



# PUBLIC EXPENDITURE: A NEW PRESENTATION

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# Public Expenditure: A New Presentation

## FOREWORD

This paper deals with certain aspects of the relationship between the Executive and Parliament in the field of public expenditure. It sets out a number of proposals for changes in present arrangements which the Government are submitting to the **Select Committee on Procedure** for their consideration. In view of the importance of this subject, the Government are issuing this Green Paper so that their proposals may form the basis of wider public discussion.

April 1969.

## CONTENTS

	<i>Paragraphs</i>	<i>Page</i>
I. INTRODUCTION ... ..	1-6	3
II. AIMS AND REQUIREMENTS OF POLICY		
The nature of public expenditure decisions ...	7-13	4
The time-scale of public expenditure decisions ...	14-18	5
The resource costs of public expenditure ...	19-25	6
III. A PROPOSED NEW PRESENTATION OF PUBLIC EXPENDITURE ... ..	26-44	7
IV. PARLIAMENT AND THE PROPOSED PRESENTATION ...	45-52	11

## ILLUSTRATIVE TABLES

Table 1. Analysis of public sector expenditure by function up to year 3 ... ..	13
Table 2. Public sector receipts and expenditure up to year 3: Summary analysis ... ..	13
Table 3. Public sector receipts and expenditure up to year 3: Analysis by function and type of transaction ... ..	14
Table 4. Public sector expenditure up to year 3: Analysis by function and spending authority ... ..	14
Table 5. Public sector expenditure up to year 3: Analysis by economic category ... ..	15
Table 6. Provisional projections of public sector expenditure by function: years 4 and 5 ... ..	16

## APPENDICES

I. Developments before and since the Plowden Report on Control of Public Expenditure ... ..	17
II. Some technical aspects of measuring public expenditure in relation to the use of resources ... ..	20

## I. INTRODUCTION

1. The adaptation of old forms to new purposes is a well-established feature of British constitutional practice. An example of such evolution over the past thirty years has been the change in the ways in which the House of Commons has discussed and considered proposals for public expenditure.

2. In the 1965-66 Session of Parliament, evidence was submitted to the House of Commons Select Committee on Procedure that, while in 1937-38 more than nine-tenths of debates on Estimates and Supplementaries were tied closely to debates upon departmental stewardship, by 1963-64 less than half such debates were handled in this way, and over half were related to "debates which do not even pretend to base themselves on an estimate".<sup>(1)</sup> Summing up the position, the Select Committee observed: "the forms of procedure by which the House considers and votes Supply have, in the course of time, come to be mainly used, not for truly financial purposes, but as a means of controlling the administration . . .";<sup>(2)</sup> but it warned ". . . the basis of financial forms must be retained; the House must not give up its right to grant or refuse to grant the money required by the Executive". In this way the House evolved its practices to serve new purposes more appropriate to the changing and growing role of public expenditure, while not losing sight of the fact that voting Supply remains an act of major constitutional importance, in which is embodied the relation of the Legislature to the Executive.

3. Side by side with these changes in parliamentary practice have gone changes in the procedures by which the Executive reaches decisions on public expenditure. The need for change was apparent over a decade ago when the Select Committee on Estimates, in the 1957-58 Session, produced a valuable report on Treasury Control of Expenditure.<sup>(3)</sup> This led directly to the setting up of the Plowden Committee, whose report, published in 1961,<sup>(4)</sup> has formed the basis of all subsequent developments. A fuller account is given in Appendix I.

4. The fundamental recommendation of the Plowden Committee was:

"That regular surveys should be made of public expenditure as a whole, over a period of years ahead, and in relation to prospective resources."<sup>(5)</sup>

This has become accepted practice under successive administrations and provides the framework for all major expenditure decisions. Although this recommendation appears straightforward and necessary, it is not in practice easy to bring together in one annual Survey consistent estimates for a number of years ahead for the whole of public expenditure.<sup>(6)</sup> It is also difficult to

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<sup>(1)</sup> Memorandum by Mr. Anthony Barker (then Lecturer in Politics in the University of Bristol) submitted to the 1965-66 Committee, page 3.

<sup>(2)</sup> Report of the Select Committee on Procedure, Session 1965-66, paragraph 3. H.C.122.

<sup>(3)</sup> The Sixth Report of the Select Committee on the Estimates, Session 1957-58. H.C.254.

<sup>(4)</sup> "The Control of Public Expenditure." Cmnd. 1432.

<sup>(5)</sup> Paragraph 12 of Cmnd. 1432.

<sup>(6)</sup> Public expenditure has been variously defined. For the purposes of this paper it is defined as the current and capital expenditure of the central Government and local authorities together with the capital expenditure and debt interest of the nationalised industries and other public corporations.

express those expenditure estimates "in relation to prospective resources". White Papers in recent years<sup>(7)</sup> have given figures for certain years ahead derived from these annual public expenditure Surveys; and Cmnd. 2915 gave some indication of developments in techniques for providing figures which will properly represent the expected outlays of the whole public sector and not just of the central Government alone.

5. But these White Papers have been occasional rather than regular or systematic, and Parliament's own consideration of public expenditure has continued to be related to the Supply Estimates for the forthcoming year. The Government have recently reviewed their own methods of reaching public expenditure decisions, and have come to the conclusion that present techniques are sufficiently firmly established for a new and important step forward to be made. The Government now propose that there should be published towards the end of each calendar year a White Paper, which will present to Parliament the results of the Government's consideration of the prospect for public expenditure. This White Paper would set out the figures for the whole public sector for a number of years, and in a new form which would help to show the likely claims on resources entailed by those public outlays. The House of Commons could then, if it so wished, supplement its present financial procedures by additional discussions on public expenditure based on this new and more comprehensive presentation.

6. The rest of this paper examines the basis for the new presentation and describes the changes which the Government propose should be introduced. Appendix II explains the technical aspects in greater detail.

## II. AIMS AND REQUIREMENTS OF POLICY

### **The nature of public expenditure decisions**

7. Decisions about public expenditure cannot be taken in isolation but must be related both to the whole range of the Government's objectives, and to the other instruments of policy available to the Government for achieving them.

8. The manifold objectives of government interlock. Some are concerned with general economic management. These include a high rate of economic growth, the maintenance of a sound balance of payments, full employment, stability of prices and a more equitable distribution of income and wealth. Other objectives are concerned with meeting the needs of the community for particular services—education, health, defence and so on.

9. To achieve these objectives there are many instruments which can be used. Among them are fiscal policy, monetary policy, and prices and incomes policy as well as the management of public expenditure programmes, separately and in total.

10. Any decision on public expenditure will affect more than one of the objectives. For instance, a decision to increase the number of students in universities may be taken from a variety of motives, of which one will be

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<sup>(7)</sup> Cmnd. 2235 in 1963, Cmnd. 2915 in 1966, Cmnd. 3515 in 1968 and Cmnd. 3936 in 1969.

to extend higher education—a social objective. But the same decision, since it will involve expenditure on new university buildings and on additional staff, will increase the pressure on resources; and because these students will join the labour force later, it will in the short run reduce the total productive resources available. Another instance is expenditure on defence, which will normally affect the balance of payments and have an impact on the balance of the internal economy as well.

11. Because public expenditure decisions affect several objectives, there are two things which the Government need to know in order to make rational decisions.

12. First is the order of priority among the objectives. This point can again be illustrated in terms of increasing the size of the universities. If the balance of the economy is to be preserved, then, other things being equal, the cost in resources (both the resources absorbed by the expenditure and those represented by the increasing number of students who will join the labour force later than they would otherwise have done) will have to be offset either by cutting some other public programmes or by reducing the private sector's use of resources to the appropriate extent through higher taxation. The effects of the offsetting action have to be weighed against the long-term social and economic benefits of expanding the universities. This is a political judgment.

13. Secondly, the Government need to know the effect of a public expenditure decision, both on the immediate objective and on all other objectives as well. An important step forward in evaluating the costs of public expenditure policies can be made by assessing what they imply in use of currently produced resources; this would give a broad indication of what would have to be currently forgone in the rest of the economy, public and private.<sup>(8)</sup> The Government's proposals in this Green Paper are directed to achieving an advance on these lines.

### **The time-scale of public expenditure decisions**

14. Many of the activities of the public sector require planning a long time in advance. To take an example from the investment programmes of nationalised industries, the introduction of North Sea gas requires a new type of transmission system and extensions to the existing distribution and storage system on some scale: conversion of consumers' appliances, domestic, industrial and other, has to be carried out town by town and house by house: each type of appliance being converted requires a special kit. These

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<sup>(8)</sup> Some kinds of public expenditure have the effect of simultaneously adding to, or subtracting from, the total of resources available and, in principle, this effect should be allowed for in calculating the current resource cost of a particular programme. An example of subtraction is increased university education which currently withdraws students from the labour force; an example of addition to resources is expenditure in development areas which uses part of the higher level of unemployed labour in those areas. The presentation of public expenditure described later in this Green Paper does not attempt to cover this complication. Nor does it take account of benefits which stem from the different items of public expenditure. In some cases these benefits can be expressed, partially at least, in economic terms, or as a return on capital. In others (e.g., social security) it is extremely difficult and perhaps impossible to derive a means of expressing benefits. But in general even expenditure with a high economic return will generate little or no increased resources in the period in which the outlay has to take place. The cost in resources of the outlays which the new presentation tries to display is therefore a good indicator of the cost in terms of what has to be immediately forgone either elsewhere in the public sector or in the private sector.

operations require careful advance planning including the training of fitters to do the conversions, the negotiation of wayleaves for pipelines, the procurement of the necessary equipment and material, including conversion kits, and other essential preliminary work. The original policy decision ramifies in this way and establishes the pattern of expenditure over a period. If at any stage beyond the earliest a plan like this is subject to a major readjustment, there is waste or increased cost.

15. This is true both for increases and decreases in a programme, for a hurried expansion can mean cost through inadequate planning and preparation. Studying the possible flexibility of the different parts of each programme means examining exactly when final decisions to commit financial or other resources need to be taken, and the likely cost in each case of revising such decisions, upwards or downwards, at later dates.

16. Major readjustments cannot in practice be spread evenly through public expenditure programmes. At any particular time only a small part of the total represents the earliest stages of a planned series of operations. The more advanced the stage reached, the more painful, because the more costly, any change becomes. Contractual and other commitments also limit the extent to which public expenditure plans can be changed quickly. For this reason changes have tended to be concentrated heavily on that part—usually a small part—of capital programmes which, though much of it may have been planned, has not been started.

17. One of the purposes of the forward planning system is to provide Departments and other agencies with a framework within which they can plan expenditure, as far ahead as is appropriate, aimed at securing the objectives for which they are responsible—education, road building, fostering technological development, defence, etc.

18. Plans laid on this basis can never be entirely precise. New policies or extensions of old ones come forward; new information causes estimates to be revised; rapidly advancing technology brings projects into the field which cannot be foreseen far ahead; some expenditures are in the hands of public authorities with their own degrees of autonomy from the central Government, such as local authorities; epidemics occur; expenditure under some policies partly depends on external factors, such as movements in world food prices. To help provide for such eventualities an adequate contingency margin must be held in reserve.

### **The resource costs of public expenditure**

19. Since 1961 the Government have conducted for their own management purposes public expenditure Surveys covering the plans for five years ahead. The presentations in these Surveys have used the same definitions as the National Income Accounts, and have expressed the expenditure plans at constant prices. This has laid an appropriate foundation for further development of the presentation in order to provide an increasingly accurate picture of use of resources by the public sector. Two main problems have been met, and much of the proposed new form of presentation which will be described in Section III below is designed to deal with them. The first may be called the “gross and net” problem—how far receipts should be shown for their offsetting effects against expenditure; the second is how far account can be taken of the effects of expenditure on savings and liquidity.

(a) *The "gross and net" problem*

20. The question here is how far gross outlays should have any associated receipts deducted from them. In the National Income Accounts receipts which are in the nature of charges are so deducted. For instance, public expenditure on school meals is shown as the expenditure on the meals less the meal charges which are levied.

21. But even expenditures net of charges may be misleading. For instance, when investment grants replaced investment allowances, the public expenditure figures were suddenly swollen, although financial transactions between the Government and private industry were relatively little changed.

22. In a rather similar way, some part of most Government grants—for instance, family allowances—comes back to the Government in tax.<sup>(9)</sup> If the grants are shown without the tax offset, the use of resources will be incorrectly measured, by comparison with those expenditures which have no such tax offsets, or which have a different one. Similar considerations apply to receipts associated with particular types of expenditure, e.g., social security contributions. So it is important to show the receipts side of the account along with the gross expenditure.

(b) *Savings and liquidity*

23. There is another way in which the gross amount of some public expenditures may overstate use of resources by comparison with that of other public expenditures, even after all tax offsets and charges have been deducted. For example, part of a family allowance, or other grant to a person, may not be spent at once but saved; or where a grant is made to a company, the whole of it may well not be spent by the company in the year in which it is paid. Similarly, when a public body buys some existing assets such as company securities or land, the immediate effect is to put money into the pockets of the former owners of the assets; such an increase in the liquidity of the private sector is unlikely to create an equivalent additional demand at once, although it may have a considerable effect in due course.

24. Other problems connected with obtaining an accurate measure of use of resources by the public sector are described in Appendix II.

25. The proposals presented in the next Section of this paper are designed to take account of the points which have been made in the preceding paragraphs.

### III. A PROPOSED NEW PRESENTATION OF PUBLIC EXPENDITURE

26. The object of the new form of presentation is to bring out the main implications for resources of public expenditure plans over the period ahead.

27. The *first change* will be to show regularly every year figures for the year preceding publication, the year of publication (year 1) and each of the four following years (years 2 to 5). The current and the two following years (years 1 to 3) will be the period for which the Government will

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<sup>(9)</sup> See Appendix II, paragraph 18.



have taken decisions. Experience has shown that year 3 is the point of time at which, taking public expenditure as a whole, there is real scope for substantial changes up or down without too great cost through disruption. Year 3, therefore, is the one on which the Government focus attention in the process of re-examining and confirming or modifying their earlier decisions, and in rolling plans forward to a further year. But since, by the time Parliament each year receives and discusses the proposed new White Paper, year 1 will be largely over and the preparation of the Estimates for year 3 will be only about a year ahead, the degree of commitment for the "focus" year will already be high.

28. It is also intended to include public expenditure figures for two further years. But the status of the figures for these years (4 and 5) will be different from that of the figures for the first three years, since the Government will not have decided the scale and composition of programmes beyond the three-year period. The figures for years 4 and 5 will represent projections of the cost of present policies, not decisions. This will be made clear in the presentation, which will differentiate between the figures for years 1 to 3 and those for years 4 and 5, which will be shown separately. As time passes and years 4 and 5 become in turn the "focus" year, fresh decisions will have to be made which will affect the components of the totals and possibly the totals themselves.

29. The *second change* concerns the capital expenditure of the nationalised industries. It is important that the full range of public expenditure should be considered at the same time and in the same context. For this reason, it is intended that the capital expenditure of the nationalised industries should be brought into the annual public expenditure review. Although the bulk of this investment is determined by commercial considerations, there are generally decisions to be taken at the margin, and it is right that these should be taken in the context of public expenditure as a whole.

30. The *third change* will be to present, along with expenditure, projections of all receipts from taxation, contributions and charges and of all other receipts accruing to the public sector, including the estimated gross trading surpluses of the nationalised industries and other public enterprises.<sup>(10)</sup> The main purpose is to overcome the problem that public expenditure figures may always be misleading so long as the revenue side is not presented at the same time (see paragraphs 20-22). For example, at the time when investment grants were introduced, the new presentation would have included not only the increase in expenditure but also the corresponding increase in revenue resulting from the withdrawal of investment allowances, and so would have shown that the balance was little affected. Also any tax flow-backs from expenditure on, say, social security benefits, will be contained in the revenue figures. So will receipts associated with particular types of expenditure, such as national insurance contributions. In this way the net effect of changes on both sides of the account will be displayed.

31. But the figures on the receipts side are not predictions as for the most part the individual expenditure figures are. They are constructed in

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<sup>(10)</sup> These projected receipts will be on the same constant price basis as the figures for expenditures.

various ways. It is assumed that national insurance contributions will rise so as to match, together with the Exchequer supplement, the assumed growth of expenditure on benefits. Similarly, projections of income from local rates are related to the expenditures of the local authorities, and assume the continuation of the existing system of grants to those authorities.

32. The projections of central Government taxation will not be intended to reflect a view about the future course of Government policy. Changes in central Government taxation are one of the main instruments for the short-term regulation of the economy; there must therefore be scope for short-term flexibility and for this reason the Government cannot commit themselves in advance. The yield of central Government taxation must be calculated by assuming that present tax rates and allowances will continue unchanged; it will also incorporate the direct effects on revenue of expenditure decisions.

33. The resulting figures will give a broad measure of the buoyancy of the revenue. Within the total yield there will, of course, on this method of projection be changes in relativities, the yield of progressive taxes, such as income tax, growing faster than that of specific taxes such as, for example, the tobacco duty. These changes in relativities are solely the result of the method of projection; they do not represent a view about what would be the most desirable, or likely, pattern of future taxation.

34. The *fourth change* will be to distinguish three categories of transactions corresponding very broadly to three markedly different degrees of use of resources:

(A) *Direct use of resources*: the expenditure side will show net transfer payments abroad and current and capital expenditure on goods and services (including the fixed investment of the nationalised industries but excluding net purchases of land, existing buildings and financial assets). On the receipts side will be set charges for goods and services and receipts from sales not on operating account. This will enable a balance to be struck corresponding to the net direct use of resources by the public sector in the purchase of goods and services (including overseas transactions).

(B) *Transfers*: the expenditure side will show transfer payments.<sup>(11)</sup> On the receipts side there will be taxes, central and local, direct and indirect (but not taxes on capital, which appear in Section C below), contributions and other receipts. (The tax receipts will include the flow-back of tax from the expenditure side, in particular from transfer payments, as explained in paragraph 22.) The outlays in this category, even after deducting the tax flow-backs which they generate, will be larger than the private expenditure which they promote because part of the receipts will go into savings rather than to the direct purchase of goods and services. The savings element, which cannot be brought directly into a system of public sector accounts, but which is included in estimates of savings in the National Income Accounts, will vary greatly from one type of transaction to another.

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<sup>(11)</sup> Transfer payments are payments made by the public sector to the private sector which are not payments for the purchase of goods, services or assets: examples are social security benefits, subsidies and debt interest. Transfer payments abroad are, however, treated as direct claims on resources.

(C) *Assets* : the expenditure side will show net purchases of land, existing buildings and financial assets, and the receipts side the inflow from taxes on capital and certain other similar receipts.

35. As between the balance of outlays and receipts in the three categories, the demand implications, particularly in the short-term, are relatively greatest for category (A); rather less for (B), because of the element of savings; and usually least for (C), where the effect on demand is primarily the result of increased liquidity and usually works through relatively slowly into the economy.

36. The *fifth change* will be to include in the total of outlays an allowance (the "relative price effect") for the likely change in the real cost of public sector purchases (particularly labour). This is examined in greater detail in Appendix II.

### The new tables

37. All these changes are embodied in Tables 2 and 3 of this paper.

38. Table 2 is a summary table covering years 1 to 3. Lines 1 to 11 show the division of transactions between expenditure and receipts and also into the three categories, direct use of resources (A), transfers (B) and transactions in assets (C). Line 12 shows aggregate public expenditure as hitherto.

39. Alongside this total the new presentation will embody two other means of summarising the position. The first is the difference between total outlays, as in paragraph 38, and total receipts (line 13 in Table 2). This gives the expected increase in public expenditure related to the yield of the tax system at existing rates of central Government taxation.

40. The second new summary figure (line 14 in Table 2) differs from this by omitting from the expenditure total the element attributable to net purchases of assets and from the receipts total the element attributable to taxes on capital and miscellaneous borrowing. This gives a balance of expenditure on resources and transfers over the corresponding receipts. To help judge the relationship between the rate of growth of these figures of the resource requirements of public expenditure and the total of national resources, an assessment will be given of the prospects for the growth of national production in the period ahead, drawn from studies such as the recent Economic Assessment to 1972 published as the Green Paper entitled "The Task Ahead". This assessment, like that given in the Green Paper, will be in terms of a range of possibilities.

41. These summary figures present only part of the situation with which economic policy must be concerned. Thus, if, for example, the balance of resources and transfers (line 14 in Table 2) were to fall, this would suggest that the pressure of public sector demand on resources would be becoming relatively easier. But it could not be predicted from this that it would be right to increase public sector demand, nor that tax rates were likely to fall; there are other claimants on the total of resources, including the consumption and investment needs of the private sector and the needs of the balance of payments. Changes in these other demands on resources might well have to be allowed for, such as an improvement in the balance of payments

or a rapid increase in private investment. The acceptable level of public expenditure can only be determined as part of the assessment of all these claims considered together.

42. Table 3 gives the same information as in Table 2 classified by functional objective.

43. In addition the presentation will include an analysis of the expenditure figures by function (as in Table 1) and by function and by spending authorities—that is, by central Government (distinguishing Vote-borne expenditure from expenditure otherwise financed, such as expenditure from the National Insurance Funds), by local authorities and by public corporations (as in Table 4); and by economic category (as in Table 5).

44. The projections of expenditure on existing policies for years 4 and 5 will be shown, analysed by function, as in Table 6.

#### IV. PARLIAMENT AND THE PROPOSED PRESENTATION

45. As already stated (in paragraph 5 above) the Government propose that this new form of presentation should be used in an annual White Paper to be laid before Parliament. The Government expect that the Select Committee on Procedure will wish to give their views on how the presentation of the White Paper could best be fitted into the annual cycle of Parliament's examination of public expenditure. It would be a matter for further consideration whether time should be set aside for debate on such a White Paper and if so on what form of motion the debate should be founded.

46. The Government believe that this new annual White Paper, which will look three and five years forward at the resource implications of public expenditure, would prove a great help to public discussion. They believe that discussion would also be helped by a revision of some existing procedures which may now have become a hindrance to clearer understanding of the subject, inside and outside the House.

47. The Government are sure that, in any revised procedures, the House of Commons will wish to continue to exercise its constitutional function of determining the provision of money for the conduct of the business of the Government. The procedure for submission of annual Estimates, and of Supplementary or Revised Estimates, at the appropriate times of the year is regarded by the Government as, in principle, well suited to this purpose, and they have no proposals for changing any of its essential features, or for altering the number of days devoted to the debating of Supply.

48. The Estimates documents are suitable for the purposes of voting and appropriating moneys, but they do not provide Parliament with a satisfactory basis for the kind of discussions of policy for which Supply days have been increasingly used. It is here that an annual White Paper is designed to help.

49. The part of present procedures which the Government see as unhelpful and indeed possibly misleading is the Vote on Account in its present form. Formally, the debate on the Vote on Account takes place on a parliamentary paper stating the sum required for the Government's operations between the beginning of the new financial year, when the authorisations of the preceding year's Appropriation Act expire, and the passage in the summer of a new Appropriation Act.<sup>(12)</sup> In practice, the document has been made more informative by including in it a summary of the complete Supply Estimates for the forthcoming year, with a comparison of the total of new Estimates with the corresponding total for the preceding year. Under present procedures, this Vote on Account total is each year the first major aggregate in the field of public expenditure which is required to come before Parliament. But its nature is such that it is liable to give a misleading impression to the House and to outside opinion at home and overseas of the content of public expenditure, of its economic significance, and of its development in comparison with preceding years.<sup>(13)</sup>

50. Because misunderstanding may be harmful to the national interest, the Chancellor of the Exchequer took the exceptional step this year of making a full statement in the House on 20th February to explain the relationship of the content of Supply expenditure to public expenditure, and of the movement in Supply expenditure compared with the previous year (7·9 per cent at current prices) to the corresponding movement in total public expenditure (1 per cent at constant prices).

51. If the Vote on Account, in its present form, were to be discontinued the need would remain for a procedure whereby the House of Commons would determine the provision of money for the first months of the new financial year. The Government's proposal is that this should be done each year in the Appropriation Act, by a clause enabling the Government to spend in the period beyond the end of the financial year and before the next Appropriation Act a stated proportion of the sums voted for the current year. To ensure that Parliament would have a full opportunity to debate the merits of such a change in procedure, the Government propose that for the first year in which this arrangement was introduced it should be made the subject of a special Bill.

52. This paper opened by referring to the adaptation and development of procedures to make them serve modern needs effectively. The Government believe that the changes proposed, and the use of the new information described in this paper, will make possible a further important advance in parliamentary and public discussion of expenditure.

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<sup>(12)</sup> Arrangements for handling Defence Votes are at present under examination by the Select Committee on Procedure.

<sup>(13)</sup> The main reasons why the total of Supply expenditure published with the Vote on Account is not a useful measure of public expenditure are as follows. First, Supply expenditure includes a great deal of expenditure on grants to local authorities which, if counted as public expenditure, would duplicate that part of the actual expenditure of local authorities which it finances. Secondly, there is a great deal of public expenditure which is not Supply expenditure including, apart from local authorities' expenditure, central Government expenditure from the National Insurance Funds. The effect of these two points is that the element of Supply expenditure which enters into the total of public expenditure (even excluding debt interest and nationalised industries' capital expenditure investment) is only about half that total. (Details are given in Table 3 of "Public Expenditure 1968-69 to 1970-71", Cmnd. 3936.) Thirdly, as that Table also shows, these various elements of public expenditure and Supply expenditure move very differently from each other from year to year.

Note: In the following six Tables, "Survey year -1" means the financial year ended on 31st March preceding publication, "Survey year 1" means the financial year of publication, "Survey year 2" the following financial year, and so on. Thus, in a 1969 White Paper, "Survey year 1" would be 1969-1970. The figures given in the Tables below relate to 1968-69 provisional outturn and are illustrative only.

TABLE 1

PUBLIC SECTOR EXPENDITURE BY FUNCTION  
SURVEY YEAR -1 TO SURVEY YEAR 3

£ million (at constant prices)

	Survey year -1	Survey year 1	Survey year 2	Survey year 3	Average annual percentage increase years 1 to 3
Defence Budget ... ..	2,247				
Other military defence ... ..	153				
Civil defence ... ..	8				
Overseas aid ... ..	210				
Other overseas services ... ..	122				
Roads and public lighting ... ..	605				
Transport... ..	262				
Technological services ... ..	186				
Other assistance to employment and industry ... ..	834				
Research Councils, etc. ... ..	86				
Agriculture, fisheries and forestry ... ..	359				
Housing ... ..	1,085				
Local environmental services ... ..	693				
Law and order ... ..	544				
Arts ... ..	16				
Education and local libraries ... ..	2,194				
Health and welfare ... ..	1,750				
Social security ... ..	3,312				
Financial administration ... ..	213				
Common services ... ..	158				
Miscellaneous services ... ..	54				
Northern Ireland ... ..	408				
Nationalised industries, etc., capital expenditure ... ..	1,543				
Debt interest ... ..	1,893				
Shortfall <sup>(1)</sup> ... ..	-24 <sup>(2)</sup>				
Relative price effect ... ..	—				
Contingency reserve ... ..	—				
<b>Total ... ..</b>	<b>18,911</b>				

(1) The difference between programmed expenditure and expected outturn.

(2) The difference between the provisional total of specific programmes and the provisional outturn shown in "Financial Statement and Budget Report, 1969-70".

Note: In the following six Tables, "Survey year -1" means the financial year ended on 31st March preceding publication, "Survey year 1" means the financial year of publication, "Survey year 2" the following financial year, and so on. Thus, in a 1969 White Paper, "Survey year 1" would be 1969-1970. The figures given in the Tables below relate to 1968-69 provisional outturn and are illustrative only.

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Nationalised industries, etc., capital expenditure ... ..	1,543				
Debt interest ... ..	1,893				
Shortfall <sup>(1)</sup> ... ..	-24 <sup>(2)</sup>				
Relative price effect ... ..	—				
Contingency reserve ... ..	—				
<b>Total ... ..</b>	<b>18,911</b>				

<sup>(1)</sup> The difference between programmed expenditure and expected outturn.

<sup>(2)</sup> The difference between the provisional total of specific programmes and the provisional outturn shown in "Financial Statement and Budget Report, 1969-70".

TABLE 2  
PUBLIC SECTOR RECEIPTS AND EXPENDITURE  
SURVEY YEAR -1 TO SURVEY YEAR 3

Summary Analysis

£ million (at constant prices)

Line	Receipts				Expenditure			
	Survey year -1	Survey year 1	Survey year 2	Survey year 3	Survey year -1	Survey year 1	Survey year 2	Survey year 3
1	A. RESOURCES							
	Charges ... ..	402			Purchases of resources for capital and current purposes ... ..	12,710		
2		—	—	—	Net expenditure ... ..	12,308		
3	B. TRANSFERS, TAXATION, ETC.							
4		—	—	—	Grants and subsidies ... ..	4,777		
5	Taxes ... ..	12,917			Debt interest ... ..	1,513		
6	Contributions:					—	—	—
	(a) National insurance <sup>(1)</sup> ... ..	1,927				—	—	—
	(b) Other ... ..	225				—	—	—
7	Other receipts ... ..	2,479				—	—	—
8	Total ... ..	17,548				6,290		
9	Balance of Section B ... ..	—	—	—		-11,258		
10	C. ASSETS							
	Taxes on capital and miscellaneous borrowing, etc. ... ..	1,048			Net purchase of land, existing buildings and financial assets ... ..	313		
11	Balance of Section C ... ..	—	—	—		-735		
12	D. TOTAL RECEIPTS (Lines 8 and 10) ... ..	18,596			TOTAL EXPENDITURE (Lines 2, 8 and 10) (Public expenditure)...	18,911		
13	E. TOTAL BALANCE (Lines 2, 9 and 11) ... ..	—				315		
14	F. BALANCE OF RESOURCES, TRANSFERS, TAXATION, ETC. (Lines 2 and 9) ... ..	—				1,050		

<sup>(1)</sup> Including Industrial Injuries.

Note: This Table would be provided for Survey year -1 and Survey years 1, 2 and 3

TABLE 3  
PUBLIC SECTOR RECEIPTS AND EXPENDITURE

Analysis by Function and Type of Transaction

£ million (at constant prices)

Expenditure positive/Receipts negative	Resources			Transfers, taxation, etc.			Balance of resources, transfers, taxation, etc. (cols. 3 and 6)	Assets			Total balance (cols. 3, 6 and 10)	Public expenditure (cols. 3, 4 and 8)
	Purchases	Charges	Net expenditure	Payments	Receipts	Balance of transfers, taxation, etc.		Net purchases	Net receipts	Balance of assets		
	(1) Line 1	(2) Line 1	(3) Line 2	(4) Line 8	(5) Line 8	(6) Line 9	(7) Line 14	(8) Line 10	(9) Line 10	(10) Line 11	(11) Line 13	(12) Line 12
Corresponding line in Table 2	Line 1	Line 1	Line 2	Line 8	Line 8	Line 9	Line 14	Line 10	Line 10	Line 11	Line 13	Line 12
1. Defence Budget ... ..	2,347	-111	2,236	1	-	1	2,237	10	-	10	2,247	2,247
2. Other military defence ... ..	152	1	153	-	-7	-7	146	-	-	-	146	153
3. Civil defence ... ..	11	-2	9	-	-	-	9	-1	-	-1	8	8
4. Overseas aid ... ..	149	-	149	61 <sup>(1)</sup>	-61	-	149	-	-	-	149	210
5. Other overseas services ... ..	121	-2	119	3	5	8	127	-	-	-	127	122
6. Roads and public lighting ... ..	566	-10	556	-	-1	-1	555	49	-	49	604	605
7. Transport ... ..	79	-	79	174	-11	163	242	9	-	9	251	262
8. Technological services ... ..	173	-12	161	10	-7	3	164	15	-	15	179	186
9. Other assistance to employment and industry ... ..	81	-1	80	692	-97	595	675	62	-	62	737	834
10. Research Councils, etc. ... ..	87	-1	86	-	-1	-1	85	-	-	-	85	86
11. Agriculture, fisheries and forestry ... ..	124	-3	121	240	-1	239	360	-2	-	-2	358	359
12. Housing ... ..	779	-	779	235	-611	-376	403	71	-	71	474	1,085
13. Local environmental services ... ..	699	-45	654	-	-11	-11	643	39	-	39	682	693
14. Law and order ... ..	529	-4	525	15	-	15	540	4	-	4	544	544
15. Arts ... ..	16	-	16	-	-	-	16	-	-	-	16	16
16. Education and local libraries ... ..	2,268	-102	2,166	-	-1	-1	2,165	28	-	28	2,193	2,194
17. Health and welfare ... ..	1,851	-106	1,745	-	-181	-181	1,564	5	-	5	1,569	1,750
18. Social Security (a) Insurance benefits and contributions ... ..	104	-	104	2,315	-1,927	388	492	-	-	-	1,385	3,312
(b) Other benefits ... ..	47	-	47	846	-	846	893	-	-	-		
19. Financial administration ... ..	193	-	193	20	18	38	231	-	-	-	231	213
20. Common services ... ..	159	-1	158	-	-4	-4	154	-	-	-	154	158
21. Miscellaneous services ... ..	52	-3	49	1	-4	-3	46	4	-	4	50	54
22. Northern Ireland ... ..	238	-	238	164	-66	98	336	6	-	6	342	408
23. Nationalised industries, etc. ... ..	1,529	-	1,529	-	-837	-837	692	14	-	14	706	1,543
24. Debt interest ... ..	380	-	380	1,513	-	1,513	1,893	-	-	-	1,893	1,893
25. Shortfall ... ..	-24	-	-24	-	-	-	-24	-	-	-	-24	-24
26. Relative price effect ... ..	-	-	-	-	-	-	-	-	-	-	-	-
27. Contingency reserve ... ..	-	-	-	-	-	-	-	-	-	-	-	-
28. Taxes and other unallocated receipts	-	-	-	-	-13,743	-13,743	-13,743	-	-1,048	-1,048	-14,791	-
29. Total ... ..	12,710	-402	12,308	6,290	-17,548	-11,258	1,050	313	-1,048	735	315	18,911 <sup>(2)</sup>

<sup>(1)</sup> This represents the provision of finance for aid expenditure, equivalent to the repayments of capital and payments of interest on earlier aid loans shown in column 5.

<sup>(2)</sup> The total of public expenditure in Table 1 of Cmnd. 3936 and of public sector expenditure in Table 9 of "Financial Statement and Budget Report, 1969-70" may be reconciled with this total as follows:

	£ million
Total public expenditure (Cmnd. 3936, Table 1) ... ..	15,870
<i>Deduct</i>	
Changes in estimated outturn between Cmnd. 3936 and end of financial year ... ..	-87
<i>Add</i>	
Nationalised industries, etc., capital expenditure ... ..	1,543
Debt interest ... ..	1,893
Total public sector expenditure (Table 9 of "Financial Statement and Budget Report, 1969-70") ... ..	19,219
<i>Deduct</i>	
Imputed rent ... ..	-308
Total public expenditure (as above) ... ..	18,911

Note: This Table would be provided for Survey year -1 and Survey years 1, 2 and 3

TABLE 4

PUBLIC SECTOR EXPENDITURE BY FUNCTION AND SPENDING AUTHORITY

£ million (at constant prices)

	Central Government		Local Authorities	Public Corporations	Total
	Supply	Other			
Defence Budget ... ..	2,247	-	-	-	2,247
Other military defence ... ..	154	-1	-	-	153
Civil defence ... ..	6	-2	4	-	8
Overseas aid ... ..	193	7	-	10	210
Other overseas services ... ..	120	2	-	-	122
Roads and public lighting ... ..	181	-	424	-	605
Transport ... ..	203	-6	61	4	262
Technological services ... ..	176	7	-	3	186
Other assistance to employment and industry ... ..	771	20	9	34	834
Research Councils, etc. ... ..	86	-	-	-	86
Agriculture, fisheries and forestry ... ..	357	-2	4	-	359
Housing ... ..	148	-2	865	74	1,085
Local environmental services ... ..	11	-	652	30	693
Law and order ... ..	102	2	440	-	544
Arts ... ..	16	-	-	-	16
Education and local libraries ... ..	340	-1	1,855	-	2,194
Health and welfare ... ..	1,499	-	251	-	1,750
Social security ... ..	893	2,419	-	-	3,312
Financial administration ... ..	151	42	20	-	213
Common services ... ..	168	-10	-	-	158
Miscellaneous services ... ..	38	9	7	-	54
Northern Ireland ... ..	-	262	112	34	408
Nationalised industries, etc., capital expenditure ... ..	-	-	-	1,543	1,543
Debt interest ... ..	-	1,257	523	113	1,893
Shortfall ... ..	-51	-4	43	-12	-24
Relative price effect ... ..	-	-	-	-	-
Contingency reserve ... ..	-	-	-	-	-
Total ... ..	7,809	3,999	5,270	1,833	18,911



TABLE 5

**PUBLIC SECTOR EXPENDITURE BY ECONOMIC CATEGORY  
SURVEY YEAR -1 TO SURVEY YEAR 3**

£ million (at constant prices)

	Survey year -1	Survey year 1	Survey year 2	Survey year 3
Current expenditure on goods and services ... ..	7,319			
Subsidies ... ..	876			
Debt interest ... ..	1,893			
Current grants to personal sector ...	3,913			
Current grants abroad ... ..	171			
Gross domestic fixed capital formation	3,829			
Increase in value of stocks ... ..	53			
Capital grants to private sector ...	667			
Net lending to private sector ... ..	75			
Loans to overseas Governments ...	88			
Drawings from United Kingdom sub- scriptions to international lending bodies ... ..	19			
Other net lending and investment abroad	-4			
Cash expenditure on company securities (net) ... ..	12			
Shortfall ... ..	—			
Relative price effect ... ..	—			
Contingency reserve ... ..	—			
<b>Total ... ..</b>	<b>18,911</b>			

TABLE 6

**PUBLIC SECTOR EXPENDITURE BY FUNCTION: PROJECTED  
EXPENDITURE, SURVEY YEARS 4 AND 5**

£ million (at constant prices)

								Survey year 4	Survey year 5
Defence Budget	...	...	...	...	...	...	...		
Other military defence	...	...	...	...	...	...	...		
Civil defence	...	...	...	...	...	...	...		
Overseas aid	...	...	...	...	...	...	...		
Other overseas services	...	...	...	...	...	...	...		
Roads and public lighting...	...	...	...	...	...	...	...		
Transport	...	...	...	...	...	...	...		
Technological services	...	...	...	...	...	...	...		
Other assistance to employment and industry	...	...	...	...	...	...	...		
Research Councils, etc.	...	...	...	...	...	...	...		
Agriculture, fisheries and forestry	...	...	...	...	...	...	...		
Housing	...	...	...	...	...	...	...		
Local environmental services	...	...	...	...	...	...	...		
Law and order	...	...	...	...	...	...	...		
Arts	...	...	...	...	...	...	...		
Education and local libraries	...	...	...	...	...	...	...		
Health and welfare	...	...	...	...	...	...	...		
Social security	...	...	...	...	...	...	...		
Financial administration	...	...	...	...	...	...	...		
Common services	...	...	...	...	...	...	...		
Miscellaneous services	...	...	...	...	...	...	...		
Northern Ireland	...	...	...	...	...	...	...		
Nationalised industries, etc., capital expenditure...	...	...	...	...	...	...	...		
Debt interest...	...	...	...	...	...	...	...		
Shortfall	...	...	...	...	...	...	...		
Relative price effect	...	...	...	...	...	...	...		
Contingency reserve	...	...	...	...	...	...	...		
<b>Total</b>	...	...	...	...	...	...	...		

## DEVELOPMENTS BEFORE AND SINCE THE PLOWDEN REPORT ON CONTROL OF PUBLIC EXPENDITURE<sup>(1)</sup>

1. The introductory section of this Green Paper outlines developments in Parliamentary procedures for considering public expenditure and the evolving techniques now being used by the Government for reaching decisions on expenditure. The purpose of the present Appendix is to elaborate on this outline.

### Development in the handling of public expenditure

2. During the 1950s there was growing dissatisfaction in Parliament, the Government, the Treasury, spending Departments and elsewhere with the handling of public expenditure. The picture of expenditure was fragmented between the central Government and other spending authorities. As public sector outlays grew, the task of planning the various programmes assumed new importance; and it could not be readily accommodated in a short-term horizon. Many expenditures called for relatively small outlays at the start and only built up to bigger sums later, so that by the time substantial effects began to show in the Budget arithmetic for the coming year, policy was too firmly established for it to be reversed, and there was little that could be done save to meet the bill, if need be through increased taxation or borrowing. But while the implications of decisions for much of the field were known to ramify far into the future, there was no complete perspective of the future in which to consider them.

3. The role of the annual Budget had changed as a result of post-war policies for maintaining full employment and managing demand in order to achieve this purpose. The implications of this for management of public expenditure were being gradually clarified. The Budget came to be recognised as primarily concerned with adjusting the short-term situation in the economy as a whole so as to bring supply and demand into balance in the year in question; but since the planning of public expenditure could only sensibly be done over a longer period, the question was posed how to gear the management of public expenditure to the management of the economy, while providing sufficient stability for public expenditure to be planned and run efficiently.

4. Attempts were made to solve this problem along lines which the Plowden Committee eventually brought to their logical conclusion<sup>(2)</sup> and which have since been embodied in routine procedures. Time horizons were extended, for example in defence expenditure, where as much as ten years may be needed to evolve and put into effect a new weapons system. As a result, from 1958 five-year defence costings, later extending to ten years, were introduced. In education, forward school-building programmes, spread over several years, had already been developed, with control focussed on the point where it would be thoroughly effective: that is, on the start of building work, coupled with limits on unit costs. For some years all public sector investment programmes were examined together, and annual White

<sup>(1)</sup> Cmnd. 1432.

<sup>(2)</sup> *ibid.*, and paragraphs 5-8 below.

Papers on public investment were published. It was to provide the perspective for these investment surveys that from 1957 five-year economic assessments of the economy as a whole were developed. Eventually the surveys of investment were absorbed in the wider and more comprehensive public expenditure Surveys started in 1961, following the Plowden Report.

### **The Report of the Select Committee on the Estimates, 1957–58, and the Plowden Report**

5. In the 1957–58 Session of Parliament, the Select Committee on Estimates examined Treasury control of expenditure, and their report led to the setting up of the Committee on the Control of Public Expenditure under Lord (then Sir Edwin) Plowden in the summer of 1959.

6. The main conclusion of the Plowden Report was as follows:

“ . . . Decisions involving substantial future expenditure should always be taken in the light of surveys of public expenditure as a whole, over a period of years, and in relation to the prospective resources. Public expenditure decisions, whether they be in defence or education or overseas aid or agriculture or pensions or anything else, should never be taken without consideration of (a) what the country can afford over a period of years having regard to prospective resources and (b) the relative importance of one kind of expenditure against another. This may appear to be self-evident, but in administrative (and, we hazard the opinion, in political) terms it is not easy to carry out.”<sup>(3)</sup>

Plowden recognised, however, that the economy is susceptible to prediction even five years ahead “only within broad limits”.

7. The Committee recommended<sup>(4)</sup> a reconstruction of the traditional system of decision-making based on four elements, of which the first and most important was:

“Regular surveys should be made of public expenditure as a whole, over a period of years ahead, and in relation to prospective resources; decisions involving substantial future expenditure should be taken in the light of these surveys.”

8. In this way the Report broadened the scope of policy decisions on public expenditure, which was now seen as extending over the whole public sector, comprehending expenditure of the central Government, whether Vote-borne or carried on the national insurance and other funds, that of local authorities (whether locally or centrally financed) and the capital investment of the nationalised industries and other public corporations. All this was to be considered in relation to the country's resources.

### **Implementation of the Plowden Report**

9. From 1961 annual Surveys of public expenditure were prepared for Ministers on the lines recommended by Plowden. A number of features of these Surveys, some of which have been set out in White Papers of 1963 and 1966,<sup>(5)</sup> should be noted:

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<sup>(3)</sup> *ibid.*, paragraph 7.

<sup>(4)</sup> *ibid.*, paragraph 12.

<sup>(5)</sup> “Public Expenditure in 1963–64 and 1967–68” (Cmnd. 2235), and “Public Expenditure: Planning and Control” (Cmnd. 2915).

- (a) as the object was to show the final expenditure of the public sector, regardless of the way in which it was financed, transactions within the public sector such as central Government grants to local authorities were excluded.
- (b) Expenditure was analysed by function, that is, by broad, closely related groups of objectives, for example, defence, health, education, social security, assistance to employment and industry, and so on.
- (c) Expenditure was also analysed by economic category (current expenditure on goods and services, gross domestic fixed capital formation, grants to persons and so on) so as to be comparable with the elements in the National Income Accounts.
- (d) Each Survey looked five years ahead—that is to say, the 1961 Survey related to the period up to and including the financial year 1965–66; and each following Survey rolled the figures forward a year.
- (e) The annual Surveys of expenditure were, from the start, considered in conjunction with annual assessments of the economic prospect over the same period.

10. Originally the Surveys dealt with only the first and fifth years. As time went on the analysis was made more detailed and figures for the intervening years were introduced. Attention came to be concentrated on the third year, for which specific decisions were taken. Decisions taken in one Survey for the years ahead provide the basis for departmental plans, and are progressively hardened in subsequent Surveys, so that they become the firm basis of management of the eventual expenditures.

## APPENDIX II

### SOME TECHNICAL ASPECTS OF MEASURING PUBLIC EXPENDITURE IN RELATION TO THE USE OF RESOURCES

1. The aim of the new presentation is to display the implications of public expenditure programmes for the use of currently available resources. Expenditure is projected on the basis of existing policies and decisions; receipts are projected on stated assumptions, notably existing rates of central Government taxation. The outlays and receipts are expressed at constant prices according to a set of conventions which bring the two sides of the account into equivalence with one another in the sense that the balance between them provides an indication of the residual financing requirements of the public sector. In the event, the borrowing which will actually be required in a given year will depend on the level of taxation eventually decided for that year, on the realised outturn of public expenditure programmes and on the changes in the level of prices.

#### The Use of Resources—Notes on Tables 2 and 3

2. In order to give a broad indication of the use of resources implied by different types of public expenditure, the relevant transactions are set out in three groups:—resources, transfers and assets. The principles underlying the allocation of expenditure items to these groups are described below; receipts items will be allocated in accordance with the same principles. The distribution of items is consonant with the present availability of data on public sector receipts and expenditures. In the course of time further improvements and refinements should be possible.

#### A. Resources

3. The principle on the expenditure side here is to include those public sector outlays which represent a direct call on resources. This means including all outlays on currently produced goods and services, for both current and capital purposes. Also included are public sector grants to private non-profit making bodies, such as universities, which spend the full grant on purchasing goods and services, and capital grants to persons. Where the public sector makes current grants to persons which lead to their withdrawal from the labour force (*e.g.*, student maintenance grants) these are also included under "Resources". Finally, net payments abroad by the public sector are treated as a use of resources because of the need to provide at least an equivalent volume of resources for the balance of payments.

#### B. Transfers

4. The expenditures included here cover public sector outlays which represent a call on resources indirectly rather than directly. This indirectness means that any associated receipts, tax deductions and savings by companies or persons have to be allowed for to arrive at the possible use of resources.

## C. Assets

5. The transactions included here are those which affect mainly the asset structure and liquidity position of companies and persons and where the effect of a given amount of public expenditure on the use of resources can therefore be expected to be markedly different from expenditures classified under A and B. Taxes on assets such as Estate Duty and Capital Gains Tax are included on the receipts side.

### Public Sector

#### Receipts

#### Expenditure

#### A. Resources

##### Charges

1. Charges and sales normally offset to current expenditure on goods and services.
2. Charges for school meals and milk and welfare foods.

##### Purchase of resources for capital and current purposes

1. Current expenditure on goods and services (other than imputed rent), gross of charges.
2. Gross domestic capital formation excluding transactions in land and existing buildings. + *Stock building*
3. Current and capital grants to private non-profit making bodies.
4. Current grants to persons (education, health and Research Councils).
5. Capital grants to persons.
6. Net expenditure abroad—current grants, debt interest and net lending less receipts of interest.

#### B. Transfers, taxation, etc.

##### Taxes

1. Taxes on income and expenditure and local rates.

##### Grants and subsidies

1. Subsidies.
2. Current grants to persons (except under education, health and Research Councils).
3. Capital grants to companies.

##### Contributions

2. National insurance.
3. Health Service.
4. Other

##### Other receipts

5. Gross trading surpluses before depreciation and stock appreciation.
6. Rent, dividends and interest other than interest receipts from abroad and imputed rent.
7. Receipts for capital works.

##### Debt interest

4. Debt interest, excluding payments abroad.

#### C. Assets

##### Taxes on capital and miscellaneous borrowing, etc.

1. Taxes on capital.
2. Borrowing from certain pension funds (net).
3. Northern Ireland Central Government borrowing (net).
4. Miscellaneous financial transactions (net) (including import deposits and adjustments for tax accruals).

##### Net purchases of land, existing buildings and financial assets

1. Purchases less sales of land and existing buildings.
2. Net lending to the private sector.
3. Cash expenditure on company securities (net).

6. In addition to expenditure, some receipts have also been allocated by function in Table 3, namely earnings (trading surpluses, rent, dividends and interest) and contributions (national insurance, health service and redundancy fund) in accordance with the allocation of the associated expenditure on assets and benefits.

7. In the case of nationalised industries and other public enterprises, gross trading surpluses have to provide for interest payments on capital and (where charged) tax payments. This reduces the amount available to the public enterprise for gross capital formation. In order that the residual financing requirement (column 11) should not be understated, the appropriate interest and tax payments have been deducted from the trading surpluses before their allocation in column 5 and entered among unallocated receipts in line 28.

8. The public expenditure totals entered in column 12 differ from previously published totals through

- (a) the exclusion of imputed rent (which has been dropped owing to the difficulties of estimation and deficiencies of coverage). Since imputed rents would be entered on both sides of the account, their inclusion would, in any event, make no difference to the figures for the balances;
- (b) the inclusion of capital expenditure by the nationalised industries, the broadcasting authorities and the Covent Garden Market Authority;
- (c) the inclusion of debt interest;
- (d) the inclusion of shortfall (the difference between programmed expenditure and expected outturn) where appropriate;
- (e) the addition of an adjustment for "relative price effect" (see paragraphs 9 to 16 below).

### **The Price Problem—constant prices and relative prices**

9. To help indicate the disposition of physical resources, public expenditure outlays are expressed at constant prices. This procedure is an extension of that used in the National Income Accounts for the revaluation of goods and services. In essence, the methodology is to revalue quantities in each year at the prices of the base year.

10. Section A of the new presentation of public expenditure covers the public sector purchases of goods and services and other expenditure which is treated as direct claims on resources (*e.g.*, overseas aid and grants to universities). These outlays are largely (about one half) concerned with the purchases of manpower to work in the public sector. It is most important that the cost of employing this manpower should be adequately reflected in the total.

11. Over time, the productivity of labour in the economy will be rising. So the cost of employing a given amount of labour in the public sector, in terms of the potential output from the private sector which has to be forgone, will rise in step with productivity in the private sector. Rising productivity in the private sector will be accompanied by rising real earnings in that



sector and real earnings in the public sector will have to keep pace if the necessary distribution of the labour force is to be achieved. Expressing public sector programmes at constant pay and prices therefore progressively understates their cost because it does not allow for the increase in opportunity cost arising from productivity changes in the private sector.

12. The constant price presentation also progressively understates the scale as well as the cost of the public services provided. This is because productivity in the public services (*e.g.*, health, education, defence) is so hard to measure that the convention is followed that the output of those employed in the public service is equal to their pay, and in a constant price presentation productivity and earnings are taken as constant. Yet the rise in productivity in the public service is occurring continuously through the application to the tasks of policemen, soldiers, doctors, teachers and clerks, of advances in technology, in organisation and in training methods. In so far as this is happening, one of two things (or a combination of them) will occur: either the country will get bigger and better services than constant price estimates indicate; or the increased productivity will enable the same level of service to be maintained with fewer staff. In the latter case the constant price estimates (which would show a decrease) would still understate the scale of the service provided. In both cases, allowance still has to be made for the increase in opportunity cost caused by rising productivity in the private sector.

13. An indication of the magnitude of the effect of the phenomenon described in paragraph 11 for the main element in public sector programmes may be obtained from a comparison of public consumption as a proportion of gross national product, first at current prices and then at constant prices. The proportions diverge year by year and on average  $1\frac{1}{2}$  per cent or 2 per cent a year would have to be added to the total of public consumption at constant prices to keep its share of the national product in line with the share at current prices. It is, of course, according to the relative demand on resources at current prices that the weight of taxation needs to be adjusted. An overall allowance for this "relative price effect" is therefore included in the presentation; it has not yet proved possible to allocate it by function, though clearly the more labour-intensive functions will account for more of it than the others.

14. The adjustment for the "relative price effect" described above relates only to current expenditure on goods and services. But the relative prices of other expenditure on resources may move differentially as well and minor adjustments may also be necessary for these, some of which may go in the opposite direction (*e.g.*, expenditure on plant and machinery). Also, expenditure which is not regarded as a direct use of resources may be regarded as a transfer of claims over resources, and this too needs to be revalued to constant prices, in accordance with the principle applied to the treatment of current expenditure on goods and services. In general the procedure followed is to calculate the proportion which the various categories of expenditure bear to G.N.P. at current factor cost for each year covered by the Survey, as revealed in the medium-term economic projections, and to apply these proportions to the corresponding estimate of G.N.P. at constant factor cost. For some important categories of expenditure, such

as social security benefits, price factors more appropriate to the particular type of outlay are used. In order that the total of expenditure at constant prices might correctly reflect the proportion which it bears to gross national product at current prices, it is necessary to make an overall adjustment. This adjustment is included in the item "relative price effect".

15. Similar adjustments to constant prices need to be made on the receipts side of the account. This is particularly the case for projected tax receipts which are first calculated at current prices and then deflated to a constant price basis.

16. The end-product of all these adjustments is a set of projections which discount the effect of general price changes, as do all constant price estimates, but also attempt to allow for changes in relative prices which projections of quantities and of employment alone cannot do.

### **Public Expenditure—short-run effect on demand**

17. In most cases of expenditures which are regarded as direct claims on resources (such as the employment of public servants, the purchase of materials and payments abroad) only minor adjustments have to be made to the gross outlays to obtain a measure of the short-run effect on demand. The only deductions are in respect of indirect taxes, such as SET paid on civil servants, or import duties included in the price of materials. In principle other adjustments should be made where the balance of payments cost, the regional impact, or the manpower content of the programme is markedly atypical. But the extent of the adjustments which have to be made on these counts is very difficult to assess, and it is not attempted in this presentation.

18. The impact of transfer payments is extremely varied because of the very different tax effects and saving adjustments which need to be made. When adjustments at the margin to any particular programme are being considered it is possible to estimate the impact effect in that case. It is not possible to show in tabular form the effect for public expenditure as a whole. Transfer payments include investment grants, social security benefits, subsidies and debt interest. The following are examples of the varied effects that can occur. In the case of grants and subsidies to industry, a change in policy is unlikely to have much effect on activity in the year in which it is instituted. At that time the main effect is likely to be on company liquidity, but in subsequent years the increased liquidity should work through into increased company outlays. In the case of payments of debt interest, any increase in outlays will generate a return stream of income-tax and surtax payments, and part of the remainder will be saved. The rest will probably be spent on goods and services. But as about a fifth of the additional consumers' expenditure on goods and services flows directly back to the Government in the form of increased indirect taxes, the end-result is that only about a half of the original increase in interest payments will be reflected in an increase in demand. Much the same considerations apply to family allowances and other grants to persons which are spread fairly evenly over the population. The impact of other social security benefits depends very much on the nature of the increase. The effect of a general increase in contributory benefits, for example, will be considerably offset by the associated increase

in contributions. Some contributory benefits are tax-free (sickness, maternity, unemployment and death benefits). Retirement, widows and guardians benefits are all taxable—but the income tax yield is normally less than half that from family allowances, since they mostly go to the lower income groups; and the proportion going into savings is certainly lower too. Supplementary benefits which are non-contributory go only to the most needy; they are tax-free and no appreciable part of them is saved, though they prevent a little dis-saving. In all cases, of course, about a fifth of any additional expenditure comes back to the public authorities in the form of purchase tax, excise duties, SET, local rates and other taxes on expenditure.

19. The demand effect of purchases of existing assets and similar capital transactions—for example when the Government buy land and existing buildings or company securities, or lend to companies or individuals—is normally only very small in the year in which they are made. In later years there tends to be some leakage of this increased liquidity into increased expenditure by companies and individuals. Loans to companies may have various effects and each major item must be separately estimated. Account has to be taken not only of the effect on demand, but of the timing of the effect on demand. In most cases the effect on demand of the public sector outlays is a lagged one, but there are examples of the reverse effect (*e.g.*, some shipbuilding loans are paid out subsequent to the increase in the activity in the shipyards which those loans have made possible).

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