation packages arising from staff leaving the public sector during the year, at a total cost of some £1.8 billion. These costs are expected to fall during 2014-15.

1.19 In the 2014-15 WGA the impacts of the fiscal consolidation should be more clearly identifiable in the Performance Report as the trends in revenues, benefits, staff reductions and changes to pension contribution rates within public sector pension schemes become more prominent and wide ranging.

Earlier delivery

1.20 The most significant step forward this year has been the timeliness of the delivery of the WGA. For the first time, HM Treasury has published the 2013-14 WGA within a calendar year of the reporting date. Given the scale and complexity of the consolidation, this represents a significant achievement. However, the Treasury is still suffering delays and problems with the quality of the data it receives from its component bodies

1.21 The Treasury is aiming to accelerate the WGA timetable even further and is working towards the delivery of the WGA within 9 months of the year end. To achieve this, it will need to ensure that the components within the WGA are able to provide more accurate and timely information.

[6] Note 7 to the *Whole of Government Accounts 2013-14*

Using the WGA to help inform the Government's financial position and enhance decision making

1.22 The WGA is one part of a wider set of processes that the Treasury uses to manage risks to public finances. In the main, financial risk management in Government centres on the fiscal; budgeting and spending; and estimates frameworks. While these frameworks were designed for different purposes, they are connected and, in many cases, draw on the same data, such as Government departments' monthly reporting of spend to date and forecasts in OSCAR[7].

1.23 The WGA has the potential to help the Treasury manage longer-term risks to the Government's assets and liabilities. These do not feature as prominently in these other frameworks as they tend to focus on Government spending, cash requirements or individual, rather than overall, financial assets and liabilities. The WGA is already being used to help manage these longer terms risks. For example, the Office for Budget Responsibility draws on the WGA, among other sources, in its consideration of the risks to the sustainability of public finances when developing its long-term projections of Government spending and receipts[8]. The Institute of Fiscal Studies has also used WGA recently to support its analysis of the public finances in advance of the upcoming budget[9].

1.24 There are two areas where the 2013-14 WGA reflects developments in the Government's balance sheet. These are the cost of financing the Government's debt; and the reporting of the risks to the Government's finances.

The cost of financing the Government's debt

1.25 Government borrowing financed mainly by the issuance of Government debt instruments, called Gilts, has increased to £1,096.1 billion from £996.2 billion during 2013-14[10], but the costs of financing this debt have only increased to £31.7 billion from £31.0 billion during the year. Therefore, the cost of financing this debt overall has fallen to 2.9 per cent from 3.1 per cent[11]. The reduction in financing costs is due to the refinancing of Gilts at more favourable rates. The Debt Management Office is responsible for managing the issuance of Gilts on behalf of the Treasury, which

[7] OSCAR, the Online System for Central Accounting and Reporting, is the Treasury's financial reporting and management system which captures and monitors central Government spend and is used to prepare the WGA.

[8] Office for Budget Responsibility, *Fiscal Sustainability Report*

[9] http://www.ifs.org.uk/uploads/gb/gb2015/gb2015.pdf

[10] Note 23 of the *Whole of Government Accounts 2013-14*

[11] Note 12 of the *Whole of Government Accounts 2013-14*

includes financing the in-year deficit and refinancing previously issued debt. During the year the Debt Management Office sold £153.4 billion of Gilts[12].

1.26 The level of Government debt will rise again in 2014-15. This reflects the continuing deficit in the public sector finances, which is likely to be in place until the end the middle of the next parliamentary session and the recognition within the WGA of Network Rail's debt of £33 billion for the first time[13]. As the level of Government debt increases, the risks associated with financing it also increase. Therefore, the Treasury should provide greater disclosure on its approach to managing the costs of financing this debt within the WGA for 2014-15.

Risks to the Government's finances

1.27 The WGA shows the most complete picture of the risks to the Government's finances, through the disclosure of contingent liabilities, guarantees and letters of comfort. The overall exposure to such liabilities fell to £167.9 billion from £173.0 billion in 2013-14[14]. The most significant increase in potential liabilities arises in HM Revenue and Customs, which has seen an increase of £14.7 billion in legal and other disputes that can result in claims against Government.

1.28 The WGA also discloses a range of unquantifiable contingent liabilities in note 32.2. These relate to residual interests and exposures to nationalised industries within the Department for Business, Innovation and Skills; regional development funds; health trusts and private sector companies engaged in health care; and risks arising from the transport of nuclear matter.

1.29 As the process of fiscal consolidation continues, the impact of changes in the operations of Government will start to be reflected in assets and liabilities in the WGA. The Treasury should look to build on its analysis of in-year transactions and include further illustrations of the impact of the changing nature of Government on assets and liabilities within the WGA as the next parliamentary session progresses.

Raising the profile of the WGA

1.30 I have previously recommended that the profile of the WGA should be raised within Government and for it to be used more effectively to help decision making. In its report on the 2012-13 WGA, the Committee of Public Accounts also recommended that the Treasury sets out how it will ensure that the Government makes much better use of the WGA to inform decisions, particularly in areas that involve long term

[12] *United Kingdom Debt Management Office Annual Report and Accounts 2013-14* Session 2014-15 HC391 July 2014

[13] Note 19 to the *Network Rail Annual Report and Accounts 2014*

[14] Notes31 and 32 to the *Whole of Government Accounts 2013-14*, excluding restatements caused by the consoldidation of UK Asset Resolution Ltd

liabilities[15]. The WGA is being used increasingly across Government in the following ways:

- The data collected for public corporations is shared with the Office of National Statistics every year to feed into the annual national statistics publication.
- The Department for Communities and Local Government publishes a version of WGA for English Local Government on its website.
- The control total for Public Private Partnerships under the Private Finance 2 regime will be implemented in 2014-15 through WGA.
- WGA is being used to assess the public sector fixed asset base with a view to identifying areas for scrutiny and rationalisation.
- WGA is the only place that reconciles accounting information to the National Accounts adding to the transparency of public finances.

1.31 The Treasury has started to take steps to embed the role of the WGA, and its underlying data, in helping to inform further areas of focus and financial risk management. Now the WGA is in its fifth year of publication, the Treasury has useful trend data which it is able to share. Specifically, the Treasury highlighted that:

- income analysis is being used to identify areas of Government where significant charging takes place, to assess whether charging regimes are operating effectively (or could be revised);
- asset data is being used as part of an assessment of how the Government can incentivise departments to make more efficient use of their land and buildings;
- contingent liabilities in WGA are being used in the Treasury's risk management processes to provide a broader view of spending risks and the consequences on public finances;
- it is working with policy teams to assist them in modelling fiscal risks across Government better (e.g. how do common factors affect overall risk);
- cross-Government staffing and redundancy information, that is only collected through the WGA, is being used by policy teams to inform their advice to ministers; and
- Treasury spending teams are using WGA data to enhance their understanding of departments' activities, which will help to inform allocation decisions in the forthcoming Spending Review and will be a key part of the fiscal consolidation programme in the next Parliament.

[15] Committee of Public Accounts, *Whole of Government Accounts 2011–12*, Thirty-second Report of Session 2013-14, HC 667, December 2013

Improving the usefulness of disclosures within the WGA

1.32 I reported in 2012-13[16] that the lack of detail in parts of the WGA continues to inhibit its usefulness and recommended that data collection is improved so that information in the WGA can be of greater use to its readers[17]. This remains the case.

1.33 For example, Note 8 to the WGA, which shows expenditure on the purchase of goods and services by Government, does not provide further analysis as to how the £189.8 billion has been spent, such as on consultancy and accommodation. The WGA also does not include disclosures showing how public spending is distributed between individual regions or nations across the UK or across the main areas of Government, such as defence, health and education. This lack of granularity within the WGA does not help the reader assess the full impact of the Government's current and future deficit reduction measures.

1.34 Following the introduction of OSCAR to support the preparation of the WGA in 2012-13, the Treasury has captured transactions in a greater level of detail. However, due to inconsistencies in the reporting of underlying data from component bodies, it is yet to be confident enough in the data to disclose more detail on spend within the WGA. Therefore, the Treasury needs to work with component bodies to improve data quality.

Highlighting the extent of fraud and error across the whole of Government

1.35 The Committee of Public Accounts recommended in its reports on the 2011-12 and 2012-13 WGAs that the Treasury should report cross-Government figures within the WGA which would show the impact of its counter-loss activities[18]. Although the WGA includes the financial impact of fraud, error and loss through the consolidation of central Government accounts, it is not yet stated explicitly. Neither does the WGA include losses from local Government and public corporations, which are not required to disclose their losses in the same way. The Treasury has committed to implementing the Committee's recommendation by July 2015[19].

[16] Report of the Comptroller and Audit General on the *Whole of Government Accounts 2012-13* Session 2014-15 HC93, June 2014

[17] Paragraphs 10 to 12 of the C&AG's Report on the Whole of Government Accounts 2012-13 Session 2014-15 HC93, June 2014

[18] Committee of Public Accounts, *Whole of Government Accounts 2011-12*, HC 667, Thirty-second Report of Session 2013–14, 12 December 2013 and *Whole of Government Accounts* 2012-13, HC 678 Twenty-sixth Report of Session 2014–15, 7 Januaru 2015

[19] Treasury Minute, Cm 8819, February 2014

Resolving the issues causing a qualified audit opinion

1.36 I am required to provide my Opinion on the WGA[20]. Since the first WGA, I have qualified my Opinion. However, during 2013-14 and subsequently, the Treasury has taken a number of steps towards introducing measures that may enable me to remove my qualifications at some point over the next four years. **Part 2 of my Report** provides further details. The Treasury has made particular progress in reducing the level of error within the elimination of intra Government transactions, which are a key part of the production of an accurate WGA.

1.37 There is one area, however, where I am likely to continue to disagree with the Treasury. The Treasury designates bodies for inclusion within the WGA based on decisions made by the ONS. However, I am of the view that Treasury should apply accounting standards in determining which bodies Government owns and controls and, hence, which should be included within the WGA. The Treasury's decision means that there are bodies excluded from the WGA which have material assets and liabilities.

[20] Government Resources and Accounts Act 2000

Part Two: Qualifications of the Comptroller and Auditor General's Audit Opinion

2.1 This part of my Report explains why I have qualified my Audit Opinion on the 2013-14 WGA. It also provides details of the progress the Treasury has made in respect of each qualification since my last Report.

2.2 This is the fifth year that I have audited the WGA and I have been able to report to Parliament that these accounts are a "true and fair" presentation of the whole of Government's financial position, although I have always qualified my opinion.

Progress in resolving qualifications

2.3 The Treasury continues to make good progress in moving towards resolving the qualification issues I have raised. Of the six qualifications raised in my Report on the 2012-13 WGA, the Treasury has made progress on five. A detailed description of the actions undertaken by Treasury follows each of my explanations for the basis of individual qualifications further in this Report.

My obligations as auditor

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

Materiality

2.5 In both my Audit Opinion and this report, I refer to the concept of materiality. This part of my report explains this concept and how I apply it in terms of performing my audit.

2.6 The concept of materiality recognises that financial statements are rarely absolutely correct, and that an audit is designed to provide reasonable, rather than absolute, assurance that the financial statements are free from material misstatement.

2.7 I consider a matter to be material if its omission or misstatement would reasonably influence the decisions of users of the financial statements. I consider the primary users of this account to be Parliament but I recognise that the financial statements will be of general interest to others.

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

2.9 The choice of materiality requires professional judgement and, for the financial statements as a whole, I set this at £8 billion for 2013-14 which is approximately 1 per cent of gross expenditure, although I give consideration to other benchmarks in the financial statements when setting materiality. I also define a lower level of materiality, termed performance materiality, which I use to evaluate the potential for unidentified errors within my testing. This is set at £5.8 billion. Materiality is not only a purely quantitative measure, but also includes a qualitative aspect and my opinion is not solely based on total error being under the materiality level.

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

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

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

2.13 The expenditure base for WGA may reduce in future years as public sector spending constraints continue. This will mean that my materiality level will reduce in line with expenditure.

Qualified opinion owing to multiple disagreements and limitation of scope of my audit

2.14 I have qualified my opinion on the 2013-14 WGA because, in a number of significant areas, the WGA does not comply with International Financial Reporting Standards as adapted for the public sector context, and this has a material effect on the figures presented. My qualifications relate to:

- the definition of public bodies that the Treasury has used to determine the boundary of the WGA;

- the inconsistent application of accounting standards; and
- how the Treasury has accounted for income from the sale of 3G and 4G licences.

2.15 I have also limited the scope of my opinion on the 2013-14 WGA because of the following issues which meant I was unable to obtain sufficient and appropriate audit evidence on which to base my opinion in certain areas:

- there was a lack of evidence to support the completeness and accuracy of the value of school's assets included in the financial statements;
- material issues arising within the audit opinions of accounts included in the WGA where auditors have limited the scope of their audit; and
- there was a lack of evidence to support the completeness of the intra-Government adjustments to remove transactions and balances between the bodies included in the WGA.

Qualified audit opinion relating to the WGA boundary

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

2.17 I cannot quantify the impact of this on the WGA with certainty, as I do not have information needed to identify the transactions that would have to be eliminated to provide a consolidated view. However, for illustrative purposes, I have examined the impact of adding the gross assets, liabilities, income and expenditure published in the individual accounts of public sector bodies that the Treasury did not include in the WGA. Although these figures are only illustrative, they demonstrate that the exclusions represent material omissions from the WGA (**Figure 2**).

Financial reporting requirements

2.18 In my previous Reports[21], I have noted that, in determining the boundary for the WGA, the Treasury has adopted the classifications of public bodies used by the Office for National Statistics (ONS). The alternative is applying accounting standards, which require the inclusion of bodies that are subject to Government control and define

[21] Comptroller and Auditor General, Report on the Whole of Government Accounts 2012-13, June 2014

Comptroller and Auditor General, Report on the Whole of Government Accounts 2011-12, July 2013

Comptroller and Auditor General, Report on the Whole of Government Accounts 2010-11, October 2012

Comptroller and Auditor General, Report on the Whole of Government Accounts 2009-10, November 2011 control as 'the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities'[22].

2.19 As a consequence of the Treasury adopting statistical, rather than accounting, standards when it comes to defining 'control', the WGA excludes Network Rail Ltd, which had net assets of £8 billion at 31 March 2014 (£8 billion at 31 March 2013). The Treasury has also not applied its own criteria consistently as there are a number of bodies that fall within both statistical and accounting definitions of Government 'control' but have not been included in the WGA[23] and include:

- bodies that are not controlled by Government, such as Parliament;
- a number of small bodies that have not been consolidated on the basis of size[24]; and
- other bodies that are partly or wholly owned by the Government, such as the Royal Bank of Scotland.

2.20 I consider it appropriate to exclude those bodies that are not controlled by the Government, as this treatment meets with accounting standards. I also consider that it is acceptable to exclude the small bodies as they do not represent a significant exclusion from the WGA. However, by adopting generally accepted accounting standards, I consider that the state owned banks, Network Rail, further education institutes and trust ports, listed in **Figure 2**, where the Government has the ability to control their activities, should be included in the WGA.

Progress since 2013-14

2.21 There has been progress in including bodies listed in Figure 2 within the WGA. Although some of the originating events driving this progress came from others, the Treasury has contributed positively by considering how these decisions impact upon, and could be reflected in, future WGAs. The developments are:

22 *International Accounting Standard 27 – Consolidated and Separate Financial Statements*.

23 Annex 2 to the WGA

24 Annex 3 to the WGA

Figure 2

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

	Revenue	Expenditure	Impact on net expenditure	Assets	Liabilities	Impact on net liability
2012-13 WGA	620.7	(799.4)	(178.7)	1,263.8	(2,893.4)	(1,629.6)
Total values of entities excluded from 2012-13 WGA	**65.6**	**(71.4)**	**(5.8)**	**2,393.8**	**(2,254.6)**	**139.2**
2013-14 WGA	648.5	(797.1)	(148.6)	1,337.3	(3,189.1)	(1,851.8)
Total values of entities excluded from 2013-14 WGA	**62.6**	**(70.8)**	**(8.2)**	**1,098.4**	**(1,020.3)**	**78.1**
2013-14 figures consist of:						
Network Rail Ltd	6.3	(5.3)	1.0	53.9	(45.7)	8.2
State-owned banks[1] (temporary ownership)	55.8	(65.1)	(9.3)	1,027.9	(968.7)	59.2
Further education institutions[2]	-	-		14.9	(5.4)	9.5
Trust Ports[3]	0.4	(0.3)	0.1	1.4	(0.4)	1.0
Other[4]	0.1	(0.1)	-	0.3	(0.1)	0.2

NOTES

1. Lloyds Banking Group plc and Royal Bank of Scotland Group plc. Note that due to the holding in Lloyds Banking Group falling below the consolidation threshold as at 31 March 2014, only the income and expenditure due to the WGA on a group basis is included above.
2. No amounts have been included for income and spending of Further Education Institutions because the majority of their operations are funded through Government grants, which are included in Note 9 to the WGA. Their assets and liabilities have been estimated from data provided by Skills Funding Agency (covering England only) for 2010-11.
3. Trust Ports - figures have been estimated from available accounts for year-ended 31 December 2013.
4. London Councils and other minor bodies.
5. The net assets of some of the entities are included in the WGA as equity investments, for example the state-owned banks are included in the accounts of the Treasury.
6. The bodies have been treated as if they had always been entirely owned by the public sector. In particular, for Royal Bank of Scotland and Lloyds Banking Group, no account has been taken of the residual private sector shareholdings.
7. Not all bodies have a March year-end, e.g. figures for the banks relate to the year ending 31 December 2013.

All figures are in £ billions.

Source: NAO analysis of Note 36 to the WGA and published accounts.

- **Network Rail Ltd**: The ONS had previously classified Network Rail Ltd as a private sector body which led the Treasury to exclude it from the WGA. However, on 17 December 2013, the ONS determined[25] that, following forthcoming changes to national accounts rules[26], Network Rail would be reclassified as being in the public sector from September 2014. The Treasury has considered the impact of this announcement and will consolidate Network Rail into the WGA from 2014-15. The consolidation of Network Rail will significantly increase the infrastructure assets within the WGA and the valuation of the network assets will need to be aligned with the other similar assets that are already reflected in the WGA. Network Rail also contains a significant debt portfolio, which will increase the valuation of Government borrowings by £33 billion.

- **Partly-owned Banks**: During 2013-14, as part of the Government's policy of returning the partly-owned banks to private ownership, the Treasury commenced disposal of its shareholdings in Lloyds Banking Group plc bringing its remaining ownership down to 24.9 per cent of the total available shares on 27 March 2014[27]. The fall in the shareholding below 30 per cent has meant that the Government is no longer defined by the Financial Conduct Authority as being a controlling shareholder in Lloyds Banking Group[28]. For the purposes of the WGA this means that as at the 31 March 2014 there is no requirement to consolidate the assets and liabilities of Lloyds Banking Group. However, as the disposal determining this position occurred at the end of the WGA financial year accounting standards require the consolidation of the income and expenditure of Lloyds Banking Group to that date and this is reflected in Figure 2. The Government announced on 17 December 2014 that it will continue to sell shares in Lloyds Banking Group plc via a Trading Plan[29] and further disposals following the 2013-14 financial year have subsequently reduced the Government's holding to 23 per cent. As at the date of this report there have been no disposals in respect of the Government's ownership of the Royal Bank of Scotland Group plc.

- **Further education institutions**: In my Reports on the WGAs for 2012-13[30],

[25] Office for National Statistics, Written statement to Parliament, ONS decision on the classification of Network Rail, 17 December 2013

[26] Office for National Statistics, Latest developments to National Accounts, 16 May 2014

[27] HM Treasury, March 2014, available at https://www.gov.uk/Government/news/Government-reduces-its-stake-in-lloyds-banking-group-to-below-25

[28] Financial Services Authority, *The Listing Rules*, April 2002, Section 3.13

[29] The Trading Plan will feed shares into the market as part of the normal transactional flow of shares during stock exchange trading http://www.ukfi.co.uk/index.php?URL_link=press-releases&Year=2014

[30] C&AG'sReport within Whole of Government Accounts 2012-13, HC HC93, June 2014, Paragraph 2.21

2011-12[31] and 2010-11[32], I recommended that the Treasury should review its criteria for including bodies within the WGA, taking into account changes in the control Government exerts over English further education institutions following the passage of the Education Act 2011. The Treasury continues to exclude English institutions from the WGA as the ONS determined that these bodies fall outside of the public sector following the 2011 Act[33]. However, under accounting standards, there remains in my view sufficient Government control to warrant their inclusion.

In addition, there are national differences across the United Kingdom. The further education institutions in Northern Ireland and Scotland remain excluded from the WGA, despite these being designated by the ONS as falling within the public sector. Further education institutions in Wales were classified as being outside the public sector in February 2015. However, the Treasury is reviewing the position of these bodies and considering the possibility, subject to any future legislative changes, of including these bodies in future years.

- **Trust Ports**: The Treasury is considering the status of Trust Ports with a view to bringing them within the 2014-15 WGA.

Recommendations for further action

2.22 I continue to recommend that the Treasury should change its criteria for including bodies within the WGA. The Treasury has started to perform work in advance of the consolidation of Network Rail to mitigate the risk of a material impact arising from inconsistent application of accounting policies in relation to the rail infrastructure assets.

2.23 Although the Treasury continues to make good progress in consolidating more bodies into the WGA, my qualification on this matter is likely to remain until all significant Government controlled entities are included in line with accounting standards. This is unlikely to occur until the Government sells a significant proportion of its shareholding in the Royal Bank of Scotland.

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

2.24 I have qualified my opinion because of the impact of the inconsistent application of accounting policies.

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

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

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

The WGA financial reporting framework

2.25 The financial reporting framework that WGA must follow is set out in the Government Financial Reporting Manual, which applies International Financial Reporting Standards (IFRS), as adapted for the public sector context. However, for 2013-14, some of the bodies included in the WGA prepared their accounts based on accounting frameworks that are inconsistent with the requirements of the Financial Reporting Manual[34].

2.26 Under accounting standards, the Treasury should identify the impact of the different frameworks and make appropriate adjustments to the WGA, where material, so that the WGA is prepared on the same basis[35]. The Treasury has undertaken an assessment of these differences and identified one material inconsistency, but has not been able to adjust for this in 2013-14. I do not have the information to fully quantify the effect of all inconsistencies that exist as a result of inconsistent financial reporting frameworks.

2.27 The one quantifiable area of material misstatement is due to differences between the financial reporting frameworks used by local Government and central Government. Local Government guidance requires local authorities to value their infrastructure assets at historic cost, and central Government requires assets to be valued at their depreciated replacement cost in line with the requirements of the Government Financial Reporting Manual[36]. The Treasury estimates that this difference in accounting treatment has resulted in an understatement of asset values of at least £232 billion[37].

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

Progress since 2012-13

2.29 In my Report on the 2012-13 WGA, I recommended that the Treasury should continue to support the Chartered Institute of Public Finance and Accountancy (CIPFA) in considering the basis of valuing assets and take steps to ensure that data collected is considered reliable.

[34] Annex 4 to the WGA

[35] *International Accounting Standard 27 – Consolidated and Separate Financial Statements*

[36] As required under paragraphs 6.2.10 to 6.2.18 of the Government Financial Reporting Manual

[37] Note 13 to the WGA: The best proxy available for depreciated replacement cost is the calculated asset value used by the Office for National Statistics from their perpetual inventory model reflected in the *National Accounts*. The 2014 *National Accounts* estimated the value of the road network at £291.8 billion as at 31 December 2013 implying a likely understatement of at least £232 billion.

2.30 CIPFA plans that the Code of Practice on Local Authority Accounting will be amended to require local authorities to account for their highways infrastructure assets using depreciated replacement cost accounting in their own financial statements from 2016-17. This timeframe will enable local authorities to prepare and collect accurate information in 2015-16, to provide opening balances for their 2016-17 financial statements.

2.31 The Treasury, as part of its data collection exercise for the 2013-14 WGA, asked local authorities to provide valuation data on its highways infrastructure assets. The objectives were both to establish a more accurate level of valuation than that presently noted in the WGA and also to learn lessons on data capture that could be implemented in the future once the Code had been amended. Although the Treasury considered the data received insufficiently robust for inclusion in the WGA, I consider this to have been a worthwhile exercise in identifying the problems of data collection in advance of the implementation of the revised Code. The Treasury has also become actively involved in the Public Infrastructure Steering Group overseeing this transition.

Recommendations for further action

2.32 The Treasury should continue its work with CIPFA to ensure that these planned changes remain on track and that it is able to take prompt action should there be early indications that the data collected by local authorities is not complete, robust, reliable or auditable. Treasury should also put in place plans to obtain depreciated replacement cost values for the remaining non-highways infrastructure assets.

2.33 Should local Government make a successful transition to depreciated replacement cost from 2016-17, which includes providing complete, robust, consistent and auditable data and auditable prior year balances, I may be able to remove my qualification in this area.

Qualification arising from disagreement in the accounting for 3G and 4G licences

2.34 I have qualified my opinion because I consider that the Treasury has not complied with the requirements for accounting for income from the sale of 3G licences in April 2000 and 4G licences in February 2013. The impact of this on the 2013-14 WGA is that income is understated by £1.3 billion, deferred income is understated by £8.9 billion (£10.2 billion in 2012-13) and the General Fund is overstated by £8.9 billion (£10.2 billion in 2012-13).

Financial reporting requirements

2.35 In April 2000, the Government raised some £22.5 billion from the sale of five licences for the electromagnetic spectrum for third generation mobile phone services. Telecommunications companies paid for the licences in full in 2000 and the Consolidated Fund accounted for these proceeds on a cash basis in its 2000-01 account. In February 2013, the Government raised a further £2.4 billion from the sale of the electromagnetic spectrum for fourth generation mobile phone services to five successful bidders. As with the previous auction telecommunications companies paid for the licences in full and the Consolidated Fund accounted for these proceeds on a cash basis in its 2012-13 account.

2.36 The accounting standard for revenue recognition explains that income should be matched to expenditure[38]. In respect of both 3G and 4G licences, the licence holders have the right to access the spectrum for 20 years and, in my view, there is an on-going cost for Government in maintaining the airwaves which is exercised by the Office of Communications (Ofcom) as the Government's communications regulator. Therefore, in my view a more appropriate accounting treatment would be to recognise this income over the licence period rather than treat it all as income in the first year. The Treasury does not agree with this view and, as disclosed in Note 1.22.2 to the WGA, believes that there are no additional performance obligations within the 3G and 4G licences. Therefore, the Treasury has not adjusted the WGA for these transactions and I have qualified my opinion accordingly.

2.37 The balance of deferred income in relation to the 3G and 4G licences at 31 March 2014 was some £8.9 billion and, although the balance continues to fall it remains material. This remaining balance will decrease over time and have a decreasing impact on the financial statements.

Progress since 2012-13

2.38 The Treasury's position on 3G and 4G licences is set out in the WGA accounting policies[39]. The Treasury's view is that it does not have any ongoing role in relation to the licences and has therefore recognised all of the revenue from the sales at the point of completion. The Treasury's view on these transactions has not changed during 2013-14, it remains of the view there are insufficient grounds to adjust the WGA[40].

2.39 In the 2013 Spending Review, the Government announced its intention to release at least 500 MHz of additional electromagnetic spectrum. Two bands of spectrum have been identified for release, a total of 160MHz of bandwidth. The spectrum will be transferred from the Ministry of Defence to Ofcom during 2014-15 and the sale is expected to complete in 2015-16.

[38] International Accounting Standard 18 – Revenue

[39] See note 1.22.2 of the accounts.

[40] Although not pertinent to my consideration of the treatment under accounting standards, in February 2014[40] , the Office for National Statistics amended their consideration of the treatment of spectrum licence sales in the United Kingdom National Accounts from treating spectrum licence sales as sales of assets to one where the income is recognised over the life of the licence

Recommendations for further action

2.40 The Treasury should, in my view, adjust the WGA for the 3G and 4G transactions in line with accounting standards and treat any future transactions in line with this framework.

Qualification arising from limitation of audit scope due to lack of evidence supporting the completeness and valuation of schools' assets included in the financial statements

2.41 I have qualified my opinion in respect to local authority maintained school assets because not all school assets are included in the WGA.

2.42 All local authority maintained schools are classified by the ONS as public sector and hence fall within the Treasury's definition for inclusion within the WGA. Taking an approach based on financial reporting standards[41], I consider that these schools should be included within the WGA, as local authorities and the Secretary of State for Education have the ability to exert control over them.

2.43 However, such schools have only been included in the WGA if their financial activities were included in the financial statements of individual local authorities. A working group, led by CIPFA, reported that not all schools were included within local authority financial statements[42].

2.44 In considering the impact of this treatment of the local authority maintained schools' sector, I have concluded that I have insufficient evidence to support the completeness and valuation of these schools' assets within the WGA. Although I have sufficient evidence over the treatment of community schools, which are accounted for within local authorities' accounts, I have been presented with no evidence to allow me to conclude that the assets of foundation, voluntary aided and voluntary controlled schools are all included within the WGA.

2.45 Based on the estimates I do have, the omissions are material to the WGA. **Figure 3** shows that up to £22 billion (2012-13: £23 billion) of assets from voluntary aided and foundation schools and £8 billion (2012-13 £8 billion) of assets from voluntary controlled schools have been omitted from the accounts. The reduction in the value of error is primarily due to a reduced number of these schools caused by their transition to Academies.

[41] *International Accounting Standard 27 – Consolidated and Separate Financial Statements*

[42] This is the correct treatment for the local authority accounts and there is no suggestion that the underlying opinions on any of these accounts are compromised.

Progress since 2012-13

2.46 The Treasury has been working with CIPFA to align the local Government accounting treatment for schools in England and Wales. The working group, in December 2013, concluded that that the balance of control rests with local authorities for community schools, voluntary controlled, voluntary aided and foundation schools, and that these schools should be included in the financial statements of local authorities. By including these schools in the financial statements of local authorities, they will be consolidated into the WGA. Following the findings of the working group the Treasury has set up a Local Authority User Group and has engaged with a number of local authorities to perform work in advance as part of the preparation for the collation of data.

2.47 CIPFA issued a consultation note[43] seeking views from stakeholders on amendments to the 2014-15 Code of Practice and, following this consultation, have amended the Code[44] to reflect the conclusion of the working group. This will mean that the currently omitted schools would be brought into the 2014-15 WGA. However, the amendments to the Code would only apply to England and Wales but not apply to those schools in Northern Ireland which are currently omitted. Schools in Scotland are included in the WGA.

Recommendations for further action

2.48 The Treasury should ensure that the data collected in the first year of implementation is sufficiently robust to be considered complete and true and fair in respect of schools brought into local authorities' accounts through implementation of the Code. In addition, the Treasury should include all schools in Northern Ireland within the WGA.

2.49 Once sufficiently robust data is available in support of the completeness and valuation of voluntary aided, voluntary controlled and foundation schools, I may be able to remove my qualification in this area.

[43]CIPFA/LASAAC, The 2014/15 code of practice on local authority accounting in the United kingdom, Invitation to comment.

[44] CIPFA, Technical Accounting Alert 3, Accounting for Local Authority Maintained Schools (England and Wales) 2014-15 Financial Statements

Figure 3

Estimated net book value of local authority maintained schools, and whether these are included or excluded from the WGA

	Voluntary aided and foundation schools (not included in WGA)		Voluntary controlled schools (may or may not be included in WGA)	
	Number	**Amount (£bn)**	**Number**	**Amount (£bn)**
Primary Schools	4,082	12.3	2,319	6,9
Secondary Schools	639	9.5	50	0.8
Total	**4,721**	**21.8**	**2,369**	**7.7**

NOTES

1. Estimates as at January 2014 based on typical carrying value of £3 million for primary schools and £15 million for secondary schools as estimated by CIPFA.
2. These estimates may be overstated as some schools may lease their assets rather than own them. There is no information available to take account of this.
3. FRAB (108) 11: Consideration of the code of practice on Local Authority Accounting 2011/12 and 2012/13 http://www.hm-treasury.gov.uk/d/frab108_11.pdf and Tables 7d and 7e of Schools, Pupils and their Characteristics.
4. https://www.gov.uk/Government/publications/schools-pupils-and-their-characteristics-january-2013

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

2.50 Where the external auditors of bodies in the WGA qualify their opinions on the statutory financial statements, I am required to consider the impact of these 'true and fair' qualifications on my opinion on the WGA. In 2013-14, external auditors qualified their opinions of some 4 accounts (10 accounts in 2012-13).

2.51 The most significant of these qualifications for 2013-14 relate to the Department for Education and the Ministry of Defence. Given their significance to the WGA, I have also qualified my opinion on the WGA.

2.52 Further details can be found in my audit opinions and within the annual accounts of the Department for Education[45] and the Ministry of Defence[46] .

Progress since 2012-13

2.53 In my Report on the 2012-13 WGA, I also qualified my opinion on the WGA due to the material impact of the qualifications of the Ministry of Defence and the Department for Education's financial statements.

[45] Department for Education Annual Report and Accounts 2013-14, Session 2014-15, HC 745.

[46] Ministry of Defence Annual Report and Accounts 2013-14, Session 2014-15, HC 764

2.54 In 2013-14, the Ministry of Defence has concluded that, in order to complete its review and conclude on whether the contracts it currently holds meet the criteria of a lease under IAS 17, Leases, further management information and supplier engagement would be required. As disclosed in its Annual Report and Accounts, the Ministry of Defence has, in agreement with HM Treasury, decided not to obtain more detailed information on the grounds that obtaining this would not represent value for money. Consequently, no conclusion can be drawn as to whether the existing contracts held represent leases and the financial impact of the omission of potential assets and liabilities cannot be determined with sufficient accuracy.

2.55 The gap in assurance in respect of the Department for Education providing insufficient evidence to recognise academies' land and buildings within its accounts has widened in comparison to 2012-13. In 2013-14, the number of academies increased from 2,823 to 3,905 and the Department has been unable to provide appropriate evidence to establish ownership of these assets. As a result the scope of this issue has grown and is likely to continue to be a source of continued qualification within the WGA.

Recommendations for further action

Ministry of Defence

2.56 The Ministry of Defence's decision not to obtain detailed information to comply with IAS 17, Leases will have an ongoing impact on the audit opinion I am able to provide on the financial statements for the foreseeable future. The Department is now considering further work in respect of the application of IAS 17, Leases to new contracts; although no formal decision has yet been taken on this matter. The Treasury should work with the Ministry of Defence to monitor progress in this area, with the aim of eliminating this qualification as its current contracts are replaced.

Department for Education

2.57 The Treasury should continue to support the Department for Education in respect of the accuracy of academies' land and buildings data. In addition, the Treasury should work with the Department for Education to seek to improve the timeliness of information that is submitted to support the WGA as this was a source of delay in the production of the 2013-14 accounts and is likely to be so in future years. This issue is linked to the need for the Department for Education to work with the Treasury to agree a more sustainable approach to consolidating the financial results of academies, that I refer to in my opinion and report on the Department's 2013-14 financial statements.

Qualification arising from the limitation of audit scope due to a lack of evidence supporting the completeness of the elimination of intra-Government transactions and balances

2.58 I have limited the scope of my opinion because of the lack of evidence supporting the completeness and accuracy of the elimination of intra-Government transactions and balances, between bodies included in the WGA.

Financial reporting requirements

2.59 The WGA is a consolidated account which is prepared by bringing together the financial activities of over 5,400 Government controlled entities. Transactions and balances between these bodies are removed so that income, expenditure, assets and liabilities are not overstated within the group financial statements, as required by accounting standards. To present a true and fair picture of the financial position and financial results of Government, it is important that the removal of these intra-Government transactions and balances is complete and accurate.

2.60 The Treasury collects information from each of the bodies in the WGA on all intra-Government transactions and with details of the relevant counter-parties. The Treasury uses this data to match balances and transaction streams and remove them from the WGA. The Treasury has made a significant improvement in reducing the level of uncertainty arising from the removal of these transactions in the WGA. Despite this, there remains a significant residual uncertainty over some of the figures in the financial statements because the removal of these transactions and balances is potentially incomplete and inaccurate. This uncertainty arises where:

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

2.61 Using the available evidence, I have estimated the level of uncertainty as being £7.3 billion (£9.1 billion in 2012-13) in gross income and expenditure and up to £2.2 billion (£3.7 billion in 2012-13) in gross assets and liabilities (**Figure 4**). The estimated errors reside mainly within individual primary statements.

2.62 It is the significance of the estimated level of uncertainty within the statements, and the potential gross overstatement of income, expenditure, assets and liabilities which has led me to qualify my opinion rather than the potential impact on the annual deficit or net liabilities. Whilst the estimate has now fallen below the £8bn materiality threshold which I apply when conducting my audit, I have concluded that there is insufficient evidence to support the removal of this aspect of my qualification this year.

Figure 4

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

	Statement of Revenue & Expenditure	Statement of Financial Position
Entities declaring different intra-Government transactions or balances	3.6	1.3
Only one entity declares an intra-Government transaction or balance	1.9	0.8
Subtotal of errors that can be linked to specific entities	**5.5**	**2.1**
Neither entity within an expected relationship declares an intra-Government transaction or balance	1.8	0.1
Impact on the financial statements (potential overstatement)	**7.3**	**2.2**

NOTES

All figures in £ billions

Source: NAO analysis of WGA 2013-14

Progress since 2012-13

2.63 In my Report on the 2012-13 WGA, I recommended that the Treasury should undertake further work to reduce the uncertainties in the elimination of intra-Government transactions and balances and I also recommended that this work should be concentrated on the area of local Government.

2.64 The Treasury has undertaken a number of actions which have contributed to the reduction of the error in the 2013-14 WGA. The Treasury has sought to maximise the benefits of the introduction of a change in IT systems by amending its data collection processes with the aim of improving the accuracy of the initial data received in the preparation of the financial statements. It also seconded staff from local Government and with sector expertise to help identify errors within the local Government data returns; and reduced the threshold at which it would investigate potential imbalances. The Treasury also used other available data from central Government sources to review the data it received.

2.65 It is encouraging that the estimated error in the eliminations data continues to show a positive downward trend. Overall, I welcome the substantial progress that the Treasury has made in this area (**Figure 5**).

Figure 5

Level of potential overstatement in the WGA

	2010-11	2011-12	2012-13	2013-14
Statement of Revenue and Expenditure	22.6	16.0	9.1	7.3
Statement of Financial Position	10.4	5.1	3.7	2.2

All figures in £ billions

Source: NAO analysis of WGA 2013-14

Recommendations for further action

2.66 The Treasury has made significant progress in reducing the elimination error over the last three years. For 2014-15, the Treasury, and the component bodies submitting data, will be operating a fully established IT system which should help produce more accurate data leading to further reduced levels of error. However, with such an extensive body of components preparing information, a significant level of error in the initial data preparation is almost inevitable and it is possible that the level of error may not be able to be reduced much further under the current method of collation and preparation.

2.67 I recommend that Treasury continues to review the structure and process of data collection in order to determine areas of potential weakness and also to consider alternative methods of proving counter party evidence in those areas which are either onerous to prove or are prone to error. If the Treasury can prove with sufficient certainty that it has reduced the level of error below my materiality threshold in the preparation of the 2014-15 WGA, then I will be able to remove my qualification.

Other issues on which I have not qualified my opinion

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

- I have included an emphasis of matter paragraph in my audit opinion for one account that is significant to the WGA. This relates to the uncertainties in estimating costs of the liabilities of the Nuclear Decommissioning Authority. This value has been calculated based on reasonable assumptions, but could change with future events.

- The external auditor of some 17 accounts (18 in 2012-13) included in the WGA qualified their audit opinions due to the existence of material irregular transactions; that is not using resources in accordance with Parliamentary intentions. Of these, two are of significance to the WGA and cover error and fraud in benefit payments and tax credit payments. These irregularities have led me to qualify my regularity opinion on the financial statements of the Department for Work and Pensions[47] and HM Revenue and Customs[48]. The scope of my audit of the WGA, which is set out in the Government Resources and Accounts Act 2000, does not require me to provide an opinion on regularity, as such irregular transactions do not lead to a qualification of my audit opinion on the WGA.

Amyas C E Morse
Comptroller and Auditor General
23 March 2015

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

[47] Department for Work and Pensions Annual Report and Accounts 2013-14, Session 2014-15, HC13, June 2014

[48] HM Revenue and Customs Annual Report and Accounts 2013-14, Session 2013-14, HC19, July 2014