

By Nick Watts, Defence Correspondent, Great North News Services

The House of Commons Public Accounts Committee (PAC) has again highlighted the lack of control in the way the MOD manages its finances. Under a new Chairman, Margaret Hodge MP, the committee has returned to the cause pursued by its predecessor in the last parliament. In sum the PAC states that the MOD does not have a handle on its finances, and this is exemplified by the way it manages the defence estate.

With an annual expenditure of some £42 bn the MOD is responsible for a defence estate which is valued at some £20 bn. In an unnerving parallel with the equipment programme, the PAC reports that the department is not sure whether its estate holding is too big, too small, or just right. The PAC also notes the department has a £36 bn shortfall in funding over the next decade. This mostly consists of the forward Equipment Programme. For the time being the MOD can ascribe these problems to the shortcomings of its predecessor. It remains to be seen how this picture will change next year. Lord Levene's Defence Reform Unit will have almost finished its work by then, and the results should be filtering through to such areas as this. Gripping the financial management of the MOD is one of Liam Fox's top priorities. We shall see.

This is a synopsis of the Public Accounts Committee critical report.

The Ministry of Defence (the Department) is responsible for over £42 billion of annual expenditure. While it has managed to stay within budget each year, it has failed to exercise the robust financial management necessary to control its resources effectively in the long term. It has also failed to match its future plans to a realistic assessment of the resources available. There is a shortfall in planned expenditure against likely funding of up to £36 billion over the next ten years. The Strategic Defence and Security Review did not explicitly set out how this long-standing gap between defence spending and funding would be resolved.

The Department's consistent pattern of planned overspend demonstrates serious organisational failings and a dangerous culture of optimism. The underlying reasons for the systemic failings in budgetary controls are the tendency towards financial over-commitment, weaknesses in the financial planning processes and a division in responsibilities and accountability for financial stewardship. The failure to integrate financial planning and control into decision making means that cuts in programmes and delays in expenditure on defence equipment are made very late in the day, leading to inefficiency, poor value for money and longer term additional costs.

The Accounting Officer has not discharged his responsibility to ensure that planned and committed expenditure across the defence budget represents value for money. For example, in 2008 the Department signed a contract to buy new aircraft carriers which was unaffordable, without having identified compensating savings. Because these savings were not subsequently

found, it was necessary within a year to delay the project, resulting in an enormous cost increase and poor value for money.

We were astonished to learn that the Department has not had an explicit financial strategy linking its funding to its priorities. Without a clear strategy, it is difficult to resolve funding conflicts or to reallocate resources when priorities change. The Department does not have the tools to help it to revisit assumptions underlying its plans, ensure plans are realistic and make provision for unexpected events and managing risk.

Furthermore, the Department does not prioritise individual elements of the defence programme against its strategic priorities. When financial savings have to be found there is then no clear basis for determining where cuts should be made. So in-year decisions on budget cuts are made on an ad hoc basis, without proper consideration of relevant priorities and needs.

The Department has made some inroads into improving its financial management; however, it has yet to give financial management the serious consideration that it deserves. The Department has now appointed a professionally qualified Finance Director, and has undertaken to provide him with the full authority he needs to do the job.

On managing the defence estate

The defence estate covers 1.5% of the UK land mass, is valued at over £20 billion, and costs an estimated £2.9 billion per year to run. The Department has reduced the amount of built estate in the UK by 4.3% between 1998 and 2008, and achieved £3.4 billion in sale receipts. However, staffing over the same period was cut by 13%, so more of the estate could and should have been released.

The Department does not assess its estate against clear objective criteria, such as the cost of running a site or the intensity of usage. The bias appears to always lie with keeping a site rather than disposing of it.

The Department does not collect centrally the information and data that would allow it to manage its estate in an effective way. It appears to lack urgency in its plans to improve its information base.

The Rt Hon Margaret Hodge MP, Chair of the Committee of Public Accounts, commented:

"The MOD's poor financial management has led to a potential shortfall of spending against funding over the next decade of £36 billion.

"It is astonishing that the Department has hitherto failed to develop a proper long-term financial strategy linking its funding to its core priorities and providing a clear basis for making cuts. Instead, it has managed to stay within budget each year by making short-term and ad hoc in-year decisions to cut programmes and defer the acquisition of kit. These have led to inefficiency and even greater costs in the longer term.

"This situation must change without delay. We welcome the MOD's appointment of a professionally qualified finance director and expect the Department to give him the powers he needs to do the job.

"We also want to see improvements in the MOD's decision-making about the defence estate which covers 1.5% of the country. The Department simply cannot say whether the estate is too large, too small or the right size. Managing a £20 billion asset with virtually no understanding of its cost or efficiency is entirely unacceptable."