

Section 2

Consolidated Departmental
Resource Accounts 2003-04

Annual Report

History and Background

The present Ministry of Defence (MoD), the Department, was formed by the amalgamation in 1964 of the Ministry of Defence, the Admiralty, the War Office and the Air Ministry, and the inclusion in 1971 of the Ministry of Aviation Supply. In 1973, the operations of the Atomic Weapons Establishment (AWE) were transferred from the UK Atomic Energy Authority to the MoD.

Principal Activity

The principal activity of the Department is to deliver security for the people of the United Kingdom and the Overseas Territories by defending them, including against terrorism; and to act as a force for good by strengthening international peace and stability.

Further definition of the Departmental Objectives in terms of output is given in Schedule 5, Resources by Departmental Aims and Objectives.

Departmental Boundary

At 31 March 2004 the Department consisted of the 11 (2002-03:11) Top Level Budget (TLB) Holders detailed in Note 27 to the financial statements, responsible for providing forces and support services required for a modern defence force. Within these TLBs there were 72 (2002-03: 81) reporting entities known as management groupings. There are 30 (2002-03: 31) on-vote Defence agencies listed in Note 31. All on-vote agencies are also management groupings, except for the Defence Procurement Agency (a TLB) and the Disposal Services Agency (part of a management grouping). Also included within the Departmental Boundary are Advisory Non-Departmental Public Bodies (NDPB) sponsored by the Department listed in Note 31. Defence Agencies also publish their own financial statements.

The five (2002-03: five) Defence Executive Agencies established as Trading Funds and owned by the Department at 31 March 2004 fall outside the Departmental Boundary and are detailed in Note 10. The seven Executive NDPBs listed in Note 11 are sponsored by the Department and fall outside the Departmental Boundary. The accounts of these bodies are published separately.

QinetiQ Holdings Limited (hereafter referred to as "QinetiQ") is a Self-Financing Public Corporation which falls outside the Departmental Boundary. The Navy, Army and Air Force Institutes (NAAFI) is also outside the Departmental Boundary.

The transactions and balances of the Armed Forces Pension Scheme (AFPS) are not consolidated within these financial statements. The report and accounts of the AFPS are prepared separately.

Future Developments

The Defence White Paper, published in December 2003, set out the Department's analysis of the future security environment, the implications for defence, strategic priorities and how it intends to adapt its planning and force structures to meet potential threats. Using the policy baseline established in the White Paper and following a rigorous examination of force structure, specific equipment requirements and supporting infrastructure, manpower and organisational structure, the Secretary of State set out, in July 2004, the changes the Department should make to the force structure and its key capacity requirements for the future.

From 1 April 2004 a new Top Level Budget was created called the Corporate Science Technology TLB. Headed up by the Chief Scientific Advisor this TLB brings together functions formerly managed in different areas of the department relating to science and technology. As at that date the Department also merged the Defence Housing Executive Agency and Defence Estates Agency with the aim of making efficiencies and improvements to the delivery of service housing. In addition, the three service manning agencies, the Naval Manning Agency, the Army Personnel Centre and the RAF Personnel Management Agency were disestablished. These changes arose as a result of one of the recommendations of a major end to end review of the Service Personnel Process and will contribute towards the rationalisation of the Armed Forces manpower, planning and career management functions as well as giving stronger emphasis to the needs of individual Service personnel.

Fixed Assets

Changes in fixed assets during the year are summarised in Notes 8, 9 and 10 to the financial statements.

Research and Development

Research and development expenditure is incurred mainly for the future benefit of the Department. Such expenditure is primarily incurred on the development of new fighting equipment and on the improvement of the effectiveness and capability of existing fighting equipment.

Amounts spent on research are not capitalised, and certain development expenditure is expensed, in accordance with SSAP13 "Accounting for Research and Development", and are included in Other Operating Costs detailed in Note 3.

Development expenditure is included in Intangible Assets, where appropriate, and shown in Note 8.

Net Expenditure

The Operating Cost Statement shows net expenditure of £34,530,547,000 which has been charged to the General Fund. Cash voted by Parliament and drawn down for the provision of Defence Capability (RfR 1), Conflict Prevention (RfR 2) and War Pensions and Allowances (RfR 3) amounting to £29,257,550,000 has been credited to the General Fund (Note 18).

Operating and Financial Review

The Operating and Financial Review is included on pages 97 to 98.

Management

Ministers who had responsibility for the Department during the year were:

Secretary of State for Defence

The Right Honourable Geoffrey Hoon, MP

Minister of State for the Armed Forces

The Right Honourable Adam Ingram, MP

Parliamentary Under Secretary of State for Defence and Minister for Defence Procurement

The Lord Bach of Lutterworth

Parliamentary Under Secretary of State for Defence and Minister for Veterans

Dr Lewis Moonie, MP (to 13 June 2003)

Ivor Caplin, MP (appointed 13 June 2003)

Composition of Defence Management Board (DMB), during the year ended 31 March 2004:

Permanent Under Secretary of State

Sir Kevin Tebbit KCB CMG

Chief of the Defence Staff

Admiral the Lord Boyce GCB OBE DL (to 1 May 2003)

General Sir Michael Walker GCB CMG CBE ADC Gen (appointed 2 May 2003)

First Sea Lord and Chief of the Naval Staff

Admiral Sir Alan West GCB DSC ADC

Chief of the General Staff

General Sir Mike Jackson KCB CBE DSO ADC Gen

Chief of the Air Staff

Air Chief Marshal Sir Peter Squire GCB DFC AFC DSc ADC FRAeS RAF (to 31 July 2003)

Air Chief Marshal Sir Jock Stirrup KCB AFC ADC FRAeS FCMI RAF (appointed 1 August 2003)

Vice Chief of the Defence Staff

Air Chief Marshal Sir Anthony Bagnall GBE KCB FRAeS RAF

Second Permanent Under Secretary of State

Ian Andrews CBE TD

Chief of Defence Procurement

Sir Robert Walmsley KCB FEng FIEE (to 30 April 2003)

Sir Peter Spencer KCB (appointed 1 May 2003)

Chief of Defence Logistics

Air Chief Marshal Sir Malcolm Pledger KCB OBE AFC BSc FRAeS RAF

Chief Scientific Adviser

Professor Sir Keith O'Nions FRS

Non-Executive members

Charles Miller Smith, Chairman of Scottish Power

Philippa Foster Back, Director of the Institute of Business Ethics

Since the end of the financial year the following changes in appointment have arisen:

Lieutenant General Kevin O'Donoghue CBE to be appointed Chief of Defence Logistics on 1 January 2005 in succession to Air Chief Marshal Sir Malcolm Pledger KCB OBE AFC BSc FRAeS RAF.

Professor Roy Anderson FRS to be appointed Chief Scientific Advisor on 4 October 2004 in succession to Professor Sir Keith O'Nions FRS.

Trevor Woolley, Finance Director, was appointed to the Board on 24 June 2004.

Remuneration of Ministers, and details of salary and pension entitlements of the members of the DMB, are shown in Note 2.3.

The Methodology of Senior Appointments

The Senior Civil Service was formed in April 1996 through an Order in Council. The recruitment principles, and their application, under which senior appointments, including those of the Permanent Under Secretary of State and Second Permanent Under Secretary of State, are made are specified in the "Commissioners' Recruitment Code", responsibility for which lies with the Civil Service Commissioners.

The Chief of Defence Procurement and the Chief Scientific Adviser are recruited on three year fixed-term appointments. The conditions covering the termination of their employment are set out in their contract documents.

The Chief of the Defence Staff, Vice Chief of the Defence Staff, Single-Service Chiefs of Staff and Chief of Defence Logistics are appointed on the recommendation of the Secretary of State for Defence to the Prime Minister. The final approval of the appointee lies with Her Majesty The Queen.

Pension Liabilities

Pension liabilities for the majority of civilian personnel and Service personnel are provided by the Civil Service Pension Scheme (CSP) arrangements and the Armed Forces Pension Scheme (AFPS) respectively. The Department makes regular payments of Accruing Superannuation Liability Charge (ASLC) into the relevant pension schemes at rates determined by the Government Actuary.

On 1 October 2002 the new CSP arrangements came into effect. Since that date all new entrants to the Department have had the option to join either the defined benefits (DB) scheme, known as "Premium", or to join the defined contributions (DC) scheme which is known as "Partnership". The previous scheme, now known as "classic", was closed to new members when the new CSP arrangements came into effect. Member contributions to Premium are 3.5% and are considered to be a general contribution to the scheme. Members in Classic continue to contribute 1.5% in respect of the Widows Pension Scheme (WPS) benefits. The Department's contributions to Partnership vary depending on the age of the individual and the amount that they contribute.

Both the Premium and Classic schemes are accounted for as Defined Contribution schemes in accordance with Treasury requirements. The pension liabilities are not included in the Department's Balance Sheet. The financial statements of these schemes are published separately.

Elements of Remuneration

Senior Civil Service and Ministers' emoluments are reviewed annually by the Review Body on Senior Salaries (SSRB). For civil servants outside the Senior Civil Service, emoluments are set on the basis of annual negotiations between the Department and the Trades Unions.

Emoluments for Service personnel are paid in accordance with rank and conditions of service and are reviewed annually by the Armed Forces Pay Review Body (AFPRB) or, for senior officers at two-star rank and above, the SSRB.

Performance and Reward

Civilian members of the DMB do not participate in any incentive/performance schemes. Their basic salary and annual increases, which could include a bonus payment, are performance related and are set by the Permanent Under Secretaries Remuneration Committee.

Pay and management arrangements for members of the SCS (one-star to three-star) reward individuals for delivery and personal achievement. These arrangements include:

- a. An objective-setting regime complementary to the Department's developing performance management system embodied in the Defence Balanced Scorecard.
- b. A performance-related incremental pay system.

Employees

The Department is committed to recruiting and retaining the best people for the job from all walks of life irrespective of race, gender or background.

Payments to Suppliers

The Department's bills, with the exception of some payments to suppliers by units locally and outside Great Britain, are paid through the Defence Bills Agency (DBA). In 2003-04, the DBA met its target of paying 99.9% of all correctly submitted bills within eleven calendar days, ensuring that the Department is in compliance with its statutory obligation under the Late Payment of Commercial Debts (Interest) Act 1998. Commercial debt interest paid by units locally during the year amounted to £336 (2002-03: £1,196).

Environmental Protection Policy

The Ministry of Defence acts as a force for good in the world, by enabling a climate that supports the pursuit of sustainable development objectives. The MoD is an operational government department and is required to manage its sustainable development aspects and impacts alongside Defence imperatives. Ensuring a better quality of life for everyone now and for future generations to come lies at the heart of the Government's Sustainable Development Strategy. The MoD is committed to these objectives in pursuit of core business.

It is the Department's intention to comply with the Government's strategy for sustainable development and to take into consideration environmental and socio-economic factors in the development of policies, projects, acquisition programmes and training activities. A Sustainable Development Steering Group has been set up to oversee the development and implementation of a Departmental Sustainable Development Strategy. A report on the Department's performance against core sustainable development indicators will be published annually.

The Department will comply with the Environmental Protection Act 1990 and Environment Act 1995 and other relevant statutory provisions and any additional requirements arising from international treaties and protocols to which the UK is a signatory. Where the Department has been granted specific exemptions, disapplications or derogations from legislation, international treaties and protocols, Departmental Standards and arrangements will be introduced which are, as far as reasonably practical, at least as good as those required by the legislation. Any powers not to apply legislation on the grounds of national security will be invoked only when such action is absolutely essential for the maintenance of operational capability.

Departmental Report

The MoD's Departmental Report which is presented to Parliament each year comprises the "Ministry of Defence Performance Report 2003-04" and "The Government's Expenditure Plans 2004-05: Ministry of Defence". The Departmental Report sets out the performance of the MoD against the objectives stated in Schedule 5 and also includes developments since the year-end, where appropriate. The Departmental Performance Report forms the first Section of the Annual Report and Accounts.

Financial Instruments

The Department does not trade or enter into any speculative transactions in foreign currencies. Forward contract commitments entered into to cover future expenditure in foreign currencies are stated in Note 28.

Provision of Information and Consultation with Employees

The MoD has a strong Whitley committee structure through which employees' representatives, in the form of recognised industrial and non industrial trades unions (TUs), are consulted on and informed of all matters likely to affect our civilian personnel. This structure is supported by formal policy and procedures for consulting and informing TUs. We also advocate the development of informal relationships with the TUs to discuss ideas together. Our policy makes clear that consulting the TUs is not a substitute for dealing with personnel direct, and vice versa. Managers and project leaders for example are encouraged to use all media available, including cascade briefings, newsletters and intranet websites/email. In respect of service personnel, the process operates through the chain of command, with no formal representation through the Trade Unions.

Auditor

The financial statements for the Department are audited by the Comptroller and Auditor General under the Government Resources and Accounts Act 2000. The Certificate and Report of the Comptroller and Auditor General on the financial statements are set out on pages 104 to 110.

Kevin Tebbit

Accounting Officer
21 September 2004

Operating and Financial Review

Last year was the first year that the Department presented the Departmental Performance Report and the Departmental Resource Accounts as a combined document, the "Annual Report and Accounts". The combined report was well received, as it brought together the non-financial performance and operational activities carried out during the year and related them to the financial outcome and the resources utilised in the year.

The operational activity during the year was again dominated by events in Iraq (Operation TELIC). The military operation that had started in March 2003 came to an end in May 2004. Since then the armed forces have been mainly engaged in various stabilisation operations and in providing much needed humanitarian assistance. The operational activities in Afghanistan and the Balkans are continuing although on a smaller scale than in the previous year. Further details of these operations are given in Section 1 of the Annual Report and Accounts.

Financial Review

The Department, for the first time since the implementation of Resource Accounting, has received a clean audit opinion on its Accounts. This is a significant achievement considering the size and complexity of the Department. One of the challenges was adapting the supply systems to provide resource based financial data; under the legacy systems only the minimum amount of financial data was held. The Department has over the last few years made significant efforts in improving these systems and the one remaining supply system issue brought forward from last year has now been resolved. The Department is for the first time able to obtain more accurate information on its stock levels and consumption. Through sound planning and control, the Department has stayed within the resources allocated to it under each of the three "Request for Resources", agreed in the Supplementary Estimates.

Net Resource Outturn

The total Net Resource Outturn was £1,002 million below the Estimate. Schedule 1 provides a summary explaining the reasons for the underspend, which is mainly due to lower than forecast non-cash costs of £674 million; the remaining £328 million is due to other costs. Of the total underspend, the Provision for Defence Capability (Request for Resources 1) accounted for £780 million, Conflict Prevention (Request for Resources 2) £180 million, and War Pensions and Allowances (Request for Resources 3) £42 million.

The Net Resource Outturn of £34,651 million was £7,362 million below last year. However, 2002-03 was an exceptional year when, some £4,000 million in the value of fixed assets was written down as a direct impact of the Quinquennial Valuation of fixed assets. The impact of the substantial write down also had the effect of reducing the depreciation charge in 2003-04 by some £1,200 million. A further £1,700 million in exceptional charges were also made in last year's accounts in respect of nuclear decommissioning provisions following a strategic review, changes in methodology carried out by BNFL, and the Quinquennial review of AWE. The balance of the reduction is accounted for by various costs, as listed in Note 3.

The Treasury standard rate for the cost of capital charge calculation was reduced from 6% to 3.5% with effect from 1 April 2003. This resulted in a reduced cost of capital charge of £2,770 million. However, there was a corresponding increase in the unwinding of interest charge relating to the discounted provisions, mainly in respect of decommissioning, which crystallised as at 1 April 2003.

Net Cash Requirement

The net cash utilised in the year was £29,338 million and was £750 million below the Estimate. The underspend is mainly due to lower cash expenditure on operations, lower than forecast capital expenditure and lower working capital expenditure.

Financial Position

The net asset value at 31 March 2004 of £81,147 million declined against last year by £291 million.

The reduction in the net asset value is largely due to the increase in the amount of provisions for liabilities and charges, as a result of recalculating the discounted provisions using a discount rate of 3.5% instead of 6% at 31 March 2003. The net impact was an increase in liabilities by some £2,400 million. This was offset by increases in fixed assets of £1,033 million and working capital of £1,073 million. The increase in working capital includes a reclassification of some £750 million, in respect of items which had been previously designated as fixed assets and now reclassified as stock.

Cash Flow

The amount drawn from the Consolidated Fund was £29,258 million. This amount was mainly utilised in financing operating activities (£23,110 million) and net capital expenditure (£5,986 million). Closing cash and bank balances were £313 million (2002-03: £416 million).

Future Developments

In July 2004, the Department announced that significant changes would be required to the force structure to meet the needs of the future, including the potential threats from terrorism. Change would also involve the level of resource capability required in the civilian work force. The changes are presently being evaluated and, when implemented, will have a significant impact on the results in future years.

Statement of Accounting Officer's Responsibilities

Under the Government Resources and Accounts Act 2000, the Department is required to prepare resource accounts for each financial year, in conformity with a Treasury direction, detailing the resources acquired, held, or disposed of during the year and the use of resources by the Department during the year.

The resource accounts are prepared on an accruals basis and must give a true and fair view of the state of affairs of the Department, the net resource Outturn, resources applied to objectives, recognised gains and losses, and cash flows for the financial year.

HM Treasury has appointed the Permanent Head of the Department as Accounting Officer of the Department, with responsibility for preparing the Department's accounts and for transmitting them to the Comptroller and Auditor General.

In preparing the accounts the Accounting Officer is required to comply with the *Resource Accounting Manual* (RAM) prepared by HM Treasury, and in particular to:

- Observe the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- Make judgements and estimates on a reasonable basis;
- State whether applicable accounting standards, as set out in the RAM, have been followed, and disclose and explain any material departures in the accounts; and
- Prepare the accounts on a going concern basis.

The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which an Accounting Officer is answerable, for keeping proper records and for safeguarding the Department's assets, are set out in the Accounting Officers' Memorandum issued by HM Treasury and published in *Government Accounting*.

Statement on Internal Control

1. Scope of responsibility

As Accounting Officer, I have responsibility for maintaining a sound system of internal control that supports the achievement of Departmental policies, aims and objectives, set by the Department's Ministers, whilst safeguarding the public funds and Departmental assets for which I am personally responsible, in accordance with the responsibilities assigned to me in Government Accounting.

During the Financial Year 2003/04, the Department's outputs were delivered through 11 Top Level Budget areas, each managed by a military or civilian Top Level Budget (TLB) Holder, together with 5 Trading Fund Agencies and 7 Non-Departmental Public Bodies (NDPB) with delegated responsibilities. Included within the TLBs are 30 (2002-03: 31¹) on-vote Defence Agencies whose Chief Executives are responsible for producing annual accounts which are laid before Parliament but which also form part of the Departmental Resource Accounts. TLB Holders operate within a framework of responsibilities delegated by me and to assist me in assessing the adequacy of control arrangements across the Department, TLB Holders provide their own Statements of Internal Control to me on an annual basis including the Agencies for which they are responsible. The MoD Trading Funds fall outside the Departmental Accounting Boundary and their Chief Executives are Accounting Officers in their own right. They therefore publish their own SICs together with their Annual Accounts. Although sponsored by the Department, the 7 NDPBs also fall outside the Departmental Boundary and their accounts are published separately. With the exception of the Oil and Pipelines Agency (OPA), the NDPBs operate within a strategic control framework contained in a financial memorandum agreed between their respective Boards of Trustees and the Department. The OPA has a Board of Directors on which the Department is represented.

Ministers are involved in the delivery of outputs, including the management of risks to delivery, through the Defence Council which is chaired by the Secretary of State for Defence and includes all the senior executive members of the Defence Management Board. Ministers also chair a variety of internal Boards which review the performance of the Trading Funds, the primary on-vote Agencies and other elements of MoD business such as Environment and Safety, and Estates. In particular, 4 Trading Funds (the Defence Aviation Repair Agency, the Army Base Repair Organisation, the Defence Science and Technology Laboratory (Dstl), and the UK Hydrographic Office) together with the Defence Procurement Agency (DPA) report to Advisory Boards chaired by MoD Ministers. The Met Office, which is also a Trading Fund, reported to the UK Met Board chaired by the 2nd PUS². Ministers are also consulted on all key decisions affecting defence, including major investment decisions and on operational matters. The Chief of Defence Staff is the Secretary of State's principal advisor on military operations and is responsible for the maintenance of military operational capability and for the preparation and conduct of military operations, including risks to successful outcomes.

2. The purpose of the system of internal control

The system of internal control is designed to manage risk to a reasonable level rather than to eliminate all risk of failure to achieve policies, aims and objectives; it can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify

¹ On 1 April 2003 the Defence Medical Education & Training Agency was formed, subsuming the responsibilities of the Defence Medical Training Organisation and the Defence Secondary Care Agency.

² From 27 July 2004 the UK Met Board became the Met Office Owner's Council, chaired by the Under Secretary of State.

and prioritise the risks to the achievement of Departmental policies, aims and objectives, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically. The system of internal control has been in place in the Department for the year ended 31 March 2004 and up to the date of approval of the annual report and accounts, and accords with Treasury guidance.

3. Capacity to handle risk

Active management of risk is fundamental to the effective achievement of Defence objectives, and is central to the way business is conducted within the Department. It informs operational decision making, contingency planning, investment decisions and the financial planning process. Risk forms an integral element of the Defence Management Board's performance reviews. Guidance on the Department's approach to risk is detailed in a Joint Service Publication³, which is periodically reviewed and updated. This sets out the Department's corporate governance and risk management policy statement and strategy to be cascaded down through TLB Holders, and provides extensive guidance to staff on definitions, criteria and methods available for risk assessment and management. It is made available to all personnel in either hard copy or via the Department's intranet. Individual training, at both awareness and practitioner level, is available to all staff via the Department's in-house training provider.

Across the Department a network of Risk Improvement Managers (RIMs) has been established. The aim of the network is to share good practice, helping those involved in improving risk management in their area to learn from others across the Department, and also drawing from the work being carried out as part of the Government-wide programme to improve the handling of risks to Government objectives.

4. The risk and control framework

The Department's Performance Management System provides the strategic framework for the consideration of risks within the Defence Balanced Scorecard and lower level scorecards, offering a starting point for the identification, evaluation, control and reporting of risk against a balanced assessment of Departmental objectives. Key Departmental objectives, performance indicators and targets are defined annually by the Defence Management Board (DMB) and cascaded to TLB Holders through Service Delivery Agreements. Performance is monitored and discussed quarterly at DMB and lower level management board meetings, including explicit consideration of key risks.

The Department's risk appetite is determined through the advice on operations given to Ministers, through decisions taken as part of the Department's annual planning round including assessing any gaps against Planning Assumptions as set out in the Defence White Paper, and through the limits and controls placed on individual investment projects as part of the Department's Investment Approval process.

5. Review of effectiveness

As Accounting Officer, I have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the executive managers within the Department who have responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports. I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the Defence Management Board and the Defence Audit Committee and a plan to address weaknesses and ensure continuous improvement of the system is in place.

³ JSP 525 *Corporate Governance and Risk Management 2nd Edition May 2004*.

The following processes are in operation in order to maintain and review the effectiveness of the system of internal control:

- A Defence Management Board (DMB), which meets monthly to manage the plans, performance and strategic direction of the Department, which comprises the senior members of the Department and has two external independent members.
- A Defence Audit Committee (DAC), chaired by an external independent member of the DMB, which has adopted a risk-based approach to internal control and is placed at the heart of the assurance process, co-ordinating the activities of internal audit, and drawing on reports from specialist assurance bodies, including:
 - Defence Environment and Safety Board
 - Departmental Security Officer
 - Defence Internal Audit
 - Director General Financial Management
 - Director of Operational Capability
 - Defence Fraud Analysis Unit
 - Scientific & Technical Director
 - National Audit Office
- A Departmental risk register, supported by operational-level risk registers, which complements the Defence Balanced Scorecard. The Departmental risk register has been reviewed and endorsed by both the DAC and the DMB.
- Through TLB Holders, a cascaded system for ensuring compliance with legal and statutory regulations. Each TLB holder is supported by an Audit Committee, which includes non-executive directors and at which representatives from the internal and external auditors are present. Like the DAC these committees have refocused their activities to provide advice on wider-business risk and assurance processes.
- A developing Business Management System through which responsibility for the effective and efficient operation of the key pan-Departmental processes, such as Planning, Human Resources and Procurement, including the identification of risks within these processes and the maintenance of effective controls to manage them, is assigned to functional heads or process owners. Process Owners report directly to the Defence Management Board.
- Through TLB Holders, a cascaded system for ensuring that business continuity plans are in place, and that these plans are tested on a regular basis. Following a revamp of the Department's business continuity management policy⁴, an in-year review by the Directorate General of Safety and Security was undertaken to ascertain how the policy is being adopted across the Department, what improvements are planned and to identify specific areas of risk and the measures being taken to mitigate those risks. The review revealed that all business continuity plans currently in place had been at minimum desktop tested and that there are no significant internal control problems.

⁴ Revised policy and guidance issued in Joint Service Policy 503 Business Continuity Management, 2nd Edition, published May 2003, and Defence Council Instruction (General) 160/03 dated 20 June 2003.

- An annual risk-based programme of internal audit provided by Defence Internal Audit (DIA), who are the primary source of independent assurance, which is complemented by the activity of the Directorate of Operational Capability (DOC), which provides independent operational audit and assurance to the Secretary of State and the Chief of Defence Staff. On the basis of the audit work conducted during the year, DIA offered Substantial Assurance that the systems of internal control, risk management and governance reviewed are operating effectively.
- Annual and Quarterly Reports providing measurable performance indicators and more subjective assessments on the Health of Financial Systems from all TLB Holders and key functional specialists. Improvements have continued to be made to our financial control during the year. The Department has delivered its outputs within the resources voted by Parliament and the Treasury's expenditure limits despite the additional workload generated by Operation TELIC and the migration to a new accounting system. The remaining NAO concern on Supply Systems has now been satisfactorily resolved with the result that the Department has for the first time achieved a true and fair audit opinion.
- Centres of Excellence for project and programme management in key areas - including Change, Equipment and Estates, integrating Office of Government Commerce (OGC) processes, tools and structures into existing Departmental management and control processes - to ensure that high-risk mission-critical projects and programmes carried out by the Department do not suffer from any of the common causes of failure identified by the OGC and the National Audit Office.
- Senior Responsible Owners across the Department who are personally responsible for delivering major programmes and their benefits to cost and time in line with best Office of Government Commerce practice.
- A dedicated team to co-ordinate, and appropriate mechanisms to strengthen, the management of scientific risks, particularly to Service personnel health, and in health, safety and environmental matters.
- Association of the Department's Directorate of Management Consultancy Services with the broader assurance community with their tasking flowing from the identification of business risk.
- A change programme to address the key risks that the introduction of the general right of access under FOI from January 2005 presents to the organisation. Stakeholders from across the department have been involved and an effective governance structure put in place. A maturity model has been used to highlight how the constituent parts of the department are progressing and as a diagnostic tool for the department to feed into performance management systems.

Kevin Tebbit

Accounting Officer

21 September 2004

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

I certify that I have audited the financial statements on pages 111 to 168 under the Government Resources and Accounts Act 2000. These financial statements have been prepared under the historical cost convention as modified by the revaluation of certain fixed assets and stocks and the accounting policies set out on pages 119 to 125.

Respective responsibilities of the Accounting Officer and Auditor

As described on page 99, the Accounting Officer is responsible for the preparation of the financial statements in accordance with the Government Resources and Accounts Act 2000 and Treasury directions made thereunder and for ensuring the regularity of financial transactions. The Accounting Officer is also responsible for the preparation of the other contents of the Annual Report and Accounts. My responsibilities, as independent auditor, are established by statute and guided by the Auditing Practices Board and the auditing profession's ethical guidance.

I report my opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Government Resources and Accounts Act 2000 and Treasury directions made thereunder, and whether in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. I also report if, in my opinion, the Annual Report including the annual performance report is not consistent with the financial statements, if the Department has not kept proper accounting records, or if I have not received all the information and explanations I require for my audit.

I read the other information contained in the Annual Report and Accounts, and consider whether it is consistent with the audited financial statements. I consider the implications for my certificate if I become aware of any apparent misstatements or material inconsistencies with the financial statements.

I review whether the statement on pages 100 to 103 reflects the Department's compliance with Treasury's guidance on the Statement on Internal Control. I report if it does not meet the requirements specified by Treasury, or if the statement is misleading or inconsistent with other information I am aware of from my audit of the financial statements. I am not required to consider, nor have I considered whether the Accounting Officer's Statement on Internal Control covers all the risks and controls. I am also not required to form an opinion on the effectiveness of the Agency's corporate governance procedures or its risk and control procedures.

Basis of audit opinion

I conducted my audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board except that the scope of my work was limited as explained below. An audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of financial transactions included in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Department in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Department's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by error, or by fraud or other irregularity and that, in all material respects, the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

In forming my opinion I have also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In my opinion:

- the financial statements give a true and fair view of the state of affairs of the Ministry of Defence at 31 March 2004 and of the net resource outturn, resources applied to objectives, recognised gains and losses and cash flows for the year then ended, and have been properly prepared in accordance with the Government Resources and Accounts Act 2000 and directions made thereunder by Treasury; and
- in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

My Report on these financial statements is at page 106.

John Bourn

Comptroller and Auditor General
29 September 2004

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

Section 1: Summary

1 The Ministry of Defence (the Department) is required by Directions issued by the Treasury to prepare annual Resource Accounts. The Resource Accounts, drawn up on an accruals basis, should be prepared in accordance with the Treasury's *Resource Accounting Manual* and should give a true and fair view of the state of affairs of the Department and of its net resource outturn, recognised gains and losses and cashflows for the year.

2 In producing its Resource Accounts the Department faces a number of challenges. It undertakes a wide range of complex functions and holds a vast range of assets. Some of these assets are held by contractors for manufacture and repair purposes. It has many old information systems which although adequate for the purposes they were designed for, are not suited in all respects to the production of accurate and timely accruals based information, particularly during the escalation of military operations. The Department has therefore had to invest considerable efforts in implementing resource accounting and budgeting, both in IT and staffing.

3 The Department has made significant efforts to improve the standard of its financial accounting information over the last five years. I qualified my audit opinion on the 2002-2003 resource accounts because I was unable to confirm some figures in the operating cost statement in respect of consumption charges for certain stock and fixed assets generated by the Defence Logistics Organisation's Air environment. The Department has continued over this last year to make strenuous efforts to secure further improvements. In Section 2 of my Report I describe these efforts in more detail and explain why as a result I have concluded that this year for the first time the Department's resource accounts are robust enough to support a true and fair opinion.

4 The Treasury's *Resource Accounting Manual* requires that losses and special payments be reported in Departments' Resource Accounts. The Ministry of Defence has faced significant changes in its expenditure programmes over recent years because of a variety of factors, including changes in threat and advances in weapons technology and the scale of change in organisational structures. These factors have led to many of the losses and special payments recorded in Note 29 to the 2003-2004 Resource Accounts. In Section 3 of my Report I consider some of the more significant losses.

5 In Section 4 of my Report I confirm that according to Departmental records the maximum numbers of military personnel maintained during 2003-2004 for the Naval, Army and Air Force Services in all active and reserve categories were within the numbers voted by Parliament.

6 The Department continues to demonstrate a strong and effective grip on the accounts production process. For 2003-2004, it has again submitted Resource Accounts for audit in line with the timetable agreed with my staff and the Treasury and it has accelerated their finalisation and publication. When compared with the quality of the Department's first Resource Accounts for 1999-2000, on which I placed a disclaimer covering a range of accounting deficiencies, the Department has consistently made good progress during the last four years in improving the quality of its accounts. As a result this year the Department has successfully cleared the one remaining substantive issue which was the basis for the qualification of my audit opinion last year. This is a significant achievement but the Department recognises that it has more to do to get the maximum benefit from the Resource Accounting and Budgeting regime. The Department assures me it is fully aware of what remains to be done and is committed to securing further improvements. My staff will continue to work closely with the Department in this task.

Section 2: Is the Department still making good progress to implement Resource Accounting effectively?

7 In my Report on the 2002-2003 Accounts¹ I explained my reasons for qualifying my audit opinion. I was unable to confirm whether stock and fixed asset accounting transactions generated by the Defence Logistics Organisation's Air environment were complete or correctly recorded. The Department has now made sufficient progress on this issue such that I am able to remove my qualification in this regard.

Stock and fixed asset accounting transactions generated by the Defence Logistics Organisation's Air environment are more robust

8 In my Report on the 2002-2003 accounts I noted the continuing problems the Department had with stock inventory systems which were not designed to provide stock accounting data for accruals based financial accounts. In particular, the supply system for the Defence Logistics Organisation's Air environment generated data that could not be wholly supported. Then, as now, the stock accounting system compares each month the opening and closing values with the movements generated by the stock inventory system. Where there is a difference a reconciling balance is automatically created. This 'autobalance' entry ensures that the accounts reflect the stock inventory system but in previous years there had been no audit trail to support it.

9 Throughout 2003-04, the Defence Logistics Organisation continued to investigate the causes of autobalance. Some of the causes identified arose from technical deficiencies within the software programming. For example, spurious transactions generated when both the definition of quantity and the unit price changed simultaneously in the stock management system. The Defence Logistics Organisation has improved the mapping of transactions from the inventory system through to the accounting system, thus reducing the need for the intervention of autobalance. There has also been an educational programme for supply system users to reduce the level of incomplete and incorrect data input, which was another major cause of autobalance transactions.

10 As a result of these actions, the Defence Logistics Organisation has reduced the net credit to the operating cost statement arising from autobalance to £181 million in 2003-04 (in 2002-2003 it was some £1,128 million). More significantly, the Defence Logistics Organisation has for the first time established an audit trail for all autobalance transactions that provides sufficient evidence to support the validity and accuracy of these transactions. Audit testing has shown that the autobalance mechanism functions as an effective and valid accounting tool. It is in this regard that I have been able to remove my qualification.

¹ MoD: Departmental Resource Accounts 2002-2003 HC 1125 Session 2002-2003: 30 October 2003

11 In order to further improve the effectiveness of its business decisions, which in a high degree depend upon the quality of its accounting data, the Defence Logistics Organisation is continuing with its programme of reducing the technical and procedural causes of autobalance.

Other developments in Resource Accounting and the disclosure of financial information

The Department has reported some £1 billion net additional resource costs were incurred on operations in Iraq during 2003-04

12 Note 27 to the Resource Account summarises the financial impact of operation TELIC during 2003-2004. TELIC is the UK name for military operations in Iraq. The total costs to date of the operation are summarised below.

£m	2002-03	2003-04	Total
Resource costs	629	1,051	1,680
Capital expenditure	218	260	478
Total	847	1,311	2,158

13 In accordance with the accounting principles agreed with HM Treasury, the Department has identified these costs on the basis of net additional costs. Expenditure such as normal wages and salaries of armed forces and civilian personnel are excluded as these would have been incurred anyway and the costs of training and exercises which have been cancelled because of the operational commitment are deducted.

14 The Department's chart of accounts is not designed to record automatically the cost of individual operations. The Department therefore undertook a specific review to determine the additional resource costs of operation TELIC attributable to the 2003-2004 account. My staff have reviewed the Department's estimates of the cost of operation TELIC up to 31 March 2004 and concluded that they are robust.

15 Some of the remaining stock and fixed assets sent to Iraq are still in use there for peacekeeping purposes. Until all unused stock and fixed assets are returned to the United Kingdom the Department will be unable to make a comprehensive assessment of stock consumption and the level of asset impairment in order to determine the full cost of operation TELIC.

16 I reported last year² that TELIC is the first major conflict where the Department has accounted for a military operation on a resource basis and that this had generated a number of accounting issues not encountered in previous operations managed under a cash accounting regime. These issues have continued to have an impact in 2003-04 and include the following:

- calculating the correct level of stock consumption to report in the resource accounts;
- the loss or impairment of fighting and other equipments which have to be recognised in the correct accounting period on an accruals basis;
- assets acquired quickly to support operations (Urgent Operational Requirements) need to be brought to account correctly.

17 The Department is committed to working in consultation with my staff to further refine its accounting policies and systems in these areas.

² MoD: Departmental Resource Accounts 2002-2003 HC 1125 Session 2002-2003: 30 October 2003

Section 3: The Department has reported significant losses and special payments

18 The Department's expenditure programmes are subject to many changes in requirements because of advances in weapons technology; changes in threat and the pace and scale of changes in organisational structures. These changes can result in the Department having to abandon procurement or development projects before the equipments are introduced into service or write off the value of assets no longer required.

19 The Treasury gives departments delegated authority to write off such expenditure as a loss or special payment after careful appraisal of all the facts, but requires departments to bring them to Parliament's attention at the earliest opportunity. Nevertheless, investigation of the circumstances can take some time. Where final details cannot be reported this may be noted as an advisory loss in departmental resource accounts.

20 The table below summarises the value of the resulting losses and special payments reported by the Department in the last four years and shows that reported losses have increased significantly in 2003-04. Note 29 of the Department's Resource Accounts for 2003-2004 discloses details of the losses, special payments and gifts.

£000	Losses	Special Payments
2000-01	78,950	180,820
2001-02	42,072	74,262
2002-03	131,084	129,118
2003-04	460,945	98,124

21 The Department has also identified some £442 million of losses incurred in previous years and not previously reported. I highlight below some of the more significant cases recorded in the Note.

The Department has incurred significant constructive losses

22 HM Treasury's *Government Accounting* defines a constructive loss as one where, for example, services are correctly ordered, delivered or provided, and are paid for as being in conformity with the order, but which owing to a change of policy or similar reason prove not to be needed or to be less useful than when the order was placed.

Nuclear submarine facilities at Devonport

23 In my Report on the 2002-2003 Accounts³, I noted that the Department had given advance notification of a constructive loss of £287 million relating to nuclear submarine facilities at Devonport and explained the reasons for the loss. This amount has been confirmed and formally reported as a constructive loss in the 2003-04 accounts.

Multi Role Armoured Vehicle (MRAV) Programme

24 The Department withdrew from the MRAV Programme, a collaborative project with Germany and the Netherlands, during 2003 and has reported a constructive loss of £48 million. This was due to changing capability requirements, with increased emphasis placed on the ability of the armed forces to meet the requirements of rapid deployment and expeditionary operations. The MRAV programme did not meet these requirements, leading to the Department's decision to withdraw from it.

³ MoD: Departmental Resource Accounts 2002-2003 HC 1125 Session 2002-2003: 30 October 2003

25 A new national programme, the Future Rapid Effect System (FRES) will meet the requirement for lighter more easily deployable armoured vehicles. These vehicles will also be integrated with the new framework of network centric capability.

The Department has given advance notification of significant losses

26 HM Treasury's *Government Accounting* requires that losses and special payments should be brought to the attention of Parliament at the earliest opportunity. Notification is separate from the accounting treatment, which will depend on the nature of the loss or special payment. A loss should be noted in the accounts even if it may be reduced by subsequent recoveries. The Department has provided advance notification for the following significant loss.

Chinook MK3 Helicopters Impairment

27 A loss of £205m arose due to the impairment of eight Chinook MK3 Helicopters. The impairment arose as it was established that, although the terms of the contract had been met, these helicopters did not meet operational requirements and could not acquire Military Aircraft Release.

28 Significant modifications to the avionics software are required to enable the helicopters to be of use operationally and it is not now anticipated that the helicopters will enter service until mid 2007. I examined these issues in more detail in my report earlier this year⁴.

Section 4: Ministry of Defence – Votes A

29 The Ministry of Defence's Votes A is presented annually to Parliament to seek statutory authority for the maximum numbers of personnel to be maintained for service with the armed forces. Note 33 to the Accounts shows that the maximum numbers maintained during 2003-04 for the Naval, Army and Air Force Services in all active and reserve categories were within the numbers voted by Parliament. My staff have been provided with strength returns to support this Note to the financial statements.

John Bourn

Comptroller and Auditor General
29 September 2004

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⁴ Battlefield Helicopters HC486 Session 2003-04: 1 April 2004

Schedule 1

Summary of Resource Outturn

for the year ended 31 March 2004

							Net Total compared to Estimate Savings/ (Excess)
	Estimate			Outturn			
	Gross Expenditure 1	A-in-A* 2	Net Total 3	Gross Expenditure 4	A-in-A* (note 4) 5	Net Total 6	7
	£000	£000	£000	£000	£000	£000	£000
Request for resources 1	34,459,419	1,377,823	33,081,596	33,679,847	1,377,823	32,302,024	779,572
Request for resources 2	1,413,610	–	1,413,610	1,233,155	–	1,233,155	180,455
Request for resources 3	1,158,005	–	1,158,005	1,116,047	–	1,116,047	41,958
Total resources	37,031,034	1,377,823	35,653,211	36,029,049	1,377,823	34,651,226	1,001,985
Non operating cost A-in-A			367,798			367,798	0
Net cash requirement			30,087,210			29,337,645	749,565
Outturn in Respect of Prior Year							
The corresponding figures for 2002-03 outturn were as follows:							
Total Resources						42,013,684	
Non operating cost A-in-A						373,756	
Net cash requirement						26,991,365	
*Appropriations-in-Aid (A-in-A)							
Summary of Income payable to the Consolidated Fund							
	Note	Forecast 2003-04		Outturn 2003-04			
		Income £000	Receipts £000	Income £000	Receipts £000		
Total	4	–	–	258,004	258,004		
Reconciliation of resources to cash requirement							
	Note	Estimate £000		Outturn £000	Savings/ (Excess) £000		
Net total resources	Sch 2	35,653,211		34,651,226	1,001,985		
Capital:							
*Purchase of fixed assets:							
– RfR 1	8/9	6,435,770		6,321,438	114,332		
– RfR 2	8/9	334,000		260,275	73,725		
– RfR 1 Capitalised provisions	8/9	–		(99,276)	99,276		
New loans to the Trading Funds	10	–		19,200	(19,200)		

The notes on pages 119 to 168 form part of these financial statements.

	Note	Estimate £000	Outturn £000	Savings/ (Excess) £000
Non operating cost A-in-A:				
Proceeds on sale of fixed assets	8/9/3	(355,371)	(481,298)	125,927
Excess non-operating costs Appropriation-in-Aid payable to the Consolidated Fund		–	137,325	(137,325)
Repayment of loans made to the Trading Funds and QinetiQ after deducting loan repayments treated as CFERs amounting to £4,213,977 shown against Outturn	10	(12,427)	(23,825)	11,398
*Repayment of Loans from the National Loans Fund	Sch 4	–	1,375	(1,375)
Accruals adjustments:				
Non-cash transactions-				
Included in operating costs	Sch 4	(7,934,719)	(7,124,595)	(810,124)
Included in net interest payable	6	(2,467,307)	(2,609,205)	141,898
Capitalised provisions shown above		–	99,276	(99,276)
		(10,402,026)	(9,634,524)	(767,502)
Cost of capital charge	18	(2,676,403)	(2,769,726)	93,323
		(13,078,429)	(12,404,250)	(674,179)
*Changes in working capital other than cash	Sch 4	621,756	422,188	199,568
*Use of provisions for liabilities and charges	17	488,700	539,167	(50,467)
Adjustment for movements on cash balances in respect of collaborative projects	14	–	(5,900)	5,900
Net cash requirement	Sch 4	30,087,210	29,337,645	749,565
* Stated in accordance with Schedule 1 requirement to include accruals within the movements in the year				

The notes on pages 119 to 168 form part of these financial statements.

Explanation of the variation between estimate and outturn (net total resources)

The Department's underspend against total net resources was caused by lower than expected conflict prevention costs under RfR2, a small underspend on war pensions under RfR3 and lower than forecast non-cash depreciation and cost of capital charges following management action across the Department to dispose of surplus assets and the impact of the Quinquennial Review (QQR) of Fixed Assets carried out towards the end of Financial year 2002-03. In the QQR there were fewer downward valuations of assets than expected, resulting in smaller accelerated depreciation charges, and the lives of many assets were extended thereby reducing associated annual depreciation costs. As part of the normal course of business resources need to be reallocated and redistributed between TLB holders as and when required in order to optimise the use of those resources in the generation of military capability and its effective use on operations. This process contributed to the in-year shortfalls and excesses shown against some of the TLB Holders. These offset each other, with no material impact on the Department's Total Resources.

Analysis of the costs of operations conducted during the year is shown in Note 27.

Explanation of the variation between estimate and outturn (net cash requirement)

Creditor and accrual balances are difficult to estimate due to uncertainties over the timing of supplier invoicing and therefore the timing of cash payments cannot be accurately predicted. In the event more goods and services were accrued due to later than anticipated presentation of bills by creditors. This had the effect of less cash being paid out than forecast when the Spring Supplementary Estimates were prepared.

Schedule 2

Operating Cost Statement

for the year ended 31 March 2004

	Note	2003-04 £000	2002-03 £000
Staff costs	2	10,435,157	9,969,242
Other operating costs	3	20,126,927	27,840,791
Gross operating costs		30,562,084	37,810,033
Operating income	5	(1,412,306)	(1,357,700)
Net operating cost before interest		29,149,778	36,452,333
Net interest payable	6	2,611,043	266,532
Cost of capital charge	18	2,769,726	5,074,726
Net operating cost		34,530,547	41,793,591
Net resource Outturn	7	34,651,226	42,013,684

Statement of Recognised Gains and Losses

for the year ended 31 March 2004

	Note	2003-04 £000	2002-03 £000
Net gain on revaluation of fixed assets and stocks	19	(2,473,614)	(4,463,447)
Receipts of donated assets and (gain) on revaluation	19	32,702	(521,653)
Prior year adjustments		–	152,917
Recognised gains during the year		(2,440,912)	(4,832,183)

The results shown above are in respect of continuing activity.

The notes on pages 119 to 168 form part of these financial statements.

Schedule 3

Balance Sheet

as at 31 March 2004

	Note	31 March 2004		31 March 2003	
		£000	£000	£000	£000
Fixed Assets					
Intangible assets	8	20,186,743		19,437,608	
Tangible fixed assets	9	66,737,257		66,444,536	
Investments	10	420,838		429,678	
			87,344,838		86,311,822
Current Assets					
Stocks and work-in-progress	12	6,318,224		5,337,125	
Debtors	13	2,675,419		2,201,652	
Cash at bank and in hand	14	312,564		415,928	
		9,306,207		7,954,705	
Creditors: amounts falling due within one year	15	5,662,598		5,383,850	
Net current assets			3,643,609		2,570,855
Total assets less current liabilities			90,988,447		88,882,677
Creditors: amounts falling due after more than one year	16	451,649		450,333	
Provisions for liabilities and charges	17	9,389,690		6,994,227	
			9,841,339		7,444,560
Net assets			81,147,108		81,438,117
Taxpayers' equity					
General fund	18		64,028,508		65,445,156
Revaluation reserve	19		15,396,444		14,181,634
Donated assets reserve	19		1,722,156		1,811,327
			81,147,108		81,438,117

Kevin Tebbit

Accounting Officer

21 September 2004

The notes on pages 119 to 168 form part of these financial statements.

Schedule 4

Cash Flow Statement

For the year ended 31 March 2004

	Note	2003-04 £000	2002-03 £000
Net cash outflow from operating activities before interest	A	23,110,005	21,165,066
Returns on investments and servicing of finance	B	(7,225)	4,363
Net capital expenditure and financial investment	C	5,977,172	5,647,360
Payments to the Consolidated Fund		279,587	533,726
Financing from the Consolidated Fund	14	(29,257,550)	(27,136,321)
Repayment of loans from the National Loans Fund		1,375	1,559
Decrease in cash at bank and in hand	14	103,364	215,753
Notes to the cash flow statement:			
A. Net cash outflow from operating activities before interest			
Net operating cost before interest	Sch 2	29,149,778	36,452,333
Non-cash transactions:			
– Depreciation and amortisation charges	3	(5,719,358)	(6,981,455)
– Impairment in value of fixed assets	3	(299,009)	(5,388,224)
– Provisions to reduce value of stock to its net realisable value	3	72,345	(111,125)
– Stocks written-off – net	3	(528,120)	(321,811)
– Auditors' remuneration	3	(3,150)	(3,405)
– Surplus/(deficit) arising on disposal of tangible fixed assets	3	71,725	45,260
– Surplus/(deficit) arising on disposal of investments	3	–	(8,397)
– Fixed Assets written off – net	3	(26,017)	(101,604)
– Fixed Asset investment written off	3	–	(219,886)
– Capital project expenditure written off	3	(268,310)	(584,928)
– Movement in provisions for liabilities and charges (excluding capitalised provisions)	17	(424,701)	(2,039,490)
		(7,124,595)	(15,715,065)
Dividends received from Trading Fund	5	8,902	8,587
Adjustments for movements in working capital other than cash			
– Increase/(decrease) in stocks/WIP		757,323	(26,645)
– Increase/(decrease) in debtors		83,431	540,276
– (Increase)/decrease in creditors		(206,831)	(507,279)
		633,923	6,352
Paid against provisions for liabilities and charges		441,997	412,859
		23,110,005	21,165,066
B. Returns on investments and servicing of finance			
Dividends received from Trading Fund	5	(8,902)	(8,587)
Interest received		(28,125)	(21,704)
Interest paid		2,639,007	282,357
Deduct: Unwinding of discount on provisions for liabilities and charges	6	(2,609,205)	(247,703)
		29,802	34,654
		(7,225)	4,363

The notes on pages 119 to 168 form part of these financial statements.

	Note	2003-04 £000	2002-03 £000
C. Analysis of capital expenditure and financial investment			
Acquisition of fixed assets		6,467,310	6,116,938
Proceeds on disposal of tangible fixed assets		(481,298)	(404,774)
Proceeds on disposal of investments		–	(39,427)
		<u>5,986,012</u>	<u>5,672,737</u>
Repayment of loans made to the Trading Funds and QinetiQ	10	(28,040)	(59,577)
Loans made to Trading Funds	10	19,200	34,200
		<u>5,977,172</u>	<u>5,647,360</u>
Analysis of Financing			
Parliamentary Funding from the Consolidated Fund (Supply)	14	29,257,550	27,136,321
(Increase)/decrease in cash at bank and in hand during the year	14	103,364	215,753
Consolidated Fund Extra Receipts (CFERs) received and not paid over		222,659	90,437
Consolidated Fund Extra Receipts (CFERs) received in prior year paid over		(134,737)	(69,430)
Part proceeds of certain fixed assets payable to Consolidated Fund		–	44,300
Grant drawn in the previous year and not spent, repaid to the Consolidated Fund during the year		(105,291)	(420,321)
Adjustment for movements on cash balances in respect of collaborative projects		(5,900)	(6,000)
Adjustment for Machinery of Government change during the year		–	305
Net cash requirement	Sch 1	<u>29,337,645</u>	<u>26,991,365</u>
Amount of grant actually issued to support the net cash requirement = £29,257,550,000.00			

The notes on pages 119 to 168 form part of these financial statements.

Schedule 5

Resources By Departmental Aim And Objectives

for the year ended 31 March 2004.

Aim

The principal activity of the Department is to deliver security for the people of the United Kingdom and the Overseas Territories by defending them, including against terrorism; and to act as a force for good by strengthening international peace and stability.

In pursuance of this aim, the Department has the following objectives:

	2003-04			2002-03		
	Gross £000	Income £000	Net £000	Gross £000	Income £000	Net £000
Objective 1: Achieving success in the tasks we undertake	3,818,272	(336,995)	3,481,277	3,752,347	(277,683)	3,474,664
Objective 2: Being ready to respond to the tasks that might arise	27,796,553	(1,019,105)	26,777,448	34,711,064	(1,016,998)	33,694,066
Objective 3: Building for the future	3,211,981	(56,206)	3,155,775	3,487,027	(60,547)	3,426,480
	34,826,806	(1,412,306)	33,414,500	41,950,438	(1,355,228)	40,595,210
Paying war pensions and allowances	1,116,047	–	1,116,047	1,200,853	(2,472)	1,198,381
Total	35,942,853	(1,412,306)	34,530,547	43,151,291	(1,357,700)	41,793,591

See additional details in Note 26.

The notes on pages 119 to 168 form part of these financial statements.

Notes to the Accounts

1. Statement of Accounting Policies

Introduction

1.1 These financial statements have been prepared in accordance with the generic Accounts Direction issued by HM Treasury under reference DAO(GEN)2/04 on 30 January 2004 and comply with the requirements of HM Treasury's Resource Accounting Manual (RAM). In order to reflect the particular circumstances of the Department, the following exceptions to the RAM have been made:

The Operating Cost Statement is not segmented into programme and non-programme expenditure, as agreed with HM Treasury.

The Department's fixed assets are not analysed using the categories set out in the RAM. The different categorisation of the fixed assets became effective from the year 2002-03, but dispensation from this new requirement has been granted by HM Treasury until 2004-05. The Department is on schedule to implement these changes for the 2004-05 Accounts.

Accounting Convention

1.2 These financial statements are prepared on an accruals basis under the historical cost convention, modified to include the revaluation of certain fixed assets and stocks.

Basis of preparation of Departmental Resource Accounts

1.3 These financial statements comprise the consolidation of the Department, its Defence Supply Financed Agencies and those Advisory NDPBs sponsored by the Department which are not self-accounting. The Defence Agencies and the Advisory NDPBs sponsored by the Department are listed in Note 31.

1.4 Five of the Department's agencies are established as Trading Funds. They therefore fall outside Voted Supply and are subject to a different control framework. Consequently, the Department's interests in the Trading Funds are included in the financial statements as fixed asset investments. Executive NDPBs operate on a self-accounting basis and are not included in the consolidated accounts. They receive grant-in-aid funding from the Department which is treated as an expense in the Operating Cost Statement.

1.5 The Department's interest in QinetiQ, a Self-Financing Public Corporation, is included in the financial statements as a fixed asset investment.

1.6 The Armed Forces Pension Scheme (AFPS) is not consolidated within these financial statements. Separate accounts are prepared by the AFPS.

1.7 Machinery of Government changes which involve the merger of two or more Departments into one new Department, or the transfer of functions or responsibility of one part of the public service sector to another, are accounted for using merger accounting in accordance with the Financial Reporting Standard (FRS) 6.

Net Operating Costs

1.8 Costs are charged to the Operating Cost Statement in the period in which they are incurred and matched to any related income. Costs of VAT recoverable from Contracted-Out Services are included net of related VAT. Other costs are VAT inclusive, although a proportion of this VAT is recovered via a formula agreed with HM Customs and Excise. Surpluses and deficits on disposal of fixed assets and stock are included within Other Operating Costs (Note 3).

1.9 Income from services provided to third parties is included in operating income, net of related VAT. Dividends are included in the operating income in the year in which the cash is received.

Fixed Assets

1.10 Through the application of the Modified Historical Cost Accounting Convention (MHCA), the Department's fixed assets are expressed at their value to the Department on an inflation-adjusted basis, i.e. at actual or estimated current values. The Department achieves this through the application of prospective indices that are applied in April of each financial year and look ahead to the subsequent balance sheet date. A suite of indices is determined by the Department's Senior Economic Advisor, in conjunction with the Defence Analytical Services Agency. Different indices are used for the following asset categories and are "self correcting" in the subsequent financial year i.e. they are adjusted to account for the actual change in prices as compared to the earlier prediction:

- Land (by region and type);
- Buildings (UK and specific overseas indices);
- Fighting Equipment (one index for each of the three Sea, Air and Land systems);
- Plant, Machinery and Vehicles – Motor Vehicles and Trailers;
- Plant, Machinery and Vehicles – Other Transport Equipment;
- Plant, Machinery and Vehicles – Machinery and Equipment;
- IT and Communications Equipment – Office Machinery and Computers; and
- IT and Communications Equipment – Communications Equipment.

1.11 Additionally all fixed assets are subject to a quinquennial revaluation by external professional valuers in accordance with FRS15.

1.12 Assets under construction are valued at cost and are subject to indexation. On completion they are released from the project account into the appropriate asset category.

1.13 The Department's policy on the capitalisation of subsequent expenditure under FRS15 is to separately account for material major refits and overhauls when their value is consumed by the Department over a different period to the life of the corresponding core asset and where this is deemed to have a material effect on the carrying values of a fixed asset and the depreciation charge. Subsequent expenditure is also capitalised where it is deemed to enhance significantly the operational capability of the equipment, including extension of life and when it is incurred to replace or restore a component of an asset that has been treated separately for depreciation purposes.

Intangible Assets

1.14 Pure and applied research costs are charged to the Operating Cost Statement in the period in which they are incurred.

1.15 Development costs are capitalised where they contribute towards defining the specification of an asset that will enter production. Development costs not capitalised are charged to Other Operating Costs. The development costs are amortised over the planned operational life of that asset type, e.g. class of ship or aircraft, on a straight-line basis. Amortisation commences when the asset type first enters operational service within the Department. If it is decided to withdraw the whole or a significant part of an asset type early, then a corresponding proportion of any remaining unamortised development costs are written off to the Operating Cost Statement along with the underlying tangible fixed assets. For the purposes of development costs, a significant withdrawal of assets is deemed to be 20% or greater of the total of the asset class.

Tangible Fixed Assets

1.16 The useful economic lives of tangible fixed assets are reviewed annually and adjusted where necessary. The capitalisation threshold is £10,000.

1.17 In these financial statements, guided weapons, missiles and bombs (GWMB) and capital spares are categorised as fixed assets and subject to depreciation. The depreciation charge in the Operating Cost Statement also includes the cost of GWMB fired to destruction. The principal asset categories and their useful economic lives, depreciated on a straight line basis, are:

	Category	Years
Land and Buildings	Land Buildings, permanent Buildings, temporary Leasehold	Indefinite, not depreciated Useful economic life 5 – 20 Shorter of expected life and lease period
Fighting Equipment (including GWMB)		Useful economic life (on a pooled basis for GWMB)
Plant, Machinery and Vehicles	Plant and Machinery Specialised Vehicles (includes non-fighting vessels and aircraft) Other standard vehicles	5 – 15 Useful economic life 3 – 5
IT and Communications Equipment	Computers Satellites Communications Equipment	3 – 7 Useful economic life Useful economic life
Operational Heritage Assets*		As other tangible fixed assets
Capital Spares	Items of repairable material retained for the purpose of replacing parts of an asset undergoing repair, refurbishment, maintenance, servicing, modification, enhancement or conversion.	Useful economic life (on a pooled basis, consistent within the life of the prime equipment supported)

*Operational Heritage Assets are included within the principal asset category to which they relate.

Donated Assets

1.18 Donated assets (i.e. those assets that have been donated to the Department or assets for which the Department has continuing and exclusive use but does not own legal title and for which it has not given consideration in return) are capitalised at their current valuation on receipt and are revalued/depreciated on the same basis as purchased assets.

1.19 A donated assets reserve represents the value of the original donation, additions, any subsequent professional revaluation and indexation (MHCA) or a professional valuation. Amounts equal to the donated asset depreciation charge, impairment costs and deficit/surplus on disposal arising during the year, are released from this reserve to the Operating Cost Statement.

Impairment

1.20 The charge to the Operating Cost Statement in respect of impairment arises on the decision to sell a fixed asset and take it out of service; on transfer of a fixed asset into stock; on reduction in service potential and where the application of MHCA indices causes a downward revaluation below the historical cost and which is deemed to be permanent in nature. Impairment also includes the cost of capital spares that are embodied into a fixed asset, as part of a major refit and overhaul, but which cannot be capitalised in accordance with FRS 15. Any reversal of an impairment cost is recognised in the operating cost statement to the extent that the original charge was recognised in the Operating Cost Statement. The remaining amount is recognised in the revaluation reserve.

Disposal of Tangible Fixed Assets

1.21 Disposal of assets is principally handled by two specialist agencies: Defence Estates for property assets and the Disposal Services Agency for non-property assets.

1.22 Property assets identified for disposal are included at the open market value with any resulting changes in the net book value charged to the Operating Cost Statement under Impairment or credited to the revaluation reserve as appropriate. On subsequent sale the surplus or deficit is included in the Operating Cost Statement under surplus/deficit on disposal of fixed assets.

1.23 Non-property assets are subject to regular impairment reviews. An impairment review is also carried out when a decision is made to dispose of an asset and take it out of service. Any write down in value to the net recoverable amount (NRA) is charged to the Operating Cost Statement under Impairment. The surplus or deficit at the point of disposal is included in the Operating Cost Statement under surplus/deficit on disposal of fixed assets. Non-property assets, where the receipts on sale are anticipated not to be separately identifiable, are transferred to stock at their NRA and shown under assets declared for disposal. Any write down on transfer is included in the Operating Cost Statement under Impairment.

1.24 Disposals exclude fixed assets written off and written on. These items are included within Other Movements in Notes 8 and 9.

Leased Assets

1.25 Assets held under finance leases are capitalised as tangible fixed assets and depreciated over the shorter of the lease term or their estimated useful economic lives. Rentals paid are apportioned between reductions in the capital obligations included in creditors, and finance charges charged to the Operating Cost Statement. Expenditure under operating leases is charged to the Operating Cost Statement in the period in which it is incurred. In circumstances where the Department is the lessor of a finance lease, amounts due under a finance lease are treated as amounts receivable and reported in Debtors.

Private Finance Initiative (PFI) Transactions

1.26 Where the substance of the transaction is that the risks and rewards of ownership remain with the Department, the assets and liabilities remain on the Department's Balance Sheet. Service charges in respect of on-balance sheet PFI deals are apportioned between reduction in the capital obligation and charges to the Operating Cost Statement for service performance and finance cost. Where the risks and rewards are transferred to the private sector the transaction is accounted for in the Operating Cost Statement through service charges in accordance with FRS 5 and Treasury Guidance.

Investments

1.27 Investments represent holdings that the Department intends to retain for the foreseeable future. Fixed asset investments are stated at market value where available, otherwise they are stated at cost. They include the Public Dividend Capital of those Executive Agencies owned by the Department and established as Trading Funds. Investments may either be equity investments, held in the name of the Secretary of State for Defence, or medium or long-term loans made with the intention of providing working capital or commercial support.

1.28 Joint Ventures are accounted for using the Gross Equity method of accounting. Under this method the Department's share of the aggregate gross assets and liabilities underlying the net equity investments are shown on the face of the Balance Sheet. The Operating Cost Statement includes the Department's share of the investee's turnover.

Stocks and Work-in-Progress

1.29 Stock is valued at current replacement cost, or historical cost if not materially different. Provision is made to reduce cost to net realisable value (NRV) where there is no expectation of consumption or sale in the ordinary course of the business. Stock provision is released to the operating costs on consumption, disposal and write-off.

1.30 Internal Work-in-Progress represents ongoing work on the manufacture, modification, enhancement or conversion of stock items. This is valued on the same basis as stocks. External Work-in-Progress represents ongoing work on production or repair contracts for external customers. This is valued at the lower of current replacement cost and NRV.

1.31 Assets declared for disposal include stock held for disposal and those non-property fixed assets identified for disposal where receipts are not anticipated to be separately identifiable.

1.32 Stocks written-off, included within other operating costs, represents the book value of stock which has been scrapped, destroyed or lost during the year, and adjustments to agree the book values with the figures shown on the supply systems.

Provisions for Liabilities and Charges

1.33 Provisions for liabilities and charges have been established under the criteria of FRS 12 and are based on realistic and prudent estimates of the expenditure required to settle future legal or constructive obligations that exist at the Balance Sheet date.

1.34 Provisions are charged to the Operating Cost Statement unless they have been capitalised as part of the cost of the underlying facility where the expenditure provides access to current and future economic benefits. In such cases the capitalised provision will be depreciated as a charge to the Operating Cost Statement over the remaining estimated useful economic life of the underlying asset. All long-term provisions are discounted

to current prices by use of HM Treasury's Test Discount Rate (TDR) which was 3.5% (2002-03: 6%) for the financial year 2003-04. The discount is unwound over the remaining life of the provision and shown as an interest charge in the Operating Cost Statement.

Reserves

1.35 The Revaluation Reserve reflects the unrealised element of the cumulative balance of revaluation and indexation adjustments on fixed assets and stocks (excluding donated assets and those financed by Government grants). The Donated Asset Reserve reflects the net book value of assets that have been donated to the Department.

1.36 The General Fund represents the balance of the taxpayers' equity.

Pensions

1.37 Present and past employees are mainly covered by the CSP arrangements for civilian personnel and the AFPS for Service personnel. There are separate scheme statements for the AFPS and CSP as a whole.

1.38 Both pension schemes are contracted out, unfunded, defined benefit pay as you go occupational pension schemes, although they are being accounted for as if they were defined contribution schemes in accordance with the HM Treasury RAM. The employer's charge is met by payment of an ASLC, which is calculated based on a percentage of pensionable pay. The ASLC represents an estimate of the cost of providing future superannuation protection for all personnel currently in pensionable employment. In addition, civilian personnel contribute 1.5% of salary to fund a widow/widower's pension if they are members of Classic and 3.5% if they are members of Premium. The Department's Balance Sheet will only include a creditor in respect of pensions to the extent that the contributions paid to the pension funds in the year fall short of the ASLC and widow/widower's pension charges due.

1.39 The pension schemes undergo a reassessment of the ASLC contribution rates by the Government Actuary at three-yearly intervals. Provisions are made for costs of early retirement programmes and redundancies up to the normal retirement age and charged to the Operating Cost Statement.

1.40 The Department operates a number of small pension schemes for civilians engaged at overseas locations. These schemes have been accounted for in accordance with the application of SSAP 24 – Accounting for Pension Costs, as set out in the HM Treasury RAM. With effect from 1 April 2003 they are accounted for in accordance with FRS 17 – Retirement Benefits. Prior year's figures have not been restated as any adjustments would not be material.

1.41 The disclosures required under FRS 17 are included in Note 2.4

Early Departure Costs

1.42 The Department provides in full for the cost of meeting pensions up to normal retirement age in respect of civilian personnel early retirement programmes and redundancies announced in the current and previous years. Pensions payable after normal retirement age are met by the CSP arrangements for civilian personnel.

1.43 There is no comparable early retirement or redundancy scheme for Service personnel but an immediate entitlement to draw pension under the AFPS accrues after 22 years' service for other ranks and 16 years' service for officers, or earlier in circumstances where exceptional approval is given.

Cost of Capital Charge

1.44 A charge, reflecting the cost of capital utilised by the Department, is included in the Operating Cost Statement and credited to the General Fund. The charge is calculated using the HM Treasury standard rate for financial year 2003-04 of 3.5% (2002-03: 6%) in real terms on all assets less liabilities except for:

- Donated assets and cash balances with the Office of HM Paymaster General (OPG) where the charge is nil.
- Liabilities for the amounts to be surrendered to the Consolidated Fund and for amounts due from the Consolidated Fund where the charge is nil.
- Assets financed by grants, where the charge is nil.
- Additions to heritage collections where the existing collection has not been capitalised, where the charge is nil.

1.45 The cost of capital charge on the fixed asset investments in the Trading Funds and in the Self Financing Public Corporation is calculated at a specific rate applicable to those entities, and is based on their underlying net assets.

Foreign Exchange

1.46 Transactions that are denominated in a foreign currency are translated into Sterling using the General Accounting Rate (GAR) ruling at the date of each transaction. US\$ and Euros are purchased forward from the Bank of England. Monetary assets and liabilities are translated at the spot rate applicable at the Balance Sheet date and the exchange differences are reported in the Operating Cost Statement.

1.47 Overseas non-monetary assets and liabilities are subject to annual revaluation and are translated at the spot rate applicable at the Balance Sheet date and the exchange differences are taken to the revaluation reserve for owned assets, or the donated asset reserve for donated assets.

2. Staff Numbers and Costs

2.1 The average number of whole-time equivalent persons employed during the year was: Service 213,600 (2002-03: 211,453) and Civilian 92,720 (2002-03: 92,358). [Source: Defence Analytical Services Agency]

2.2 The aggregate staff costs, including grants and allowances paid were as follows:

	2003-04 £000	2002-03 £000
Salaries and Wages	8,332,356	7,819,361
Social Security costs	609,865	506,837
Pension costs (see Note 2.4)	1,442,696	1,357,703
Redundancy and severance payments	50,240	285,341
	10,435,157	9,969,242
Made up of:		
Service	7,973,835	7,385,185
Civilian	2,461,322	2,584,057
	10,435,157	9,969,242

2.3 For the year ended 31 March 2004 the salary, pension entitlements and the value of any taxable benefits-in-kind for Ministers in respect of their services to the Department is detailed below and should be read in conjunction with the following notes.

Ministerial Salaries and Allowances

† The presentation below is based on payments made by the Department and thus recorded in these Accounts. In respect of Ministers in the House of Commons, Departments bear only the cost of the additional ministerial remuneration. The salary for their services as an MP £56,358 pa with effect from 1 April 2003 (2002-03 £55,118 pa with effect from 1 April 2002), and various allowances to which they are entitled are borne centrally by the House of Commons. However, the arrangements for Ministers in the House of Lords is different in that they do not receive a salary but rather an additional remuneration which cannot be quantified separately from their Ministerial salaries. This total remuneration, as well as the allowances to which they are entitled, is paid by the Department and is therefore shown in full in the figures below.

** Lords Ministers' Night Subsistence paid to The Lord Bach of Lutterworth was £27,866 in 2003-04 (2002-03: £27,133). These figures are included in the salary figures disclosed. No Minister received payment of the London Supplement allowance this year.

Ministers who have not attained the age of 65, and who are not re-appointed to a relevant Ministerial or other paid office within three weeks, are eligible for a severance payment. One such payment was made in 2003-04 (2002-03: Nil).

Ministerial Pensions

Pension benefits for Ministers are provided by the Parliamentary Contributory Pension Fund (PCPF). The scheme is statutory based (made under Statutory Instrument SI 1993 No 3253, as amended).

Those Ministers who are Members of Parliament are also entitled to an MP's pension under the PCPF. The arrangements for Ministers provide benefits on an 'average salary' basis with either a 1/50th or 1/40th accrual rate, taking account of all service as a Minister. (The accrual rate has been 1/40th since 15 July 2002 but Ministers, in common with all other members of the PCPF, can opt to increase their accrual rate from 5 July 2001, or retain the former 1/50th accrual rate and the lower rate of employee contribution.)

Benefits for Ministers are payable at the same time as MPs' benefits become payable under the PCPF or, for those who are not MPs, on retirement from ministerial office on or after age 65. Pensions are increased annually in line with changes in the Retail Prices Index. Members pay contributions of 6% of their Ministerial salary if they have opted for the 1/50th accrual rate, and 9% if they have opted for the 1/40th accrual rate. There is also an employer contribution paid by the Exchequer representing the balance of cost. This is currently 24% of the Ministerial salary.

The Cash Equivalent Transfer Value (CETV)

This is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. It is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the pension benefits they have accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total ministerial service, not just their current appointment as a Minister. CETVs are calculated within the guidelines and framework prescribed by the Institute and Faculty of Actuaries.

The real increase in the value of the CETV

This takes account of the increase in accrued pension to owing inflation and contributions paid by the Minister and is calculated using common market valuation factors for the start and end of the period.

Benefits-in-kind for Ministers

Minister's private use of Official cars is exempt under the rules governing the definition of taxable benefits-in-kind. Mr Hoon was provided with living accommodation. The value of the benefit is calculated in accordance with the Inland Revenue regulations. No tax is charged on the living accommodation itself; a charge is made on the value of associated services, limited to 10% of taxable Ministerial salary.

Ministers:

Figures for 2003-04 in bold, 2002-03 in italics

	Salary (as defined below)	Taxable Benefits-in- kind	Total Accrued Pension at retirement as at 31 March 2004	CETV at 31 March 2003	CETV at 31 March 2004	Real increase in CETV as funded by employer
	£000	(to nearest) £000	£000	£000	£000	£000
<i>Secretary of State for Defence:</i> The Right Honourable Geoffrey Hoon, MP †	70-75 <i>65-70</i>	7,100 <i>3,500</i>	5-10 <i>0-5</i>	54	72	8
<i>Minister of State for the Armed Forces:</i> The Right Honourable Adam Ingram MP †	35-40 <i>35-40</i>	Nil <i>Nil</i>	5-10 <i>0-5</i>	54	66	7
<i>Parliamentary Under Secretary of State and Minister for Defence Procurement:</i> The Lord Bach of Lutterworth † **	90-95 <i>90-95</i>	Nil <i>Nil</i>	5-10 <i>0-5</i>	58	78	12
<i>Parliamentary Under Secretary of State for Defence and Minister for Veterans:</i> Dr Lewis Moonie, MP † (Until 13 Jun 2003)	10-15 <i>25-30</i>	Nil <i>Nil</i>	0-5 <i>0-5</i>	25	27	1
Ivor Caplin MP † (From 13 June 2003)	20-25	Nil	0-5	9	14	3
Salary includes gross salary, performance pay and allowances paid.						

Defence Management Board:

The salary, pension entitlements and the value of taxable benefits-in-kind for the Department's senior management board, the DMB, were as below.

Figures for 2003-04 in bold, 2002-03 in italics

	Salary (as defined below)	Taxable Benefits-in- kind	Total Accrued Pension at retirement as at 31 March 2004	CETV at 31 March 2003	CETV at 31 March 2004	Real increase in CETV as funded by employer (Note)
	£000	(to nearest £100)	£000	£000	£000	£000
<i>Permanent Under Secretary of State</i> Sir Kevin Tebbit KCB CMG	165-170 <i>150-155</i>	33,000 <i>29,200</i>	Pension 65-70 Lump sum 205-210	1,075	1,223	101
<i>Chief of the Defence Staff</i> Admiral the Lord Boyce GCB OBE DL (Until 1 May 2003)	<i>175-180</i>	<i>25,400</i>	<i>CONSENT</i>	<i>TO DISCLOSE</i>	<i>WITHELD</i>	
General Sir Michael Walker GCB CMG CBE ADC Gen (From 2 May 2003)	165-170 <i>(see below)</i>	27,900 <i>(see below)</i>	Pension 85-90 Lump sum 265-270	1,207	1,604	
<i>First Sea Lord and Chief of the Naval Staff</i> Admiral Sir Alan West KCB DSC ADC	125-130 <i>65-70</i>	21,300 <i>12,100</i>	Pension 60-65 Lump sum 185-190	1,241	1,292	
<i>Chief of the General Staff</i> General Sir Mike Jackson KCB CBE DSO ADC Gen (From 3 Feb 2003)	135-140 <i>20-25</i>	22,200 <i>3,300</i>	Pension 65-70 Lump sum 200-205	1,162	1,185	
General Sir Michael Walker GCB CMG CBE ADC Gen (Until 2 Feb 2003)	<i>105-110</i>	<i>17,900</i>				
<i>Chief of the Air Staff</i> Air Chief Marshal Sir Peter Squire GCB DFC AFC ADC FRAeS RAF (Until 31 Jul 2003)	40-45 <i>125-130</i>	7,600 <i>22,500</i>	Pension 65-70 Lump sum 195-200	1,245	1,263	
Air Chief Marshal Sir Jock Stirrup KCB AFC ADC FRAeS FCMI RAF (From 1 Aug 2003)	85-90 <i>Nil</i>	14,800 <i>Nil</i>	Pension 55-60 Lump sum 175-180	1,069	1,260	
<i>Vice Chief of the Defence Staff</i> Air Chief Marshal Sir Anthony Bagnall KCB OBE ADC FRAeS RAF	130-135 <i>125-130</i>	22,900 <i>20,500</i>	Pension 65-70 Lump sum 200-205	1,243	1,262	
<i>Second Permanent Under Secretary of State</i> Ian Andrews CBE TD	125-130 <i>115-120</i>	28,300 <i>29,500</i>	Pension 40-45 Lump sum 115-120	569	641	55
<i>Chief of Defence Procurement</i> Sir Robert Walmsley KCB FEng FIEE (Until 30 Apr 2003)	10-15 <i>130-135</i>	2,600 <i>43,200</i>	Pension 5-10 Lump sum 25-30	151	152	1
Note:						
Figures for the real increase in Cash Equivalent Transfer Values (CETV) are not yet available for Service members of the Defence Management Board.						

	Salary (as defined below)	Taxable Benefits-in- kind	Total Accrued Pension at retirement as at 31 March 2004	CETV at 31 March 2003	CETV at 31 March 2004	Real increase in CETV as funded by employer
	£000	(to nearest £100)	£000	£000	£000	£000
Sir Peter Spencer KCB (From 1 May 2003)	105-110 <i>Nil</i>	29,000 <i>Nil</i>	Pension 0-5	0	18	15
Chief of Defence Logistics Air Chief Marshal Sir Malcolm Pledger KCB OBE AFC BSc FRAeS RAF (From 2 Sep 2002)	125-130 65-70	Nil <i>Nil</i>	Pension 60-65 Lump sum 115-120	1,204	1,284	
Chief Scientific Adviser Professor Sir Keith O'Nions FRS	145-150 135-140	25,700 27,700	Pension 35-40 Lump sum 115-120	676	720	15
Non-executive member of the DMB Charles Miller Smith (Chairman of Scottish Power) (From 29 May 2002)	25-30 15-20 <i>Fees</i>					
Non-executive member of the DMB Philippa Foster Back † (Director of the Institute of Business Ethics) (From 10 Jul 2002)	35-40 10-15 <i>Fees</i>					
† Mrs Foster Back's fees are £25,000 per annum. Fees for 2003-04 include an increase payable from July 2002.						
Salary includes gross salary, performance pay and allowances paid.						

Benefits-in-kind figures for civilian members of the DMB represent the value obtained from the private use of official cars, and for Service members of the DMB represents the value obtained from use of Official Service Residences. The Department has an arrangement with the Inland Revenue where MoD pays the tax liability that would ordinarily be paid by the individual. The tax liability consists of income tax, and where applicable, employees NIC. This tax liability is therefore included in the figures disclosed to arrive at the full 'value' of the benefit to the individual.

Details of Chief Executives and other senior staff of agencies are given in the agency accounts.

Pensions

2.3 The Principal Civil Service Pension Scheme (PCSPS) is an unfunded multi-employer defined benefit scheme but the Ministry of Defence is unable to identify its share of the underlying assets and liabilities. A full actuarial valuation was carried out at 31 March 1999 for the PCSPS. Details can be found in the resource accounts of the scheme which are published and laid before the House of Commons. The PCSPS accounts are also available on the web at www.civilservice-pensions.gov.uk.

For 2003-04, employers' contributions of £218,459,000 in respect of civilian staff were payable to the OPG (2002-03: £211,677,000) at one of the four rates in the range of 12 to 18.5 per cent of pensionable pay, based on salary bands. Rates will remain the same for next year, subject to revalorisation of the salary bands. Employer contributions to the PCSPS are to be reviewed every four years following a full scheme valuation by the Government Actuary.

For Service personnel, employers' contributions of £1,224,237,000 (2002-03: £1,146,025,000) were also made to the Armed Forces Pension Scheme (AFPS) based on rates determined by the Government Actuary. The applicable rates were 33.8% of pensionable pay for Officers and 18.2% for other ranks.

The contribution rates reflect benefits as they are accrued, not when costs are actually incurred, and reflect past experience of the scheme.

2.4 Certain other employees are covered by other schemes such as the NHS Superannuation Scheme and the Teachers' Superannuation Scheme. Contributions to these schemes in 2003-04 are included within the amount of £218,459,000 shown in Note 2.4 above.

Cash Equivalent Transfer Values

2.5 A Cash Equivalent Transfer Value (CETV) is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the pension scheme, not just their service in a senior capacity to which disclosure applies. The CETV figures, and from 2003-04 the other pension details, include the value of any pension benefit in another scheme or arrangement which the individual has transferred to the CSP arrangements and for which the CS Vote has received a transfer payment commensurate to the additional pension liabilities being assumed. They also include any additional pension benefit accrued to the member as a result of their purchasing additional years of pension service in the scheme at their own cost. CETVs are calculated within the guidelines and framework prescribed by the Institute and Faculty of Actuaries.

Real increase in CETV

2.6 This reflects the increase in CETV effectively funded by the employer. It takes account of the increase in accrued pension to owing inflation, contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market valuation factors for the start and end of the period.

3. Other Operating Costs

	2003-04 £000	2002-03 £000
Operating expenditure:		
– Fuel	161,329	184,665
– Stock consumption	1,059,775	1,222,151
– Surplus arising on disposal of stock (net)	(29,456)	(14,388)
– Provisions to reduce stocks to net realisable value	(72,345)	111,125
– Stocks written off (net)	528,120	321,811
– Movements: includes personnel travelling, subsistence/relocation costs and movement of stores and equipment	491,226	505,272
– Utilities	220,327	223,048
– Property management	1,393,283	1,453,041
– Hospitality and entertainment	7,991	7,320
– Accommodation charges	422,888	320,557
– Equipment support costs	3,804,132	3,135,174
– Increase in nuclear and other decommissioning provisions (Note 17)	154,509	1,635,223
– IT and telecommunications	737,717	628,447
– Professional fees	549,048	468,201
– Other expenditure	2,032,368	1,870,940
– Research expenditure and expensed development expenditure	1,011,213	977,707
Depreciation and amortisation:		
– Intangible assets (Note 8)	902,707	1,256,067
– Tangible owned fixed assets (Note 9)	4,838,283	5,766,924
– Donated assets depreciation - release of reserve	(46,625)	(48,845)
– Tangible fixed assets held under finance leases (Note 9)	24,993	7,309
Impairment on fixed assets (Notes 8 & 9):		
– Quinquennial valuation	–	3,855,123
– Other	299,010	1,534,601
Impairment – donated assets release of reserve	(1)	(1,500)
(Surplus)/ Deficit arising on disposal of tangible and intangible fixed assets		
– Tangible and Intangible fixed assets	(68,676)	(44,219)
– Donated assets – release of reserve	(3,049)	(1,041)
– Loss on sale of shares in QinetiQ	–	8,397
Fixed assets written off/(written on) - net	26,017	101,604
Write down of the value of investment in QinetiQ	–	219,886
Capital project expenditure written off	268,310	584,928
Bad debts written off	27,491	14,709
Decrease in bad debts provision	(2,939)	(5,523)
Rentals paid under operating leases	214,328	311,003
Auditors' remuneration – audit work only	3,150	3,405
Grants-in-Aid	54,790	49,128
Exchange differences on foreign currencies: net deficit/(surplus)	(622)	12,276
War Pensions and Allowances	1,117,635	1,166,265
Total Other Operating Costs	20,126,927	27,840,791

4. Analysis of income payable to the Consolidated Fund

In addition to Appropriations-in-Aid the following income relates to the Department and is payable to the Consolidated Fund. (Cash receipts are shown in italics).

	2003-04 Forecast		2003-04 Outturn	
	Income £000	Receipts £000	Income £000	Receipts £000
Operating income and receipts – excess A-in-A	–	–	85,315	<i>85,315</i>
Non operating income and receipts – excess A-in-A	–	–	137,325	<i>137,325</i>
Subtotal	–	–	222,640	<i>222,640</i>
Other operating income and receipts not classified as A-in-A	–	–	35,364	<i>35,364</i>
Other non-operating income and receipts not classified as A-in-A	–	–	–	–
Other amounts collectable on behalf of the Consolidated Fund	–	–	–	–
	–	–	<u>258,004</u>	<u><i>258,004</i></u>

The table above does not include loans repaid by QinetiQ and paid to the Consolidated Fund amounting to £4,213,977.

5. Operating Income

	2003-04 £000	2002-03 £000
External customers		
Rental Income – property	54,717	54,020
Other	1,171,897	1,115,777
Other Government Departments and Trading Funds and QinetiQ		
Rental income – property	4,974	2,058
Dividends received from Trading Funds (Note 10)	8,902	8,587
Other	171,816	177,258
	<u>1,412,306</u>	<u>1,357,700</u>
Of which:		
Appropriations-in-Aid	1,378,937	1,334,286
CFER – Payable to the Consolidated Fund	33,369	23,414
	<u>1,412,306</u>	<u>1,357,700</u>
Appropriations-in-Aid shown on Schedule 1 is the lower of the amounts shown in the Estimate and the Outturn:		
Outturn:		
– Operating Income (see above)	1,378,937	1,334,286
Included in other operating costs:		
– Refunds of formula based VAT recovery	46,766	44,112
– Profit on disposal of stock (net) (Note 3)	–	14,388
– Profit on disposal of tangible and intangible fixed assets (net) (Note 3)	–	45,260
– Foreign exchange gains	37,435	11,721
	<u>1,463,138</u>	<u>1,449,767</u>
Estimate:		
Appropriations-in-Aid as shown in the Spring Supplementary Estimate	1,377,823	1,695,949
Excess Appropriations-in-Aid payable to the Consolidated Fund as CFERs	<u>85,315</u>	<u>–</u>

6. Net Interest Payable

	2003-04 £000	2002-03 £000
Interest receivable:		
– Bank interest	(20,006)	(3,643)
– Loans to Trading Funds	(6,637)	(7,119)
– Loans to a Self Financing Public Corporation – QinetiQ	(1,346)	(5,054)
– Other interest receivable	(137)	–
	(28,126)	(15,816)
Interest payable:		
– Bank interest	164	6
– Loan interest	3,536	3,612
– Unwinding of discount on provision for liabilities and charges (Note 17)	2,609,205	247,703
– Finance leases and PFI contracts	26,264	31,026
– Commercial debt	–	1
	2,639,169	282,348
Net interest payable	2,611,043	266,532

7. Reconciliation of Net Operating Cost to Control Total and Net Resource Outturn

	2003-04 £000	2002-03 £000
Net operating cost (Schedule 2)	34,530,547	41,793,591
– Add income scored as Consolidated Fund Extra Receipts and included in operating income and interest (inc. excess Appropriation-in-Aid) (Note 4)	120,679	39,197
– Proceeds on part disposal of QinetiQ included in operating costs	–	39,427
– Prior year adjustment	–	141,469
Net resource outturn	34,651,226	42,013,684

Net operating cost is the total of expenditure and income appearing in the Operating Cost Statement. Net Resource Outturn is the total of those elements of expenditure and income that are subject to parliamentary approval and included in the Department's Supply Estimate. The Outturn against the Estimate is shown in the Summary of Resource Outturn (Schedule 1).

8. Intangible Assets

	£000
Cost or Valuation	
At 1 April 2003	23,753,098
Additions	1,665,395
Disposals	(31,372)
Impairment	(46,867)
Revaluations	97,738
Other movements	(513,174)
At 31 March 2004	<u>24,924,818</u>
Amortisation	
At 1 April 2003	(4,315,490)
Charged in Year	(902,707)
Impairment	(10,916)
Disposals	31,372
Revaluations	334,143
Other movements	125,523
At 31 March 2004	<u>(4,738,075)</u>
Net Book Value:	
At 31 March 2004	<u>20,186,743</u>
At 1 April 2003	<u>19,437,608</u>

Note:

- i) Intangible asset valuations are based on the actual costs incurred over time, where available, or derived by applying a ratio to the tangible fixed asset valuations based on the historical relationship between development and production costs. The intangible asset valuations were indexed using the appropriate Gross Domestic Product (GDP) deflator to determine the opening balance sheet valuation;
- ii) Intangible assets include development expenditure in respect of fixed assets in use and assets under construction where the first delivery into operational use of the asset type has taken place;
- iii) Additions on intangible and tangible fixed assets (Note 9) include accruals amounting in total to £2,204,303,000 (2002-03: £2,066,322,000); and
- iv) Other movements comprise reclassifications to tangible fixed assets and transfers to operating costs.

9. Tangible Fixed Assets

	Land and Buildings £000	Fighting Equipment £000	Plant, Machinery and Vehicles £000	IT and Comms Equipment £000	Capital Spares £000	Assets Under Construction £000	Total £000
Cost or Valuation							
At 1 April 2003	16,080,431	42,050,778	6,840,039	1,226,425	18,947,812	12,511,081	97,656,566
Additions	53,721	90,004	77,998	183,309	580,583	3,930,703	4,916,318
Capitalised provisions	(20,633)	(78,643)	–	–	–	–	(99,276)
Donations	911	–	2,819	3	–	–	3,733
Impairment	(34,374)	(116,496)	(35,009)	(41,699)	(57,612)	(7,862)	(293,052)
Disposals	(406,764)	(7,672)	(82,071)	(13,623)	(1,097,824)	(436)	(1,608,390)
Revaluations	836,551	554,643	958,436	(46,354)	393,616	200,800	2,897,692
Other movements	(2,879)	1,661,208	(562,841)	(78,724)	42,801	(3,457,076)	(2,397,511)
At 31 March 2004	16,506,964	44,153,822	7,199,371	1,229,337	18,809,376	13,177,210	101,076,080
Depreciation							
At 1 April 2003	(738,095)	(15,523,883)	(2,544,096)	(412,646)	(11,993,310)	–	(31,212,030)
Charged in year	(617,950)	(2,583,599)	(454,778)	(181,101)	(1,025,848)	–	(4,863,276)
Impairment	45,199	193,104	(14,702)	11,146	(182,922)	–	51,825
Disposals	2,487	7,622	79,625	12,411	1,093,623	–	1,195,768
Revaluations	(29,154)	(158,489)	(920,115)	48,311	(231,756)	–	(1,291,203)
Other movements	130,307	1,068,418	107,755	188,488	285,125	–	1,780,093
At 31 March 2004	(1,207,206)	(16,996,827)	(3,746,311)	(333,391)	(12,055,088)	–	(34,338,823)
Net Book Value: At 31 March 2004	15,299,758	27,156,995	3,453,060	895,946	6,754,288	13,177,210	66,737,257
At 1 April 2003	15,342,336	26,526,895	4,295,943	813,779	6,954,502	12,511,081	66,444,536

Note:

- Additions on intangible assets (Note 8) and tangible fixed assets include accruals amounting in total to £2,204,303,000 (2002-03: £2,066,322,000);
- Other movements comprise reclassifications between tangible fixed asset categories, intangible assets, assets under construction, stock and transfers to operating costs;
- Fixed Assets as at 31 March 2004 include capitalised provisions at cost of £222,519,000 (2002-03: £321,000,000); and
- The figure impairments above includes the following amounts in respect of reversals of impairments: Land and Buildings £32.296 million, Fighting Equipment £122.305 million, Plant, Machinery and Vehicles £0.495 million and IT and Comms Equipment £0.581 million.

9.1 The net book value of tangible fixed assets by each major class of asset includes an amount of £329,852,000 (2002-03 £115,389,000) in respect of assets held under finance leases and PFI contracts. Detail by asset category is as follows:

	Land and Buildings £000	Fighting Equipment £000	Plant, Machinery and Vehicles £000	IT and Comms Equipment £000	Capital Spares £000	Assets Under Construction £000	Total £000
Gross Cost:							
At 31 March 2004	102,604	130,804	87,263	64,797	–	–	385,468
At 1 April 2003	41,708	42,305	77,560	5,437	–	–	167,010
Accumulated Depreciation:							
At 31 March 2004	8,046	42,553	4,794	223	–	–	55,616
At 1 April 2003	1,719	20,511	27,429	1,962	–	–	51,621

9.2 Analysis of Land and Buildings:

	Freehold £000	Long Lease £000	Short Lease £000	Beneficial Use* £000	Total £000
Net Book Value:					
At 31 March 2004	13,726,472	268,518	71,471	1,877,832	15,944,293
At 1 April 2003	13,967,993	215,304	54,147	1,767,858	16,005,302

The net book values at 31 March 2004 and 1 April 2003 include assets under construction of £644,535,000 and £662,966,000 respectively.

*Relates to properties that are being used by the Department where no legal title is held. Such properties have been valued on the same basis as all other properties used by the Department.

9.3 Professional valuation of Land and Buildings was carried out by external valuers, as follows:

Year last valued	Valuation £000
Before 1 April 2001	535,207
2001-2002	696,405
2002-2003	13,847,177*
2003-2004	618,959

*2002-03 Quinquennial Revaluation

9.4 All categories of fixed assets, except Intangibles, Assets under Construction and Capital Spares, were subject to a quinquennial revaluation with an effective valuation date of 1 April 2002.

9.5 Operational land and buildings were valued by two firms of external professional valuers: the Valuation Office Agency valued the UK estate and the Overseas estate was valued by ATIS REAL Weatheralls, whose valuers are members of the Royal Institution of Chartered Surveyors (RICS). These valuations were undertaken in accordance with the RICS Appraisal and Valuation Manual and were on the basis of the existing use value to the Department and did not take account of alternative use value. Because of the specialised nature of the Departmental estate, the great majority of assets were thus valued on the Depreciated Replacement Cost basis.

9.6 Surplus land and buildings were valued by qualified internal Defence Estates staff, on the basis of Open Market Value.

9.7 Plant, Machinery & Vehicles and IT & Communications were both valued on a Depreciated Replacement Cost basis by the Valuation Office Agency, whose valuers are members of the Royal Institution of Chartered Surveyors.

10. Investments

	Trading Funds Public Dividend Capital £000	Trading Funds Loans £000	Other Investments £000	QinetiQ £000	Total £000
At 1 April 2003	184,254	117,203	1	128,220	429,678
Movements during year:					
DARA – new loan		19,200			19,200
Repayment of Loans					
–QinetiQ				(4,214)	(4,214)
–DARA		(7,240)			(7,240)
–UK Hydro Office		(303)			(303)
–DSTL		(2,128)			(2,128)
–ABRO		(14,155)			(14,155)
At 31 March 2004	184,254	112,577	1	124,006	420,838

Public Dividend Capital and Loans at 31 March 2004 were held in the following Trading Funds:

	Public Dividend Capital £000	Loans £000	Interest Rate % p.a.
DSTL	50,412	1,064	8.375
Met Office	58,867	–	–
The UK Hydrographic Office	13,267	11,679	8.375
DARA	42,303	71,830	4.882
ABRO	19,405	28,004	5.375 - 5.625
	184,254	112,577	

Analysis of loans repayable by instalments:

	Due within one year £000	Due after one year £000	Total £000
DSTL	1,064	–	1,064
The UK Hydrographic Office	303	11,376	11,679
DARA	7,240	64,590	71,830
ABRO	2,154	25,850	28,004
	10,761	101,816	112,577

At 31 March 2004, the loan made to QinetiQ Group Limited, a subsidiary undertaking of QinetiQ, amounted to £45,886,000 (31 March 2003: £50,100,000) and the book value of investment in QinetiQ amounted to £78,120,000. The loan note is repayable from the net proceeds of disposals of certain identified assets. The loan note was interest free until 30 June 2003 and thereafter interest has been charged at rates relating to LIBOR.

As at 31 March 2004, the loans repaid by QinetiQ and subsidiary undertakings, representing the partial original asset value of the business since its formation on 1 July 2001, amounted in total to £104,114,000 (2002-03: £99,900,000). Cash received on part disposal of the shares to The Carlyle Group during 2002-03 amounted to £39,427,000.

10.1 Other Investments:

Investments, including "Golden" shares, were held in the following at 31 March 2004 and 31 March 2003:

	7.5% Non-cumulative irredeemable preference shares at £1 each
Chamber of Shipping Limited	688 Shares
British Shipping Federation Limited	55,040 Shares
	Preferential 'Golden' Shares at £1 each
Devonport Royal Dockyard Limited	1 Share
Rosyth Royal Dockyard Limited	1 Share
Atomic Weapons Establishment plc	1 Share
Atomic Weapons Establishment Pension Trustees Limited	1 Share
QinetiQ Group plc	1 Share
QinetiQ Limited	1 Share
BAE Systems Marine (Holdings) Ltd (formerly VSEL Limited)	1 Share
	Non Preferential Shares of £1 each
International Military Services Limited	19,999,999 Shares

Shareholding in QinetiQ

The Department holds 5 classes of shares in QinetiQ. A brief summary of the financial and voting rights of each class are detailed below in order of their ranking in accordance with the Articles of Association of QinetiQ.

Convertible "A" ordinary (3,773,481 shares of 1p each – 49% of class)

Voting rights – holders of these shares are entitled to receive notice of, attend, speak and vote at general meetings of the company.

Dividends – none to be paid until Preference Shares have been redeemed in full along with any accrued Preference Dividend.

Convertible "B" ordinary (285,833 shares of 1p each – 49% of class)

Dividend and Voting rights as per "A" Ordinary shares.

Convertible Preferred (3,752,686 shares of 1p each – 100% of class)

Voting rights – this class of shareholder is not entitled to receive notice of, nor attend, speak or vote at general meetings of the company.

Dividends – until conversion each Convertible Preferred share in issue will be entitled to the same dividend as paid on each "A" Ordinary Share.

Redeemable Cumulative Preference (70,308,000 shares of £1 each – 62.5% of class)

Voting rights – preference shareholders are not entitled to receive notice of, nor attend, speak or vote at general meetings of the company.

Dividend – to be paid at the rate of 9% per annum on the nominal value of the preference shares held.

Dividends will not be paid, but will accrue until the preference shares are redeemed at the Sale, Listing or the Winding up of the company. The dividend accrued on these shares will be recognised in the Operating Cost Statement in the year in which it is received, in accordance with accounting policy in Note 1.9.

In June 2004, the Department received £48,542,475 on the partial redemption of some of these shares and an amount of £5,759,382 in respect of the dividend accrued on these shares up to the date of redemption.

Special Rights Redeemable of £1 each - the one "Special Share", which is held by MoD

The Special Shareholder has the right to require the Company to implement and maintain a regime which protects the defence and security interests of the nation. Voting rights – the Special Shareholder must receive notice of, and may attend and speak at general company and share class meetings, but carries no voting rights, except to enforce certain aspects of the compliance regime.

Preferential "Golden" Shares at £1 each (1 share QinetiQ Group plc, 1 share QinetiQ Limited)

The Preferential "Golden" Shareholder has the right to require the Company to implement and maintain a regime which protects the defence and security interests of the nation. Voting rights – the Special Shareholder must receive notice of, and may attend and speak at general company and share class meetings, but carries no voting rights, except to enforce certain aspects of the compliance regime.

Dividends – the Special Shareholder has no right to share in the capital or profits of the company other than – in the event of a liquidation – to be repaid the capital paid up in respect of the special share before other shareholders receive any payment.

QinetiQ also issued other classes of shares on its formation, which are not shown above. These shares were issued to the employees of the company.

10.2 Net assets

The reported net assets, after deducting loans due to MoD, of the investments held at 31 March 2004 and 31 March 2003 were:

	31 March 2004 £Million	31 March 2003 £Million
The UK Hydrographic Office	48.7	40.9
Met Office	167.8	159.5
Defence Aviation Repair Agency (DARA)	67.2	59.1
Defence Science and Technology Laboratory (DSTL)	176.5	140.5
QinetiQ	225.2	140.0
Army Base Repair Organisation (ABRO)	57.3	43.7
Total	742.7	583.7

During the year, a dividend of £6,000,000 (2002-03: £6,000,000) was received from DSTL and a dividend of £2,902,359 (2002-03: £2,587,166) was received from The UK Hydrographic Office in respect of the financial year ended 31 March 2003. These are included within operating income. No dividend was received from Met Office, Defence Aviation Repair Agency, QinetiQ and ABRO.

10.3 The Department has a 100% interest in the non-preferential shares of International Military Services Limited, a company registered in England. International Military Services Limited ceased trading on 31 July 1991. Following settlement of outstanding contracts, the company will be liquidated. The Department has written down the value of the investment to nil.

10.4 All the shares held are unlisted and are valued at historical cost. The 7.5% Non-cumulative irredeemable preference shares in Chamber of Shipping Limited and British Shipping Federation Limited are valued at 1p each reflecting the value at which shares would be recovered by the two companies should membership by the Department be ceded, as laid down in the articles of association of the respective companies.

10.5 "Golden" shares confer on the Secretary of State for Defence special rights regarding ownership, influence and control, including voting rights in certain circumstances, under the individual articles of association of the relevant companies in which the shares are held. Further detailed information can be obtained from the companies' individual annual reports and accounts which can be obtained from:

Company	Registration Number
Devonport Royal Dockyard Limited, Devonport Royal Dockyard, Devonport, Plymouth PL1 4SG	02077752
Rosyth Royal Dockyard Limited, Rosyth Royal Dockyard, Rosyth, Fife KY11 2YD	SC101959
Atomic Weapons Establishment plc, AWE Aldermaston, Reading, Berkshire RG7 4PR	02763902
Atomic Weapons Establishment Pension Trustees Limited, AWE Aldermaston, Reading, Berkshire RG7 4PR	02784144
QinetiQ Group plc, 85 Buckingham Gate, London SW1E 6PD	4154556
QinetiQ Limited, 85 Buckingham Gate, London SW1E 6PD	3796233
BAe Systems Marine (Holdings) Limited, Warwick House, PO Box 87, Farnborough Aerospace Centre, Farnborough, Hants, EU14 6YU	1470151

11. Related Party Transactions

11.1 The Defence Science and Technology Laboratory, The UK Hydrographic Office, the Met Office, the Defence Aviation Repair Agency and the Army Base Repair Organisation (ABRO) operate as Executive Defence Agencies financed by Trading Fund. QinetiQ is a Self Financing Public Corporation. These fall within the ambit of the Department and are regarded as related parties outside the Departmental Boundary with which the Department has had material transactions. All transactions are carried out on terms which are contracted on an arms length basis, and are subject to internal and external audit. The NAAFI is outside the Departmental Boundary and is also regarded as a related party.

The following bodies are Executive NDPBs of the MoD. They are self-accounting on an accruals basis, and are regarded as Related Parties. During the year, each NDPB has had a material transaction with the Department, as listed below:

Fleet Air Arm Museum

Grant-in-Aid: £550,323 (2002-03: £527,578)

Commodore Naval Aviation (Deputy Chairman), Commanding Officer HMS Heron (RNAS Yeovilton), Commanding Officer HMS Seahawk (RNAS Culdrose), Director Support Operations (Rotary Wing), and Assistant Director Policy Co-ordination & Aviation (Director Naval Operations) are members of the Board of Trustees.

National Army Museum

Grant-in-Aid: £4,413,460 (2002-03: £4,747,800)

No Departmental representation.

Royal Air Force Museum

Grant-in-Aid: £6,810,815 (2002-03: £6,060,731)

No Departmental representation.

Royal Marines Museum

Grant-in-Aid: £688,061 (2002-03: £654,601)

Director Royal Marines, Corps Secretary Headquarters Royal Marines and Corps Regimental Sergeant Major, Royal Marines Stonehouse, Plymouth are members of the Board of Trustees.

Royal Naval Museum

Grant-in-Aid: £962,120 (2002-03: £882,286)

Naval Base Commander Portsmouth and Chief of Staff (Warfare) CinCFleet are members of the Board of Trustees.

Royal Navy Submarine Museum

Grant-in-Aid: £509,332 (2002-03: £488,008)

Rear Admiral Submarines is a member of the Board of Trustees.

Oil and Pipelines Agency

Agency Fees: £1,600,000 (2002-03: £1,523,000) VAT recovery £280,000 (2002-03: £266,525).

Director Defence Fuels Group is a member of the Board of Directors.

Other

Ian Andrews CBE TD, Second Permanent Under Secretary of State, is a trustee of the Imperial War Museum. Mr Charles Miller Smith is Chairman of Scottish Power. These entities are therefore related parties of the Ministry of Defence.

The payments made to these entities were:

		£000
Imperial War Museum	Various transactions	15
Scottish Power	Various transactions	5,443

During the year there were also various works of art and other items transferred to and from the Imperial War Museum. No value was attributed to these items.

Note:

- i) The Department also pays a number of grants to other bodies outside the Departmental Boundary. These include Grants-in-Aid to the Royal Hospital Chelsea and the Commonwealth War Graves Commission; and
- ii) The museums are designated NDPBs under the National Heritage Act 1983. Each NDPB is required to produce annual accounts in accordance with the Charities (Accounts and Reports) Regulations 1995 (Statutory Instrument 1995 No. 2724). The Oil and Pipelines Agency is a corporate body established under the Oil and Pipelines Act 1985.

Joint Ventures and Collaborative Projects**11.2 European Transonic Windtunnel GmbH (ETW):**

At 31 March 2004, the Department had no future involvement in ETW. Payments of £260,000 were made during the year.

The Department had a 31% interest in ETW, a non-profit making company, which was jointly owned by the governments of France, Germany, the Netherlands and the United Kingdom. ETW provided facilities for developments or research relating to air vehicles. Under a Memorandum of Understanding extended in January 2000, the Department was committed to making payments up to 31 March 2004. All of which was recoverable from the Department of Trade and Industry. The contributions made to ETW are charged to operating costs when incurred.

The Department is also involved in collaborative projects with various foreign countries for the development and production of fighting equipment. Costs capitalised represent the Department's proportion of the total cost of a project.

12. Stocks and Work in Progress

	31 March 2004 £000	31 March 2003 £000
Work in progress	60,058	39,116
Raw materials and consumables	6,255,211	5,294,617
Assets declared for disposal	2,955	3,392
	6,318,224	5,337,125

Note:

Raw materials and consumables at 31 March 2004 include some £750 million which was reclassified from fixed assets into stocks during the year.

13. Debtors

	31 March 2004 £000	31 March 2003 £000
Amounts falling due within one year		
Trade debtors	133,695	171,404
Deposits and advances	39,437	24,398
Value Added Tax	244,920	251,683
Amounts owed by other Government Departments	68,252	66,641
Amounts owed by entities in which the Department has a participating interest	7,446	10,517
Other debtors	209,570	211,480
Prepayments and accrued income	1,224,380	879,643
Amount due from Consolidated Fund	–	39,665
	1,927,700	1,655,431
Amounts falling due after one year		
Trade debtors	50,254	13,506
Other debtors	88,948	103,838
Prepayments and accrued income	608,457	428,451
Amounts owed by other Government Departments	–	299
Amounts owed by entities in which the Department has a participating interest	60	127
	747,719	546,221
Total debtors amounts falling due after one year	747,719	546,221
Total Debtors	2,675,419	2,201,652

Note:

- i) Other debtors include loans for house purchase and other loans made to staff amounting to £91,317,714 (2002-03: £97,554,131). The number of staff with house purchase loans was 13,927 (2002-03: 14,452); and
- ii) Prepayments, shown under amounts falling due within one year, include an amount of £343,500,000 paid into an Escrow account in 2002-03 in respect of an adjudication decision where an appeal is pending.

14. Cash at Bank and in Hand

	31 March 2004 £000	31 March 2003 £000
At 1 April	415,928	631,681
Net Cash Inflow/(Outflow):		
Received from Consolidated Fund	29,257,550	27,136,321
Utilised	(29,360,914)	(27,352,074)
Increase/(decrease) during year	(103,364)	(215,753)
At 31 March	312,564	415,928
Represented by:		
Balances at the OPG	279,166	147,197
Commercial Banks and Cash in Hand	33,398	268,731
	312,564	415,928
The balance at 31 March comprises:		
Consolidated Fund Extra Receipts received during the year and due to be paid to the Consolidated Fund (Note 15)	222,659	134,737
Amounts due from the Consolidated Fund for supply	(80,095)	144,956
Amount in respect of prior year payable to the Consolidated Fund	–	(39,665)
Net amount due to the Consolidated Fund	142,564	240,028
Amounts held in respect of Collaborative Projects (see note below)	170,000	175,900
Total	312,564	415,928

Note:

The cash at bank balance includes £170,000,000 (2002-03: £175,900,000) of sums advanced by foreign governments to the Department on various collaborative projects where the United Kingdom is the host nation. Advances made by foreign governments for the procurement of defence equipment on their behalf are also included in this amount. The corresponding liability for these advances is shown under creditors due within one year.

15. Creditors: amounts falling due within one year

	31 March 2004 £000	31 March 2003 £000
Trade creditors	472,930	608,803
Payments received on account	7,979	6,160
Other taxation and social security	203,939	164,041
Other creditors	357,592	400,635
Accruals and deferred income	4,216,352	3,736,625
Obligations under finance leases	4,853	549
Obligations under PFI contracts	10,418	6,105
Payable to the Consolidated Fund	142,564	279,693
Amounts owed to other Government Departments	5,281	2,561
Amounts owed to entities in which the Department has a participating interest	239,091	177,303
Loans	1,599	1,375
Total creditors due within one year	5,662,598	5,383,850

Note:

Amounts payable to the Consolidated Fund amounting to £142,564,000.00 (2002-03: £279,692,811.63) comprise:

	31 March 2004 £000	31 March 2003 £000
CFERs received during the year	19	1,110
CFER – proceeds on part sale of shareholding in QinetiQ	–	39,427
CFER – proceeds of certain fixed assets	–	44,300
CFER – loan repayments by QinetiQ	–	49,900
Excess Operating Appropriations-in-Aid	85,315	–
Excess Non-Operating Appropriations-in-Aid	137,325	–
	<u>222,659</u>	<u>134,737</u>
Amount repayable by Consolidated Fund in respect of prior year	–	(39,665)
Amount in respect of supply to be set off against CFER liability (Note iii)	(80,095)	144,956
Net amount payable to Consolidated Fund	142,564	240,028
Amount shown within debtors due within one year	–	39,665
	<u>142,564</u>	<u>279,693</u>

Note:

- i) Loans are from the National Loans Fund in respect of the Armed Forces Housing Loans. These are fully repayable between years 2012 and 2028, with the last instalment due on 20 February 2028. Interest on the loans is payable at rates ranging from 4.25% to 7% per annum.
- ii) Included in other creditors are amounts advanced by foreign governments to the Department in respect of various collaborative projects where the United Kingdom is the host nation and for the procurement of defence equipment on their behalf of £170,000,000 (2002-03 – £175,900,000).
- iii) The amount comprises amounts drawn down from the Consolidated Fund £29,257,550,000 less net cash requirement (Schedule 1) of £29,337,645,000.

16. Creditors: amounts falling due after more than one year

	31 March 2004 £000	31 March 2003 £000
Other creditors	96,897	287,953
Accruals and deferred income	2,655	14,844
Obligations under finance leases:		
– Amounts payable between one and two years	5,372	360
– Amounts payable between two and five years	8,413	502
– Amounts payable over five years	6,528	3,163
Obligations under PFI contracts:		
– Amounts payable between one and two years	16,884	9,204
– Amounts payable between two and five years	43,837	21,470
– Amounts payable over five years	219,215	59,128
Amounts owed to other Government Departments	–	–
Amounts owed to entities in which the Department has a participating interest	21	283
Loans:		
– Amounts payable between one and two years	2,527	1,599
– Amounts payable between two and five years	8,500	5,396
– Amounts payable over five years	40,800	46,431
Total creditors due after more than one year	<u>451,649</u>	<u>450,333</u>

17. Provisions for Liabilities and Charges

	Nuclear Decommissioning £000	Other Decommissioning & Restoration costs £000	Early Retirement Commitments £000	Other £000	Total £000
At 1 April 2003	5,529,752	144,801	361,293	958,381	6,994,227
Increase in Provision	175,518	27,799	26,935	259,859	490,111
Unwinding of discounting	2,524,769	16,059	28,209	40,168	2,609,205
Amounts released	(29,010)	(2,979)	(8,851)	(24,570)	(65,410)
Reclassifications	140	2,344	(5,900)	3,416	–
Amounts capitalised	(99,276)	–	–	–	(99,276)
Utilised in year	(283,124)	(3,120)	(90,739)	(162,184)	(539,167)
At 31 March 2004	<u>7,818,769</u>	<u>184,904</u>	<u>310,947</u>	<u>1,075,070</u>	<u>9,389,690</u>

Analysis of amount charged/(credited) to Operating Cost Statement

	2003-04 £000	2002-03 £000
Charged/(credited) to:		
Staff costs	40,379	232,485
Nuclear and Other Decommissioning provisions	154,509	1,635,223
War Pensions and Allowances	866	–
Other costs	228,947	171,782
Net interest (receivable)/payable	2,609,205	247,703
	<u>3,033,906</u>	<u>2,287,193</u>
Made up of:		
Increase	490,111	2,345,459
Release	(65,410)	(305,969)
	<u>424,701</u>	<u>2,039,490</u>
Unwinding of discount	2,609,205	247,703
Net increase in provisions	<u>3,033,906</u>	<u>2,287,193</u>

Nuclear Decommissioning

17.1 HM Treasury issued instructions to reduce the rate used for discounting the value of provisions from 6% to 3.5% effective from 1 April 2003. This accounted mainly for the increase in the value of provisions at the Balance Sheet date of £2,384,868,000 and increased the operating costs by the same amount.

17.2 Nuclear decommissioning provisions relate principally to the cost of facility decommissioning and the treatment and storage of nuclear waste arising at British Nuclear Fuel plc (BNFL) sites, operations at United Kingdom Atomic Energy Authority (UKAEA) sites, operations at MoD sites, operations of Royal Navy submarines and for the Departmental share of planning and constructing a national repository for the eventual disposal of that waste.

17.3 A new body will be created called the Nuclear Decommissioning Authority (NDA) to take over the responsibility for certain nuclear clean up issues. The authority will sit within the DTI. It is expected the MoD will transfer to NDA our liabilities relating to civil nuclear sites and the associated value of our provisions and funding for decommissioning costs. The liability for the decommissioning of MoD sites and for the disposal of submarine waste will not be transferred at this stage. The initial transfer is expected to take effect from 1 April 2005.

Liabilities have arisen since the late 1940's and will continue well into the future as a result of ongoing production and operations associated with the manufacture and reprocessing of Special Nuclear Materials (SNM). The majority of the liability is historic and relates to facilities used for the production of SNM by BNFL and its predecessor the UKAEA. The Atomic Weapons Establishment is the other main source of MoD's liabilities.

The liabilities include the costs associated with decommissioning and care and maintenance of redundant facilities including submarines (the conditioning, retrieval and storage of contaminated materials), research and development and the procurement of capital facilities to handle the various waste streams. Calculation of the provision to cover the liabilities is based on schedules of information received by the MoD from major decommissioning contractors. These schedules are based on technical assessments of the processes and methods likely to be used in the future to carry out the work. Estimates are based on the latest technical knowledge and commercial information available, taking into account current legislation, regulations and Government policy. The amount and timing of each obligation are therefore sensitive to these factors. These sensitivities and their likely effect on the calculation and amount of the liabilities are reviewed on an annual basis.

The latest estimate of the undiscounted cost of dealing with the MoD's nuclear liabilities is £23,387,678,000 (2002-03: £21,947,363,000).

The estimate of £7,818,769,000 (2002-03: £5,529,752,000) at 31 March 2004 represents the liabilities discounted at 3.5% and expressed in 2003/4 money values.

The estimated timescale over which the costs will need to be incurred is as follows:

	2004 £bn	2003 £bn
Up to 3 years	1.5	1.2
From 4 – 10 years	2.1	1.9
Beyond 10 years	4.2	2.4
Total	7.8	5.5

The bulk of the earlier anticipated costs relate to pre and post 1971 liabilities allocated to the Department. The significance of pre and post 1971 refers to the formation date of BNFL. Specific liabilities refer to the BNFL Sellafield, Springfields, Capenhurst, Calder Hall and Chapelcross sites.

Later provisions have been made to cover the costs associated with the research, development and construction of the NIREX Deep Waste Repository (DWR). The provisions have been based on advice provided by NIREX.

However, the policy for the disposal of intermediate and high level waste has yet to be clarified following the previous government's rejection, in May 1997, of planning consent for the proposed DWR. Pending the current government's consideration of a House of Lords Sub Committee report on means of disposing radioactive waste, the UK holders of such waste are working on the assumption that a repository will not be available earlier than 2040. This will necessitate the continued provision of interim storage.

Other Decommissioning and Restoration

17.4 Other decommissioning and restoration provisions relate primarily to contaminated sites where the Department has a constructive or a legal obligation to restore the sites for normal use and for the decommissioning of certain fighting equipment and GWMB.

Early Retirement Pensions

17.5 Where the Department implements an early retirement scheme, provision is made for future liability payable to civilian early retirees. This includes provisions arising from the "80:20 Scheme" under which 20% of the cost was borne by the Department and 80% was borne by the Civil Superannuation Vote. This scheme was terminated in 1997 and the full cost of the obligations are now payable by CSP.

Other

17.6 Other provisions include costs arising from the disposal of fixed assets; redundancy and relocation costs associated with reorganisation and restructuring; and amounts payable under guarantees, litigation and contractual arrangements. Provisions include those concerning an adjudication decision where an appeal is pending.

18. Reconciliation of Net Operating Costs to changes in General Fund

	2003-04 £000	2002-03 £000
Net Operating Cost for the Year (Sch 2)	(34,530,547)	(41,793,591)
Paid and payable to the Consolidated Fund	(182,125)	(317,780)
Parliamentary funding from the Consolidated Fund (Sch 4)	29,257,550	27,136,321
Transfer to General Fund of realised element of:		
– Revaluation reserve (Note 19)	1,258,804	830,832
– Donated asset reserve (Note 19)	6,794	6,537
Non-cash charges:		
– cost of capital charge (Sch 2)	2,769,726	5,074,726
– auditors' remuneration (Note 3)	3,150	3,405
Net decrease in General Fund	(1,416,648)	(9,059,550)
General Fund at 1 April	65,445,156	74,504,706
General Fund at 31 March	64,028,508	65,445,156

19. Reserves

	Revaluation Reserve £000	Donated Asset Reserve £000
At 1 April 2003	14,181,634	1,811,327
Arising on revaluation during the year (net)	2,473,493	(36,386)
Additions during the year	–	3,733
Transfers and reclassifications	121	(49)
Transferred (to) / from Operating Cost Statement	–	(49,675)
Transferred (to) / from General Fund	(1,258,804)	(6,794)
At 31 March 2004	15,396,444	1,722,156

20. Capital Commitments

Capital Commitments for which no provision has been made in these financial statements, were as follows:

	31 March 2004 £000	31 March 2003 £000
Contracted but not provided for	15,158,637	17,824,501

21. Financial Commitments

Commitments under operating leases:

	Land and Buildings		Other	
	31 March 2004 £000	31 March 2003 £000	31 March 2004 £000	31 March 2003 £000
The Department was committed to making the following payments during the next year in respect of operating leases expiring:				
Within one year	7,883	6,284	15,178	12,844
Between two and five years	13,733	11,644	69,413	14,483
After five years	168,517	144,678	48,596	109,828
	190,133	162,606	133,187	137,155

22. Private Finance Initiative (PFI) Commitments

22.1 The payments made during the year in respect of on and off Balance Sheet PFI transactions were £605,139,000 (2002-03: £542,048,000).

22.2 The service payments which the Department is committed to make during the year 2004-05 are analysed below by time-bands specifying the period in which the individual commitment expires:

	31 March 2004 £000	31 March 2003 £000
In the 2nd to 5th years	181,324	225,325
In the 6th to 10th years	94,986	126,969
In the 11th to 15th years	49,693	3,820
In the 16th to 20th years	34,312	15,830
In the 21st to 25th years	185,566	127,451
In the 26th to 30th years	54,252	75,531
In the 31st to 35th years	1,300	–
In the 36th to the 40th years	30,060	–
In the 41st to the 45th years	–	6,250

The following information is provided for those schemes assessed as off Balance Sheet:

Project Description	Capital Value* £000	Contract Start**/ End Dates	
Training, Administration and Financial Management Information System (TAFMIS): Provision of training administration and financial management information systems to the Army Training and Recruiting Agency (ATRA)	41,000	Aug 1996	Aug 2007
Hazardous Stores Information System (HSIS): Provision of an information management service for hazardous stores safety datasheets with 2,000 users	1,000	Feb 1997	Dec 2007
Defence Fixed Telecommunications System (DFTS): Integration of 50 fixed telecommunications networks used by the Armed Forces and MoD, including the delivery of voice, data, LAN interconnect and other WAN services	70,000	Jul 1997	Jul 2007
Electronic Messaging Service: Interoperability of messaging services for the Army	33,000	Apr 1997	Apr 2007
Medium Support Helicopter Aircrew Training Facility (MSHATF): Provision of 6 flight simulator training facilities, covering three different types of helicopter, at RAF Benson	114,000	Oct 1997	Oct 2037
Hawk Synthetic Training Facility: Provision of replacement simulator training facilities at RAF Valley	19,000	Dec 1997	Dec 2015
Joint Services Command and Staff College (JSCSC): Design and delivery of a new tri-Service Command and Staff Training College infrastructure and supporting services, including single residential accommodation and married quarters (of which £29 million relates to on-balance sheet)	92,800	Jun 1998	Jun 2028
Attack Helicopter Training Service: Provision of full mission simulator, 3 field deployable simulators, ground crew, maintenance and armament training	165,000	Jul 1998	Sep 2027
Family Quarters Yeovilton: Provision of married quarters accommodation for 88 Service families at RNAS Yeovilton	8,200	Jul 1998	Jul 2028
RAF Lyneham Sewage Treatment: Refurbishment of existing sewage treatment facilities, serving a population of 7,000, to meet regulatory standards at RAF Lyneham	3,809	Aug 1998	Aug 2023
Tidworth Water and Sewerage: Pathfinder project providing water, sewerage and surface water drainage, serving a population of 12,000 military and dependants at Tidworth.	5,000	Feb 1998	Aug 2018
RAF Mail: Provision of informal messaging services for the RAF	12,000	Nov 1998	Nov 2008
Fire Fighting Training Units: Provision of fire fighting training for the Naval Recruiting and Training Agency (NRTA)	22,500	Apr 1999	Apr 2019
Light Aircraft Flying Training: Provision of flying training and support services for Air Experience Flying (AEF) and University Air Squadron (UAS) Flying Training	20,000	Apr 1999	Mar 2009

Project Description	Capital Value* £000	Contract Start**/ End Dates	
Tornado GR4 Synthetic Training Service: Provision of aircraft training service at RAF Marham and RAF Lossiemouth	61,700	Jun 1999	Jun 2031
Army Foundation College: Provision of teaching and training facilities for the further vocational education and military training of high-quality school leavers	73,400	Feb 2000	Dec 2029
RAF Cosford/RAF Shawbury Family Quarters: Provision of married quarters accommodation for 145 Service families at RAF Cosford and RAF Shawbury	15,100	Mar 2000	Jun 2025
Central Scotland Family Quarters: Provision of married quarters accommodation for 164 Service Families in Central Scotland	24,700	Aug 1999	Jan 2021
Tri-Service Material Handling Equipment: Provision of Tri-Service materials handling capability	35,000	Jun 2000	Jun 2010
Commercial Satellite Communication Service (INMARSAT): Provision of world-wide commercial satellite communication system for Royal Navy Ships to run for five years	2,600	Mar 2001	Mar 2006
E3D Sentry Aircrew Training Service: E3D Sentry simulators instructors and maintainers at RAF Waddington	6,900	Jul 2000	Dec 2030
Lynx MK 7 and 9 Aircrew Training Service: Provision for simulator training facility for Lynx MK 7 and 9 helicopter aircrew	15,400	Jul 2000	Jul 2025
Tri-Service White Fleet: Provision, management and maintenance of support vehicles in the UK	40,000	Jan 2001	Jan 2011
Family quarters at Wattisham: Provision of married quarters accommodation for 250 service families	34,200	May 2001	Mar 2028
Family quarters at Bristol / Bath / Portsmouth: Provision for married quarters accommodation for 317 service families	78,000	Nov 2001	Sep 2028
Defence Housing Executive Information Systems (DOMIS): Provision for a management information system for the Defence Housing Executive	11,600	Oct 2001	Sept 2010
Marine Support to Range and Aircrew Training: Provision of management, manning, operation and maintenance of Air Support Craft and Range Safety Craft	11,800	Dec 2001	Dec 2012
Astute Class Training: Provision of a training environment for crewmen and maintainers to support Astute Class submarines for 30 years	79,600	Sep 2001	Sep 2031
Strategic Sealift (RoRo): Provision of strategic sealift services based on six RoRo ferries in support of Joint Rapid Reaction Force (JRRF) deployments	175,000	Jun 2002	Dec 2024
Field Electrical Power Supplies (FEPS): Provision of generator sets to support operational electrical requirements in the field	73,500	Jul 2002	Jun 2022
Material Handling Equipment: Provision of tri-service material handling equipment for Army, Navy and RAF storage depots	12,300	Aug 2002	Jul 2010
Aquatrine Project A: Provision of water and waste water services	154,000	Apr 2003	Nov 2028
Hayes Records and Storage: Pan-Government Records Management and Archive Services	11,100	Sep 2003	Sep 2028
Defence Sixth Form College: Development of a sixth form college to help meet the future recruitment requirements in the Armed Forces and MoD Civil Service	20,000	Jun 2003	Aug 2033
Colchester Garrison: Redevelopment, rebuilding and refurbishment to provide accommodation and associated services (messing, education, storage, workshops)	539,000	Feb 2004	Feb 2039
Skynet 5: Range of satellite services, including management of existing Skynet 4 satellites	1,079,000	Oct 2003	Feb 2018
<p>* The capital value is based on private sector partners' capital investment, where known, or otherwise the capital value of the public sector comparator.</p> <p>** The dates when the contracts were signed.</p>			

The following PFI projects, where service delivery has commenced, are treated as on balance sheet and their service payment commitments for the year 2004-05 are included in the table shown above: Lossiemouth FQs; RAF Fylingdales; Defence Helicopter Flying School; Defence Animal Centre; Naval Communication; Provision of storage facilities; Main Building Redevelopment, part of the Joint Services Command and Staff College, Heavy Equipment Transporter and Defence Electronic Commerce Services.

Since the year ended, the Department has signed a PFI contract for Devonport Support Services for a period of 25 years. The contract is for the provision of support services and Fleet accommodation centre services at Devonport Naval Base (HMS Drake).

No specific contingent liabilities have been identified in respect of the PFI contracts listed above.

23. Contingent Liabilities and Contingent Assets Disclosed Under FRS 12

Contingent Liabilities

Contingent liabilities estimated at some £1,127,000,000 (2002-03: £1,318,000,000) were identified. Indemnities issued to contractors and suppliers that were quantifiable as at 31 March 2004 amounted to £852,000,000 (2002-03: £1,162,000,000).

Contingent Assets

A US salvage company, Odyssey Marine Exploration, has found what is believed to be the wreck of HMS Sussex, which sank in the Western Mediterranean in 1694 carrying gold and silver coins estimated to be valued at the time at £1 million. If confirmed as HMS Sussex the wreck and its contents are legally the property of Her Majesty's Government.

A licensing agreement was signed on 27 September 2002 between the Disposal Services Agency of the Ministry of Defence, on behalf of Her Majesty's Government and Odyssey for further archaeological exploration of the wreck of HMS Sussex and recovery of artefacts et cetera. Under the agreement the net proceeds of the sale of coins and other marketable artefacts will be shared between the two parties. Insufficient certainty exists at present as to the presence or value of any potential recovery of artefacts to quantify the contingent asset.

24. Contingent Liabilities Not Required To Be Disclosed Under FRS 12 But Included For Parliamentary Reporting And Accountability

24.1 Quantifiable

MoD has entered into the following quantifiable contingent liabilities by offering guarantees, indemnities or by giving letters of comfort. None of these is a contingent liability within the meaning of FRS12 since the likelihood of a transfer of economic benefit in settlement is too remote.

	1 April 2003	Increase in year	Liabilities crystallised in year	Obligation expired in year	31 March 2004	Amount reported to Parliament by departmental minute
UNRESTRICTED						
Indemnities						
Residual liability for the remediation of unidentified contamination in parts of the former Rosyth Naval Base which has been sold to Rosyth 2000 plc.	Up to £1,000k				Up to £1,000k	n/a
Termination liabilities arising out of MoD's association with the Research Council under the Joint Grants Scheme.	£17,620k	NIL	NIL	NIL	£17,620k	£17,620k
Liabilities arising from insurance risk of exhibits on loan to the Army, Navy and RAF Museums.	£1,489k	£476k (1)	NIL	NIL	£1,965k	
RESTRICTED						
Details on restricted liabilities not given because they are sensitive due to commercial confidentiality, national security, or where public knowledge of a guarantee could prompt claims from third parties.						

Explanation of movement

(1) General Reassessment of risk.

Reconciliation between disclosed amount and amount reported to Parliament

The last comprehensive valuations were as reported in the 2001-02 Treasury return.

24.2 Unquantifiable

MoD has entered into the following unquantifiable contingent liabilities by offering guarantees, indemnities or by giving letters of comfort. None of these is a contingent liability within the meaning of FRS12 since the likelihood of a transfer of economic benefit in settlement is too remote.

Unrestricted Indemnities

- Indemnity given in relation to the disposal of Gruinard Island in the event of claims arising from the outbreak of specific strains of anthrax on the Island.
- Indemnity to Devonport Royal Dockyards Ltd (DRDL) in respect of nuclear risks under the Nuclear Installations Act 1965.
- Indemnity to the Babcock Group in respect of nuclear risks under the Nuclear Installations Act 1965.
- Indemnities to Devonport Royal Dockyards Ltd (DRDL) and the Babcock Group in respect of non-nuclear risks resulting from claims for damage to property or death and personal injury to a third party.
- Product liability to British Aerospace in respect of work carried out by third party contractors on aircraft for which BAe are Design Authority and for which BAe, at MoD's request provide the third party contractor with design advice and verification.

Restricted Indemnities

- Details on restricted liabilities are not given because they are sensitive due to commercial confidentiality and national security.
- Explanation as to why unquantifiable: These liabilities are unquantifiable due to the nature of the liability and the uncertainties surrounding them.

25. Post Balance Sheet Events

The Defence White Paper, published in December 2003, set out the Department's analysis of the future security environment, the implications for defence, strategic priorities and how it intends to adapt its planning and force structures to meet potential threats. Using the policy baseline established in the White Paper and following a rigorous examination of force structure, specific equipment requirements and supporting infrastructure, manpower and organisational structure, the Secretary of State set out, in July 2004, the changes the Department should make to the force structure and its key capacity requirements for the future.

26. Notes to Schedule 5

The net costs of the Departmental Objectives are determined as follows:

Objective 1: Achieving success in the tasks we undertake

This objective comprises the following:

	2003-04			2002-03		
	Gross £000	Income £000	Net £000	Gross £000	Income £000	Net £000
Operations	1,236,721	(3,566)	1,233,155	1,117,429	–	1,117,429
Other military tasks	1,733,706	(74,893)	1,658,813	1,658,433	(52,743)	1,605,690
Contributing to the community	419,977	(59,784)	360,193	564,923	(59,129)	505,794
Helping to build a safer world	427,868	(198,752)	229,116	411,562	(165,811)	245,751
Total	3,818,272	(336,995)	3,481,277	3,752,347	(277,683)	3,474,664

Costs are identified as follows:

- *Operations* comprises the additional costs incurred deploying the armed forces in military operations, e.g. in Iraq, over and above the costs of maintaining the units involved at their normal states of readiness;
- *Other military tasks* includes ongoing military commitments, e.g. to security in Northern Ireland and Overseas Commands, and the costs of identifying and countering the threat of terrorist attack on the UK mainland, and of maintaining the integrity of UK waters and airspace;
- *Contributing to the community* includes ongoing support activities, e.g. search and rescue, administration of cadet forces. In addition, it includes the costs of assistance to other Government Departments and agencies, e.g. in counter drugs operations; and
- *Helping to build a safer world* includes the costs of defence diplomacy undertaken to build confidence and security with our allies. It also includes the Department's support of wider British interests.

Objective 2: Being ready to respond to the tasks that might arise

The costs of delivering the military capability to meet this objective are analysed among force elements of the front line commands, including joint force units where these have been established, and a small number of centrally managed military support activities.

In addition to the direct operating costs of the front line units, they include the attributed costs of logistical and personnel support, identified by reference to the output costs of supplier Management Groupings.

In common with all Objectives, these also contain a share of the costs of advising ministers and accountability to Parliament, and apportioned overheads for head office functions and centrally provided services. The total comprises the full costs, including support services, of force elements grouped under the following headings:

	2003-04			2002-03		
	Gross £000	Income £000	Net £000	Gross £000	Income £000	Net £000
Royal Navy						
Aircraft carriers	299,679	(6,880)	292,799	421,865	(5,550)	416,315
Frigates and Destroyers	1,744,387	(35,195)	1,709,192	3,080,057	(51,136)	3,028,921
Smaller warships	293,095	(9,139)	283,956	504,617	(17,923)	486,694
Amphibious ships	344,496	(5,581)	338,915	436,480	(6,763)	429,717
Strategic sealift	2,691	(70)	2,621	15,283	(655)	14,628
Fleet support ships	360,029	(12,507)	347,522	474,224	(13,110)	461,114
Survey and other vessels	160,030	(3,249)	156,781	232,336	(8,923)	223,413
Naval aircraft	1,429,942	(37,403)	1,392,539	1,246,648	(25,599)	1,221,049
Submarines	4,904,164	(42,492)	4,861,672	5,662,233	(73,110)	5,589,123
Royal Marines	617,431	(13,078)	604,353	481,415	(4,615)	476,800
	10,155,944	(165,594)	9,990,350	12,555,158	(207,384)	12,347,774
Army						
Field units	6,585,112	(212,672)	6,372,440	7,613,358	(231,653)	7,381,705
Other units	2,519,327	(169,006)	2,350,321	3,031,434	(184,282)	2,847,152
	9,104,439	(381,678)	8,722,761	10,644,792	(415,935)	10,228,857
Royal Air Force						
Strike/attack and offensive support aircraft	2,464,139	(57,067)	2,407,072	3,212,034	(74,360)	3,137,674
Defensive and surveillance aircraft	2,140,241	(28,380)	2,111,861	2,772,787	(50,136)	2,722,651
Reconnaissance and maritime patrol aircraft	370,066	(19,639)	350,427	737,534	(26,796)	710,738
Tankers, transport and communications aircraft	1,079,959	(40,135)	1,039,824	1,257,826	(46,723)	1,211,103
Future capability	345,722	(6,515)	339,207	312,281	(6,003)	306,278
Other aircraft and RAF units	784,155	(30,982)	753,173	1,131,165	(40,584)	1,090,581
	7,184,282	(182,718)	7,001,564	9,423,627	(244,602)	9,179,025
Centre Grouping						
Joint and multinational operations	341,411	(193,658)	147,753	628,716	(55,623)	573,093
Centrally managed military support	310,388	(73,987)	236,401	549,567	(80,464)	469,103
Maintenance of war reserve stocks	700,089	(21,470)	678,619	909,204	(12,990)	896,214
	1,351,888	(289,115)	1,062,773	2,087,487	(149,077)	1,938,410
Total Objective 2	27,796,553	(1,019,105)	26,777,448	34,711,064	(1,016,998)	33,694,066

Note:

The 2003-04 and 2002-03 figures shown above are not comparable. 2002-03 was an exceptional year when, some £4,000 million in the value of fixed assets was written down as a direct impact of the Quinquennial Valuation of fixed assets. The impact of the substantial write down also had the effect of reducing the depreciation charge in 2003-04 by some £1,200 million. A further £1,700 million in exceptional charges were also made in last year's accounts in respect of nuclear decommissioning provisions following a strategic review and changes in methodology carried out by BNFL, and the Quinquennial review of AWE. The balance of the reduction is accounted for by various costs, as listed in Note 3.

Most groupings are self explanatory. The following however should be noted:

- *Smaller warships* includes mine hunting and offshore patrol vessels;
- *Amphibious ships* includes assault ships providing platforms for landing craft and helicopters, and Royal Fleet Auxiliary landing support ships;
- *Strategic sealift* is the Roll-On Roll-Off ferry facility supporting the Joint Rapid Reaction Force;
- *Fleet support ships* includes Royal Fleet Auxiliary ships providing tanker and replenishment support to warships;
- *Survey and other vessels* includes ocean and coastal survey and ice patrol ships;
- *Naval aircraft* include Sea King, Lynx and Merlin helicopters deployed in anti-submarine, airborne early warning, Royal Marine support, and reconnaissance and attack roles;
- *Submarines* includes the operating costs of submarines and support of nuclear propulsion and weapons systems, including nuclear decommissioning;
- *Army – Field units* includes 1 (UK) Armoured Division, 3 (UK) Division, Joint Helicopter Command and Theatre troops;
- *Army – Other units* includes Regional Divisions and Land support and training;
- *Strike/attack and offensive support aircraft* includes Tornado GR1/GR1A/GR1B/GR4/GR4A, Joint Force Harrier and Jaguar aircraft deployed in strike/attack and offensive support roles;
- *Defensive and surveillance aircraft* includes Tornado F3 and Sentry AEW1 aircraft deployed in UK air defence, and NATO and UN peacekeeping commitments;
- *Reconnaissance and maritime patrol aircraft* includes Canberra and Nimrod R1 aircraft deployed on reconnaissance, and Nimrod MR2 aircraft on maritime patrol. (Tornado GR1A/4A included in *strike/attack and offensive support aircraft* also undertake reconnaissance roles);
- *Tankers, transport and communications aircraft* includes C-17, Hercules, Tristar and VC10 aircraft providing air transport and air to air refuelling, and smaller transport aircraft (BAe 125/146 and Squirrel helicopters) used in a rapid communications role;
- *Future capability* includes primarily the preparatory costs for the introduction of the Typhoon aircraft;
- *Other aircraft and RAF units* includes ground forces (e.g. the RAF Regiment) and miscellaneous aircraft not included elsewhere;
- *Joint and multinational operations* includes Chief of Joint Operations HQ and the costs less receipts of UK participation in NATO;
- *Centrally managed military support* includes intelligence operational support and Special Forces; and
- *Maintenance of war reserve stocks* includes the holding costs and charges of munitions and other stocks, above the levels required for planned consumption.

Objective 3: Building for the future

This objective comprises the following elements:

	2003-04			2002-03		
	Gross £000	Income £000	Net £000	Gross £000	Income £000	Net £000
Research	1,007,082	(75)	1,007,007	972,089	–	972,089
Equipment programme	2,204,899	(56,131)	2,148,768	2,514,938	(60,547)	2,454,391
Total	3,211,981	(56,206)	3,155,775	3,487,027	(60,547)	3,426,480

- *Research* comprises the costs, including capital charges, of the Research Building Block, and research expenditure incurred by other TLBs; and
- *Equipment Programme* refers to the administration and programme costs, primarily of the Defence Procurement Agency, associated with specifying requirements for and procurement of fighting equipment and other assets. The values of fixed asset additions are shown in Note 9.

Attribution to Objectives

Gross expenditure of £27,155 million (75.6%) (2002-03 - 76.4%) and Operating Income of £692 million (49.0%) (2002-03 – 48.9%) were allocated to tasks, force elements or activities directly supporting the Objectives. The rest was apportioned in one of two ways:

- by means of cost attributions to "customer" Management Groupings, using local output costing systems to identify the full local costs of services provided. Cost attributions from suppliers are analysed onward to final outputs on advice from the recipients. If specific advice is not given, attributed costs are assumed to follow the same pattern as locally incurred expenditure;
- as an element of central overhead, shared among Objectives in proportion to all other attributions. The force elements etc. described above receive a share of the expenditure and income components of these overheads, on the basis of their net costs. The central overheads comprised:

	2003-04			2002-03		
	Gross £000	Income £000	Net £000	Gross £000	Income £000	Net £000
Support for ministers and Parliament	18,971	(33)	18,938	9,380	(3)	9,377
Departmental corporate services	1,356,300	(91,033)	1,265,267	1,164,202	(279,767)	884,435
Strategic management	207,188	(11,911)	195,277	507,630	(9,562)	498,068

- *Support for ministers and Parliament* includes the central provision of advice to ministers and the costs, wherever incurred in the Department, of dealing with Parliamentary business;
- *Departmental corporate services* comprises internal support functions, e.g. payment of bills, payroll administration, and housing and medical care for service personnel; and
- *Strategic management* comprises Departmental policy making functions in strategic, personnel, scientific and medical matters.

Capital employed

The deployment of the Department's capital in support of its objectives does not follow the pattern of operating costs. Net assets totalling £61,252 million (75.5%) support the military capability required to meet Objective 2. The remainder comprises assets wholly attributable to tasks within Objective 1 (£3,689 million – 4.5%), and intangible assets, fighting equipment and other assets under construction, and assets related to equipment procurement within Objective 3 (£16,218 million – 20.0%), and payment of War Pensions and Allowances (-£12 million).

27. Segmental Analysis of Net Resource Outturn by Top Level Budget (TLB) Holders

	2003-04						2002-03
	Other Current Expenditure	Grants	Operating Appropriations -in-Aid	Total Net Resource Outturn	Total Net Resource Estimate	Total Net Outturn Compared with Estimate	Total Net Resource Outturn
	£000	£000	£000	£000	£000	£000	£000
TLB HOLDER							
Commander-in-Chief Fleet	3,383,418	–	(16,884)	3,366,534	3,439,409	72,875	4,998,342
General Officer Commanding (N Ireland)	654,891	–	(1,550)	653,341	656,399	3,058	717,454
Commander-in-Chief Land Command	5,077,714	83	(215,694)	4,862,103	5,110,107	248,004	5,483,101
Air Officer Commanding-in-Chief RAF Strike Command	3,497,856	–	(28,760)	3,469,096	3,569,005	99,909	4,829,141
Chief of Joint Operations	571,667	–	(36,182)	535,485	499,046	(36,439)	678,989
Chief of Defence Logistics	8,272,492	9,987	(331,891)	7,950,588	8,643,801	693,213	11,183,743
2nd Sea Lord/Commander-in-Chief Naval Home Command	743,638	–	(47,003)	696,635	691,566	(5,069)	740,124
Adjutant General	1,785,636	–	(28,500)	1,757,136	1,728,922	(28,214)	1,748,733
Air Officer Commanding-in-Chief RAF Personnel & Training Command	1,146,606	–	(142,337)	1,004,269	1,026,283	22,014	1,086,581
Central	3,052,370	120,927	(524,511)	2,648,786	2,591,628	(57,158)	2,766,889
Defence Procurement Agency	4,861,520	(1,717)	(42,198)	4,817,605	4,702,526	(115,079)	5,083,169
Major customers' research budgets*	419,842	–	(75)	419,767	422,904	3,137	414,578
Total (RFR 1)	33,467,650	129,280	(1,415,585)	32,181,345	33,081,596	900,251	39,730,844
Total (RFR 2) (Note 2)	1,233,155	–	–	1,233,155	1,413,610	180,455	1,117,429
Total (RFR 3) (Note 1)	1,116,047	–	–	1,116,047	1,158,005	41,958	1,165,411
Total	35,816,852	129,280	(1,415,585)	34,530,547	35,653,211	1,122,664	42,013,684
Income netted off against operating expenditure between TLB holders	(3,279)		3,279				
Items netted off against other operating costs but treated as Appropriations in Aid for Schedule 1 (Note 4)	84,201		(84,201)				
Excess Operating Appropriations-in-Aid			85,315	85,315		(85,315)	
Items treated as CFERs to be allocated	1,995		33,369	35,364		(35,364)	
	35,899,769	129,280	(1,377,823)	34,651,226	35,653,211	1,001,985	42,013,684
				Sch 1	Sch 1		Sch 1

* Major customers' research budgets is not a Top Level Budget (TLB) Holder.

Note 1: War Pensions and Allowances – Programme Costs

The Chief Executive of the Veterans Agency is not a Top Level Budget Holder, but exercises all the responsibilities for the programme costs.

Note 2: Conflict Prevention (RFR2)

The analysis of the Conflict Prevention costs is as follows:

Operations	Operating Costs £000
BALKANS	103,584
AFGANISTAN (includes VERITAS, FINGAL and JACANA)	35,865
IRAQ	1,050,563
CONGO	1,003
SIERRA LEONE	735
EUFYROM	808
	1,192,558
Programme Expenditure	40,597
TOTAL	1,233,155

The Department's cost of operation in Iraq (Operation TELIC) forms the main component of the above costs. Further details and assumptions used in arriving at these figures are as set out below:

General

1. The MoD had £1.539 bn (2002-03: £1bn), including £334 million (2002-03: £400 million) for capital expenditure, in voted provision for Operation TELIC in the Spring Supplementary Estimates 2003-04.
2. The resource outturn in 2003-04 for the operation was £1.051 bn (2002-03: £629 million), which reflects the costs for the period to 31 March 2004.
3. The capital expenditure for Operation TELIC paid and accrued in the financial statements amounted to £260 million (2002-03: £218 million)
4. Full details of the Department's aims and performance assessment for Operation TELIC are provided in the Departmental Performance Report.

Assumptions

The following assumptions have been used in arriving at the net resource Outturn figures for Operation TELIC:

1. In accordance with the accounting principles agreed with HM Treasury, the Department has identified the costs of Operation TELIC on the basis of net additional costs. Expenditure such as wages and salaries are not included as they would have been incurred in any event, and the costs of activities such as training and exercises, which have been cancelled because of the operational commitment, have been deducted;
2. There have been no fixed asset impairments resulting from the operation in Iraq, though cost of equipment destroyed in the conflict is included. It is likely that repair and refurbishment costs will need to be incurred in the future in order to bring the equipment back into full operational use; these costs will be reflected in the Operating Cost Statement in the year in which they are incurred;

3. Stock consumption was determined by taking the opening stock in Iraq on 1st April 2003, adding to it issues shipped during the year, deducting stock shipped back to the UK and the year-end stock figure; the latter amount was assessed on the basis of various stock returns received from Iraq. Stock consumption is charged at a gross cost and the related stock provision movements are shown under the stock provision line in the Operating Cost Statement.
4. Write offs of fighting equipment and GWMB, charged in the financial statements, are based on actual records.

28. Financial Instruments

FRS 13, Derivatives and Other Financial Instruments, requires disclosure of the role which financial instruments have had during the period in creating or changing the risks an entity faces in undertaking its activities. Because of the largely non-trading nature of its activities and the way in which government Departments are financed, the Department is not exposed to the degree of financial risk faced by business entities. Moreover, financial instruments play a much more limited role in creating or changing risk than would be typical of the listed companies to which FRS 13 mainly applies. Financial assets and liabilities are generated by day-to-day operational activities and are not held to change the risks facing the Department in undertaking its activities.

Liquidity risk

The Department's revenue and capital resource requirements are voted annually by Parliament and are therefore not exposed to significant liquidity risks.

Interest rate risk

A significant proportion of the Department's financial assets and liabilities carry nil or fixed rates of interest. The exposure to interest risk is therefore not significant.

Foreign currency risk

The Department enters into forward purchase contracts annually with the Bank of England to cover the majority of its foreign exchange requirements for the following year. The details of the outstanding foreign currency contracts were as follows:

Currency	Foreign Currency US\$/Euro 000	Weighted Average Exchange Rate (=£1)	31 March 2004 Sterling £000	31 March 2003 Sterling £000
2004/ 2005 delivery (2003/ 2004 delivery)				
US Dollar	1,520,000	1.5677	969,581	(870,378)
Euro	1,350,000	1.4253	947,173	(696,466)
2005/ 2006 delivery				
US Dollar	1,558,000	1.7463	892,182	
Euro	1,278,000	1.4289	891,949	
Total			<u>3,700,885</u>	<u>(1,566,844)</u>

The 31 March 2004 mid-market closing rates for US Dollar and Euro were £/\$ 1.8378 and £/Euro 1.4955 respectively.

Fair values

Financial assets

The Department's financial assets include investments and loans made in Trading Funds, MoD agencies funded through a Trading Fund and QinetiQ, a Self Financing Public Corporation. The net assets of these bodies (excluding MoD loans) and the interest rates applicable to these loans are shown in Note 10. Other financial assets fair values approximate to their book values.

Financial liabilities

The Department's liabilities include loans from National Loans Fund Obligations under finance leases and PFI contracts and a loan from AWE amounting in total to £368.9 million (2002-03: £155.3 million). The fair values of these liabilities will be different from their book values but since these represent only 2.4% of the gross liabilities and provisions, the impact on the Department's net assets will not be material. The fair values of provisions for liabilities and charges are not materially different to their book values which are stated after discounting at the Treasury rate of 3.5%. Other liabilities fair values approximate to their book values.

29. Losses and Special Payments

Losses and Special Payments shown below fall within the following two categories:

- A) Closed cases where all the case work has been finalised and the cases have been formally signed off. These are reported below in accordance with Treasury's Resource Accounting Manual.
- B) Cases where formal sign off cannot, and has not, taken place until all the work necessary to establish the validity and the exact amount of the loss has been concluded. Where an individual loss or special payment exceeds £100,000, this is disclosed in the Accounts under "Advance Notification". The amounts stated under Advance Notification are the best estimates and are reflected in the Accounts where appropriate. Advance Notification also includes cases brought forward from the previous year. Where these cases have been formally signed off during the year, they are shown under the closed cases section of the Losses Statement.

CLOSED CASES	
Losses Statement	£000
Total (excluding gifts): 12,847 cases	460,945
Details (cases over £100,000)	
Cash Losses	
New premises were constructed for a non-synopsis welfare facility contrary to the rules on the provision of assistance to non-MoD agencies. The incident was subject to investigation and limitations on the use of property management funds reinforced. (LAND)	274
British Defence Staff Washington: Write off of a control account balance. (CENTRAL)	189
Property Management arrangements were erroneously used to refurbish non-synopsis welfare facilities in Germany. The incident was investigated by a Board of Inquiry which found mismanagement rather than any impropriety. (LAND)	148
A cash loss of £137,895 has been incurred as the result of the Navy Days event which took place in Devonport Naval Base during August 2002. A forecast of income and expenditure for the Navy Days 2002 assumed a breakeven position with 60,000 visitors attending. Although expenditure fell within the budget, income was lower than anticipated mainly due to reduced visitor numbers (44,551). (DLO)	138
Claims Waived or Abandoned	
Treasury approval has been obtained to abandon a £49.987M claim against the contractor following cancellation of project VIXEN in February 1997. The MoD received £14.550M in compensation but agreed to pay £3.504M in Treasury Solicitor costs. (DPA)*	38,941

Losses Statement	£000
In February 2002 HM Treasury agreed to waive a claim of £2.3 million in respect of Edinburgh House. Subsequently, this transfer has been included in an agreement signed with the Government of Gibraltar (GOG), the "Lands Memorandum", gifting a number of properties to GOG. (CJO)	2,339
Treasury approval has been granted to write off £309,405.76 as a claim abandoned/waived. This loss of revenue occurred as a result of incorrect charging for Operational Sea Training between October 1995 and March 1998. Operational Sea Training is provided to foreign navies in return for full payment, but at the time of the loss the rules for charging were not clearly expressed. (DLO)	309
A contract was placed with Dieselpart Ltd on the 1st February 1995 for a contract period of three years for the reconditioning of pumps and water pumping equipment. Dieselpart Ltd went into liquidation in March 1997, causing the net loss of £230,448.45 for rejected work and additional cost. (DLO)	230
Claim against EDS in respect of payroll services waived in accordance with AFPAA Amended Contract FY03/04. (CENTRAL)	131
Stores and other Losses	
Following the closure of the Defence Storage and Distribution Centre, Sub Depot (formerly ABSDA Sub Depot) Thatcham in March 2000, finalisation of the Sub Depot's equipment and stores accounts revealed that, in a number of instances, accounting procedures covering movement of equipment and stores had not been fully complied with. As a result the audit trail was incomplete and, whilst no physical loss has been proven, the value of all stores unaccounted for on closure must be written off as a loss. (DLO)*	1,889
A Ptarmigan Radio Relay vehicle crashed during an Exercise and was damaged beyond repair. The accident was fully investigated by a Board of Inquiry and Accident Investigation teams. (LAND)	1,055
Water seeped through the seals on laptop cases following their storage, in the open, resulting in the loss of JFACHQ laptops. (STC)	160
Fire in a workshop building at School of Electrical and Mechanical Engineering, Bordon on 26 Sep 02. Investigation by the Defence Fire Service determined that the cause of the fire was an accident. There were no injuries or fatalities. (AG)	159
Constructive Losses	
The Departmental Resource Accounts (DRAC) for 2002/03 identified the impact of reviewing the accounting treatment for the Submarine facility at Devonport to reflect planned workload. The impact of this change in accounting treatment was a write down of £287 million which is classified as a Constructive Loss. (DLO)*	287,000
A decision was taken in taken in 2003 to withdraw from the Multi Role Armoured Vehicle (MRAV) programme. The strategic environment had changed markedly, with much greater emphasis on rapid deployability and expeditionary operations. The design of MRAV could not effectively meet this change in requirement. A constructive loss of £48M was incurred covering the UK costs of participating in the multilateral collaborative programme up to the point of withdrawal. (DPA)	48,000
The in service date for the Astute Class Training Service (ACTS) PFI project will be delayed as a consequence of slippage to the Astute submarine programme. This has resulted in a constructive loss. (DPA)	31,373
Write-off of equipment that, owing to the recent closure of a number of security force bases in Northern Ireland and reductions in operational activity, is no longer of use. (GOCNI)	18,088
Following the decision to cancel project PASCO a contract termination agreement was signed in July 2003. Costs incurred up to this period have been written off as a constructive loss. (DPA)	12,245
A constructive loss was incurred following a performance/cost trade decision in 2003 not to pursue a digital integration of the Rangeless Airborne Instrumented briefing System (RAIDS) training system onto Tornado F3. The decision was made on grounds of value for money in the light of the significant capability improvements already delivered by RAIDS at the lesser level of integration. (DPA)	5,269
A constructive loss has been incurred in relation to equipment purchased under an Urgent Operational Requirement (UOR) in June 1999. The equipment was never fully accepted in to service. Disposal action was delayed in light of further conflicts but in June 2003 it was confirmed that there had been no requests for the equipment in theatre. (DPA)	1,022
A project to design a suitable trailer to carry specialist equipment has been cancelled due to technical difficulties identified during trials. (DPA)	644
A fruitless payment of £355,033.31 was made for work initiated by Defence Clothing Integrated Project Team. A contract was agreed with NITECH Ltd to produce 40,000 Personal Combat Torches to issue to Special Forces. The work was started in 1993. However, when the torches were tested, they were found to be noisy due to the loose-fitting of the battery. Although this criterion was not mentioned in the contract, it made the torches unsuitable for Special Forces operations. (DLO)	355
The Defence Transport and Movements Agency (DTMA) Airlift Planning System (DAPS) was to introduce IT support to the military Air Transport planning process with the aim of ensuring the maximum possible usage of the Air Transport Force (ATF). Following the initial introduction of the system in July 02, a user evaluation was carried out and it was found that the DAPS operation was too slow to be useable. In addition, there were interface problems between DAPS and the Integrated Air Transport System (IATS). Further work may have overcome the DAPS / IATS interface problems. However, HQ 2 Gp (RAF) had decided to replace IATS with the Boeing Operational Command System (BOCS) and an interface between DAPS and BOCS was not possible. These problems resulted in a constructive loss of £204,760. (DLO)	205
RNAS Culdrose – Clean up costs incurred in 2003-04 following discharge of aviation fuel in June '02. Total amount incurred: £652,000. (FLEET)	66

Losses Statement	£000
Gifts	
International Courtesy Rules	
Supplies and services provided on a reciprocal basis to Commonwealth and Foreign Navy vessels during visits to British ports at Clyde, Portsmouth, Devonport and Gibraltar. (CENTRAL)	2,246
Other	
Ebrington Barracks, a Non-Core MoD site in Northern Ireland, transferred to the Office of the First Minister/ Deputy First Minister of the Northern Ireland Executive. (CENTRAL)	13,000
Spitfire TB752 and Hurricane LF751 transferred to the Royal Air Force Museum for onward loan to the Spitfire and Hurricane Memorial Building Trust. (DLO)	375
Combat Support Vehicles Support IPT (now known as General Support Vehicles) was instructed by the AL Hussein Project Team in 2003-04 that a number of Scammel Commanders were to be sold to the Jordanian Armed Forces. This had ministerial approval. The equipments were sent to IRAQ and then on to Jordan once they had been replaced by the new Heavy Equipment Transporter (HET). The write off of these equipments occurred in 03/04 and was £760,076.22. The receipt of monies for these equipments will be received into MoD Centre in 04/05 and is approximately £598k. The net loss to the MoD will be approximately £162k.(DLO)	162
De-mining equipment transferred to the Government of Kenya. (CJO)	156
Special payments	
Total: 284 cases	98,124
The Court of Appeal ruled against the Department and in favour of pensioners and widows affected by the Hulme judgement. In addition to reviewing attributable pension entitlement decisions made on the original basis of 'the balance of probabilities' and paying the cost of past pensions, the Department has set up provision for payment of compensation amounting to £77.2 million. (CENTRAL)	77,200
Compensation for loss of interest on Income Tax wrongly deducted from invalidity pensions. (CENTRAL)	12,600
An extra-contractual payment was approved arising from failure to provide fully working government furnished equipment in a timely manner for the Automated Message Switch Comcen Equipment Replacement Programme. (DPA)*	4,294
An extra-contractual payment was approved in relation to a submarine programme in June 2003. This followed a claim from the contractor that failure to supply submarine and threat data resulted in additional costs being incurred. (DPA)	3,700
Ex-gratia payments have been made during 2003-04 on account to British Nuclear Fuels plc and the United Kingdom Atomic Energy Authority towards the cost of treating and disposing of nuclear wastes and decommissioning plant at British Nuclear Fuels plc sites. The total amount paid to date: £1,341,000.(DPA)	166
An ex-gratia payment was made to a civilian employee, in respect of a complaint against the Department that was upheld. (DLO)	150
ADVANCE NOTIFICATION	
Previously notified in 2002-03	
A constructive loss arose from the UK Government decision not to proceed into production for either long range (loss £205 million) or medium range (loss £109 million) anti-tank guided weapons system. (DPA)*	314,000
DSMS formed part of the DLO Business Change Programme. During development, doubts surfaced about the programme's ability to deliver the expected benefits and its affordability leading to the programme being suspended and a potential constructive loss of £118 million. Work is still going on to finalise the case which is expected to be formally reported in 2004/05. (DLO)*	118,000
Re-negotiation of a contract for the Nimrod reconnaissance aircraft project has resulted in a possible claim abandoned (£39 million) and a constructive loss (£36 million). (DPA)*	75,000
Increased development costs relating to the Brimstone project arising from the non-availability of trial platforms. (DPA)*	9,165
A delay in the production of helicopter training course material has resulted in a potential write-off. (CJO)*	8,500
Communication equipment located on a remote hilltop site was stolen resulting in a possible stores loss	573
Metropole Building re-wire project (fraud); an alleged fraud during 1990-1995 which is still being investigated. (CENTRAL)*	500
A depletion and disposal of surplus stock has arisen due to improved processes and procedures as a result of the Strategic Defence Review and the formation of the Defence Logistics Organisation. It is not possible at this time to separate out the associated value from that arising as a result of ongoing activity but when the value has been determined it will be noted in the future year's Resource Accounts. (DLO)*	
Not previously notified	
Cash Losses	
British Defence Staff Washington: Net write off to regularise the various control accounts used to manage Foreign Military Sales in the USA. (CENTRAL)	8,332

Losses Statement	£000
A review of the Overseas Leave Travel Scheme and the Welfare Warrants Scheme Allowances indicated that a possible over payment has arisen at one of the Department's establishments. Initial assessment of the loss is £850,000 but investigations are proceeding. (PTC)	850
A combined cash loss of £199,263.24 relating to 4 un-reconciled control accounts emanating from the Anglo/French FRUGAL agreement on the development and production phases of the Jaguar aircraft is being investigated. This will result in write off action. (DLO)	199
Claims Waived or Abandoned	
Debts for the training of the Pakistan Navy during the period 1989 to 1991 are awaiting final write off authorisation; a provision for the full amount of the debt is reflected in the accounts. (2SL)	117
Stores and other Losses	
Loss as a result of a fire on an AS90 (self-propelled artillery gun) during Ex Saif Sareea 2 (Oman). Work is ongoing and the case is expected to be formally reported in 2004-05. (LAND)	2,202
Renegotiations in respect of the Hydrographic and Oceanographics Survey Vessels (SVHO) contract has resulted in a possible claim abandoned. (DPA)	1,034
Part of an accommodation block in Clive Barracks, Tern Hill was destroyed as a result of arson. Work is ongoing to finalise the case and is expected to be completed in 2004-05. (LAND)	500
Loss, through fire, of miscellaneous equipment during Operation TELIC. Investigations are ongoing and will be formally reported when the case work has been completed. (LAND)	375
Although no physical loss occurred, incomplete documentation on ammunition movements during an Operation in Afghanistan resulted in paper deficiencies in stock holding. The case will be finalised in 2004-05. Measures have been taken to prevent any recurrence. (LAND)	241
A constructive loss of £147,683.14 occurred in February 2001. It represents the write off of two C130J right-hand main undercarriage shock struts: the faulty struts were mislaid between the unit staffs and the CRILS team at RAF Lyneham. An urgent inquiry was convened between January and April 2002. (DLO)	148
A stores loss identified during a stock check when a signal squadron disbanded. A full investigation is ongoing and will formally be reported when the case work has been completed. (LAND)	132
A fire involving stores, fuel products and munitions destroyed buildings, tents and other property during an Operation. Investigations were conducted and found that the accident was not attributable to a single individual or specific act of negligence. (LAND)	104
Constructive Losses	
A loss of £205 million has arisen following the impairment of Chinook MK3 helicopters. (DPA)	205,000
A loss of £65 million has been incurred following impairment of an operational building (DPA)	65,000
The extended range ordnance modular charge system has been cancelled as a result of technical difficulties and could result in a possible write-off. (DPA)	34,540
The decision to suspend and now seek cancellation of the Remote Ammunitioning Facility Tamar at Devonport Naval Base will result in a constructive loss of £25M. The project was suspended in May 2002 following a Defence Ordnance Group study showing that the effects of potential ammunition explosions would be more localised than originally predicted. It was concluded that a satisfactory facility could be provided at the submarines' current berths within the Naval Base, without the need to construct a remote facility. Since then Devonport has established confidence that existing facilities can be used and full costs of the cancellation have become clearer. Ministerial approval is now being sought to cancel the project. Once this is received, the constructive loss will be formally reported in the 2004-05 accounts. (DLO)	25,000
Retrospective notification of a constructive loss of £18 million incurred as a result of the write off of Project ACCESS. A strategic Options Study, involving all stakeholders, identified the need for more joined up IS support to Attack Helicopter and agreed that further development of Project ACCESS should be cancelled. (DLO)	18,000
A contract to provide a centrifuge required to train aircrew for modern agile fast jet aircraft at high G force has been cancelled resulting in a potential write-off. (DPA)	14,400
There is the possibility of a loss in relation to the Harrier Night Bombing System. (DLO)	12,896
Advance notification that an estimated loss of £6.5M has been incurred through the procurement of new aircraft lifts that were to be fitted to Royal Naval Aircraft Carriers. A more cost effective solution has been found which takes advantage of technical advances and the lifts are no longer required. There were various expressions of interest in buying the aircraft lifts from the MoD, but none of these have resulted in a sale so far. A constructive loss write off case is now being prepared. (DLO)	6,500
Advance notification that an estimated loss of £1.5M has been incurred by the cancellation of the Oasis Stores and Engineering Project (OSEE). The development of the IT project was subject to delays and was not deemed fit for purpose in its current form when trials were undertaken in mid 2002. At the same time a review of DLO projects carried out by McKinsey & Co found that OSEE did not meet the new recommended criteria for the continuation of IT projects. It was therefore recommended that the project should be suspended. There has been some mitigation of the loss through an arrangement to purchase licences for a different product in use in the MoD and a constructive loss write off case is now being prepared. (DLO)	1,500

Losses Statement	£000
This loss relates to a settlement payment made to a service provider as a result of a termination of contract due to technical reasons relating to Defence Information Infrastructure (C) requirements. (DLO)	850
A constructive loss has arisen as a result of the need to re-design the roof at RNAS Yeovilton after it was found that the recently constructed roof obscured the view of the end of the runway from the Aircraft Control Tower. (FLEET)	618
The loss represents a settlement payment made to Elonex as a result of a technical breach of contract. (DLO)	600
A constructive loss arose in respect of the Voice Monitoring and Analysis Facility (VMAF) due to several factors including a limited capability and a change in policy placing the onus on contractors to provide their own capability testing. (DLO)	434
The Defence Communication Services Agency (DCSA) incurred training costs for infrastructure managers, in respect of the PASCO contract which was terminated; the costs in respect of the main contract were written off by DPA. (DLO)	290
A payment of £170,000 incurred due to the need to recover terminal boxes sent to a third party for disposal could result in a possible fruitless payment. (DLO)	170
Retrospective notification is given of a constructive loss, currently estimated at £151,000, incurred as a result of accidental scrapping of 45 Lynx Metal Tail Rotor Blades in October 2002, that were originally destined for recovery by industry. (DLO)	151
Special Payments	
Delays in supplying design information and equipment has resulted in a claim on the MoD relating to additional delay and dislocation costs. (DPA)	40,000
*Reported as an Advance Notification in 2002-03.	

30. Non-Operational Heritage Assets

The Department owns a range of non-operational heritage assets from historically significant defence equipment, through archive information, to museum and art collections. In accordance with HM Treasury policy non-operational heritage assets are normally valued except where:

- a) The cost of the valuation outweighs the benefits that the knowledge of the valuation would deliver; or
- b) it is not possible to establish a sufficiently reliable valuation.

On the above basis, no non-operational heritage assets, except land, were valued at the year-end.

30.1 The scope and diversity of the holdings of non-operational heritage assets which are not valued is illustrated by the examples detailed in the table below:

Item	Location	Description
HMS Victory	Portsmouth	HMS Victory is a 100 gun, first rate ship of the line, most famous for her role as Lord Nelson's Flagship at the Battle of Trafalgar. Victory was commissioned into the fleet in 1778 and serves today as flagship to 2nd Sea Lord/Commander-in-Chief Naval Home Command. Open to the public since 1928, Victory now attracts around 400,000 visitors a year.
Army Historic Aircraft Flight	Middle Wallop	Formed in the late 1980s, the flight consists of eight aircraft and makes about 14 public appearances between Easter and October.
Historic Gun Collection	DSDC Donnington	The museum currently holds a collection of 749 small arms of British and foreign origin together with a small number of larger weapons.
Battle of Britain Memorial Flight	RAF Coningsby	Formed in 1973 the Memorial Flight operates 11 mainly World War 2 aircraft that appear at in excess of 250 airshows, public events and state occasions. Memorial Flight aircraft can also be viewed by the public at their hangar at RAF Coningsby.
MoD Art Collection	Various locations	The MoD Art Collection comprises approximately 800 works of fine art and 250 antiques such as clocks and furniture. Many other miscellaneous items, such as photographs and manuscripts are contained in the archive. At the core of the collection are works commissioned by (and bequeathed to) the Admiralty during the 19th century, and those given to the Admiralty and to the War Office by the War Artists Commission at the end of Second World War. Items from the MoD art collections are displayed in conference rooms and senior officers' accommodation throughout the defence estate. The most important items are on permanent public display in the National Maritime Museum and on temporary loan to many other public museums and galleries.
Records and artworks	London, Taunton	The Admiralty and Institute of Naval Medicine Libraries and the Air Historical Branch (London) comprise text and records of historical and research items. Although not open to the public, access is available on application.
Artefacts, records and artworks	Various locations	Some 69 Regimental and Corps Museums exist across the country. Ownership of the buildings and contents of the museums varies between the MoD, local authorities and regimental associations. The museums, which are open to the public, trace the history of the regiments and comprise displays of uniforms, weapons, medals and records.

31. Entities within the Departmental Boundary

The entities within the boundary during 2003-04 were as follows:

Executive Agencies	Advisory Non-Departmental Public Bodies
Armed Forces Personnel Administration Agency	Advisory Committee on Conscientious Objectors
Army Personnel Centre	Animal Welfare Advisory Committee
Army Training and Recruitment Agency	Armed Forces Pay Review Body
British Forces Post Office	Dartmoor Steering Group
Defence Analytical Services Agency	Defence Nuclear Safety Committee
Defence Bills Agency	Defence Scientific Advisory Council
Defence Communication Services Agency	Independent Board of Visitors for Military Corrective Training Centres
Defence Dental Agency	National Employers' Liaison Committee
Defence Estates	Review Board for Government Contracts
Defence Geographic and Imagery Intelligence Agency	Royal Military College of Science Advisory Council
Defence Housing Executive	
Defence Intelligence and Security Centre	
Defence Medical Education Training Agency	
Defence Procurement Agency	
Defence Storage and Distribution Agency	
Defence Transport and Movements Agency	
Defence Vetting Agency	
Disposal Services Agency	
Duke of York's Royal Military School	
Medical Supply Agency	
Ministry of Defence Police	
Naval Manning Agency	
Naval Recruiting and Training Agency	
Pay and Personnel Agency	
Queen Victoria School	
RAF Personnel Management Agency	
RAF Training Group Defence Agency	
Service Children's Education	
Veterans Agency	
Warships Support Agency	
	Other Entities
	The Reserve Forces and Cadet Associations (formerly TAVRA)

32. Actual Outturn – Resources and Cash

Actual Outturn – resources:

Request for resources 1: Provision of Defence Capability.

Actual amount net resources Outturn £32,302,024,114.93.

Actual amount of savings in resources over Estimate £779,571,885.07.

Request for resources 2: Conflict Prevention.

Actual amount net resources Outturn £1,233,155,000.00.

Actual amount of savings in resources over Estimate £180,455,000.00.

Request for resources 3: War Pensions and Allowances, etc

Actual amount net resources Outturn £1,116,047,094.00.

Actual amount of savings in resources over Estimate £41,957,906.00.

Actual Outturn – cash:

Net cash requirement: Outturn net cash requirement was £29,337,645,888.93

The amount surrenderable to the Consolidated Fund was £142,563,607.45.

33. Votes A Statement – Statement of Approved Maximum Armed Forces Numbers

33.1 Votes A Statement is presented annually to Parliament to seek authority for the maximum numbers of personnel to be maintained for service with the Armed Forces for the year and is audited by the National Audit Office.

33.2 Maximum numbers of personnel to be maintained for service with the Armed Forces:

	Numbers voted by the House of Commons	Maximum numbers maintained	Peak dates
Officers, Men & Women for NAVAL SERVICE	46,025	41,553	1 April 2003
Officers, Men & Women for ARMY SERVICE	128,195	121,207	1 October 2003
Officers, Men & Women for AIR FORCE SERVICE	57,415	53,775	1 March 2004

33.3 Maximum numbers of personnel to be maintained for service with the Reserve Forces:

	Numbers voted by the House of Commons	Maximum numbers maintained	Peak dates
Reserve Naval and Marine Forces	17,600	15,466	1 Feb 2004
Special Members of the Reserve Naval Forces	300	163	1 July 2003
Reserve Land Forces	84,000	71,861	1 May 2003
Special Members of the Reserve Land Forces	6,000	58	1 March 2004
Reserve Air Forces	23,050	16,293	1 April 2003
Special Members of the Reserve Air Forces	550	66	1 Jan 2004