UK Government Investments

THE CONTINGENT LIABILITY CENTRAL CAPABILITY

Exploring the UK government's contingent liabilities

Contents

Foreword from Director of the CLCC

I joined government last year to head up the newly established **Contingent Liability Central Capability (CLCC) team**, and I am excited to take on this new and challenging role.

The UK government's contingent liabilities, which impact government finances only if future uncertain events occur, are complex and varied. They range from nuclear decommissioning to international guarantees supporting developing countries, from clinical negligence claims in the NHS to procurement indemnities for large infrastructure projects. Contingent liabilities can be an important policy tool in supporting economic growth. They may be created through government's role as insurer of last resort[1], where government takes on risk that the private sector cannot, both to protect the public and provide stability when unforeseen events occur.

It is imperative that when government takes on risk, the risk is well understood and managed. Estimating the likelihood of an event occurring, the timing and potential costs requires finance teams in departments to undertake complex analysis on the outcome of uncertain future events.

Establishing the CLCC within UK Government Investments (UKGI) in partnership with the Government Actuary's Department (GAD) brings together expertise to ensure these complex issues benefit from specialist industry knowledge and analysis. Our unique combination of credit, insurance and Civil Service policy professionals allow us to better understand the extent of the government's financial risks and how those risks are correlated across the government's portfolio. The UK government is leading the way in seeking to drive efficient management of its balance sheet, and the CLCC has a key role to fulfil in supporting these objectives.

The CLCC will provide analysis of new contingent liabilities and build a picture of the outstanding contingent liability risk across government to create consistent data sets and outputs. By using relevant expertise, we can quantify, price, and manage risk more accurately, improve risk sharing with the private sector, and bring together data to enable an enhanced understanding of the

1 Government as Insurer of Last Resort, published by HM Treasury March 2020

consolidated risks to which government is exposed. This will be a multiyear effort that will enable stress testing of targeted parts of the portfolio, of the whole dataset and wider fiscal risk modelling.

Going forward, the CLCC will collect contingent liability data on a regular basis and ensure relevant and better information is available to decision makers. On the way, the CLCC will be sharing its understanding of the existing risks with departments and using what it has learned to bring best practice recommendations and set the standard for data. The CLCC are supporting departments to efficiently structure new contingent liability applications and find economic solutions to deliver policies.

I am proud of what we have achieved in the first 12 months as a new unit within government. Publishing this inaugural progress report offers the opportunity to summarise those achievements as well as set out the vision for the coming years. The team is keen to hear views and comments from those with an interest in this project as the CLCC continues to progress its goals.

Siobhán Duffy, Director, Contingent Liability Central Capability

Executive Summary

The Contingent Liability Central Capability (CLCC) is an analytical and advisory unit providing contingent liability expertise. The unit forms part of UK Government Investments (UKGI), which is the government's centre of excellence for corporate finance and governance.

In its first year of operation, the CLCC has established itself as a new unit offering support to government departments and has started the process to bring together a consolidated understanding of the landscape of government's contingent liabilities. This report sets out the unit's progress to date and plans for future years.

What is a contingent liability?

Contingent liabilities are liabilities that are uncertain but might lead to future expenditure if specific conditions are met or specific events happen. They are disclosed to Parliament and in departments' accounts in line with Managing Public Money and accounting standards. These disclosures provide a starting point in understanding government's contingent liabilities; however, there are some limitations in the depth and richness of information provided.

When looking at contingent liabilities, different definitions apply depending on the purpose. In this report, we focus on contingent liabilities as defined in the relevant accounting standard IAS 37[2]. In broad terms, this refers to items with less than a 50% likelihood of occurring or which cannot be quantified reliably, and which are not covered by other accounting standards. Further details are set out in Annex 1.

Importance of managing contingent liabilities

Contingent liabilities represent a significant source of financial risk which is uncertain and evolving over time. Due to this, organisations such as the Organisation for Economic Co-operation and Development (OECD) and International Monetary Fund (IMF) have taken an interest in contingent liabilities.

In an IMF paper, contingent liabilities were characterised as 'hidden deficits', noting crystallisations of contingent liabilities are correlated to one another and tend to occur during periods of growth reversals and crises, accentuating pressure on budgets during already difficult times. The IMF noted that countries with stronger institutions are able to better control and address the underlying risks so that they are less exposed to contingent liability crystallisations[3].

Further, the OECD has cited the importance of managing balance sheet risks, guarantees and other contingent liability

2 IAS 37 is the international accounting standard which covers treatment of contingent liabilities
3 IMF Working Paper WP/16/14, The Fiscal Costs of Contingent Liabilities: A New Dataset

risks to increase the resilience of public finances in the wake of the COVID-19 crisis[4].

What is the CLCC's role?

Our mission is to strengthen contingent liability expertise within government and improve how government manages its portfolio of risk from contingent liabilities.

The CLCC is primarily focused on two types of contingent liabilities, indemnities and financial guarantees, which may be incurred as part of the government's role as 'insurer of last resort'[5]. When reporting on government's landscape of contingent liabilities, we will aim to include all items which fall within the accounting definition of contingent liabilities, even though our expert analysis will be focused on the narrower subset of indemnities and financial guarantees.

Indemnities
Where the government agrees to cover costs if a certain event occurs.

Financial guarantees
Where the government agrees to pay the debts of a third party if they default.

Purchaser protections
When assets are sold market-standard warranties to confirm government has undertaken proper due diligence of an asset.

Legal cases
Lawsuits which are directly brought against the government as a result of undertaking its core activities.

Our three strategic objectives are to:

- **Review and report on existing contingent liabilities,** to inform risk management and contingency planning. To date we have completed projects with the Department for Business, Energy and Industrial Strategy (BEIS) and the Department for Transport (DfT) to review their existing contingent liabilities. Through this and work with other departments, we have gained a better understanding of how contingent liabilities are managed across government and data availability.
- **Provide advice and analysis on new contingent liability proposals.** These may be referred to us via HM Treasury or other departments directly. We help teams quantify risks (including expected loss and probability of crystallisation), suggest risk mitigations and advise on charging premiums for the risks the government takes on. To date, we have advised on over 50 cases; an example is set out overleaf.
- **Promote best practice across government** to assess and report on the financial impacts of contingent liabilities consistently and accurately. To date the CLCC has produced guidance on calculation of expected losses with plans to develop further guidance in the future. We have put in place Account Managers to join up with 17 departments, established relationships with the National Audit Office (NAO) and the Office for Budget Responsibility (OBR), and founded the Contingent Liability Advisory Network (CLAN), a cross-government group of contingent liability practitioners meeting regularly to share advice, ideas and challenges.

---

4 OECD Best Practices for Managing Financial risk. To note, the CLCC has not included COVID-19 schemes such as BBLS and CBILS in its analysis as, on an accounting basis, these schemes are reported as on-balance sheet items in line with IFRS9

5 The CLCC's current remit is focused on contingent liabilities where the government takes on risk that the private sector cannot and fall within the accounting definition of contingent liabilities per IAS 37. Thus the CLCC is focused on financial guarantees and indemnities, however, this may be subject to change in the future.

Foreign, Commonwealth and Development Office (FCDO) – Clean Green Initiative

During COP26 (2021 United Nations Conference on Climate Change), the UK launched the Clean Green Initiative to help developing countries take advantage of green technology and grow their economies sustainably. The Clean Green Initiative includes a package of guarantees to support clean infrastructure projects.

The CLCC provided specialist advice and expertise in structuring and managing guarantees and supported the FCDO in delivering their package of guarantees. This included the India Green Guarantee to support clean and resilient infrastructure in sectors such as clean energy, transport and urban development and the Room to Run guarantee scheme to unlock financing capacity from the African Development Bank for projects across the Africa.

Our expertise was able to support the FCDO in achieving its goals to scale up public and private investment in sustainable infrastructure globally.

A snapshot of the government's contingent liability landscape

Contingent liabilities in numbers

As of 2021, maximum quantified contingent liability exposure amounted to **£214bn,** equating to **9% of UK GDP** at the time.

There are **326** contingent liabilities across 15 government departments. For **137** of these contingent liabilities maximum exposure has been quantified, with the remaining **189** unquantified.

Source: *CLCC analysis of department annual report and accounts 2020-21.*

During our first year, we have drawn together initial insights based on publicly available information at the time (including departmental accounts and Whole of Government Accounts[6]), combined with further data collected through the CLCC's work to advise on the flow of new contingent liabilities and projects with selected departments.

The following charts show the number and value of contingent liabilities by department from published 2020-21 accounts. Across the fifteen[7] sets of accounts, 58% of the 326 contingent liabilities included were classed as unquantifiable. Figure A.1 shows a range in disclosed values, with six departments (HM Treasury (HMT), Department of Health and Social Care (DHSC), UK Export Finance (UKEF), Department for Transport (DfT), Department of for Digital, Culture, Media and Sport (DCMS) and the Foreign, Commonwealth and Development Office

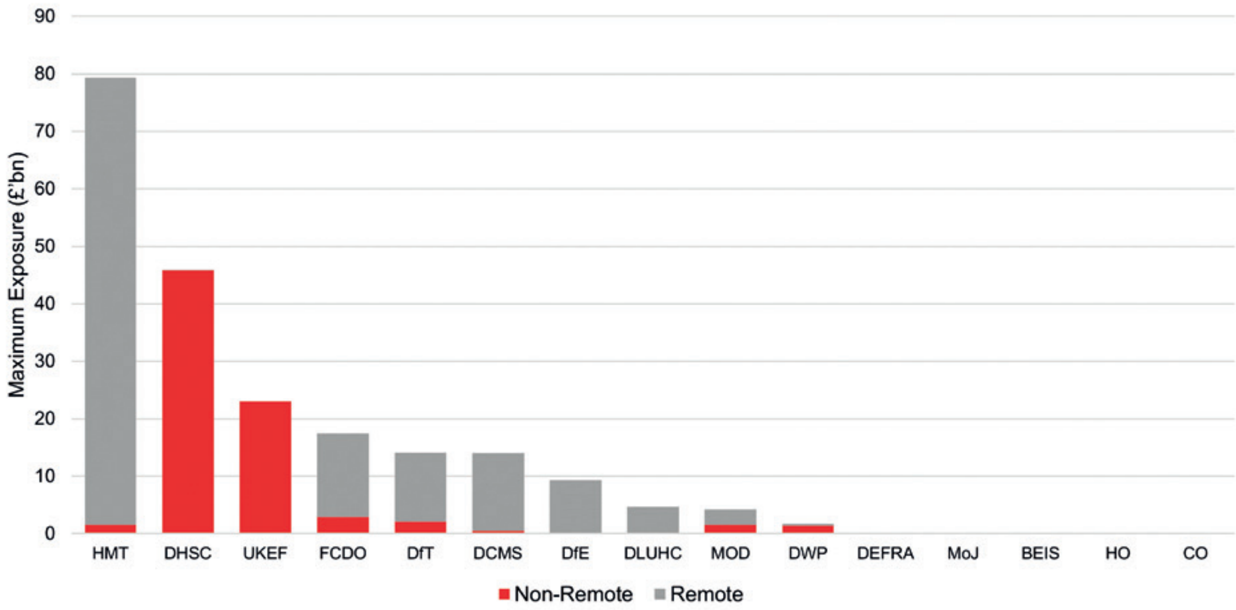
6 The Whole of Government Accounts, 2019-20 is a consolidated set of financial statements for the UK public sector.

7 We investigated 23 ministerial departments for contingent liabilities, however we removed departments beyond our remit, which currently does not include devolved administrations and local authorities, and those that did not report any contingent liabilities, leaving 15 departments.

(FCDO)) disclosing aggregate quantified contingent liabilities greater than £10bn.

Among these departments, the most significant contingent liabilities in terms of maximum exposure are: a provision in the EU withdrawal agreement relating to the European Investment Bank, purchaser protections and the Covid Corporate Financing Facility (HM Treasury); clinical negligence claims in the NHS (DHSC); international guarantees and insurance contracts (UKEF); callable capital on investments in International Financial Institutions (FCDO); procurement indemnities for large infrastructure projects such as Intercity Express and HS1 (DfT) and the BT pension scheme guarantee (DCMS). These few examples highlight the variety and breadth of contingent liabilities across government.

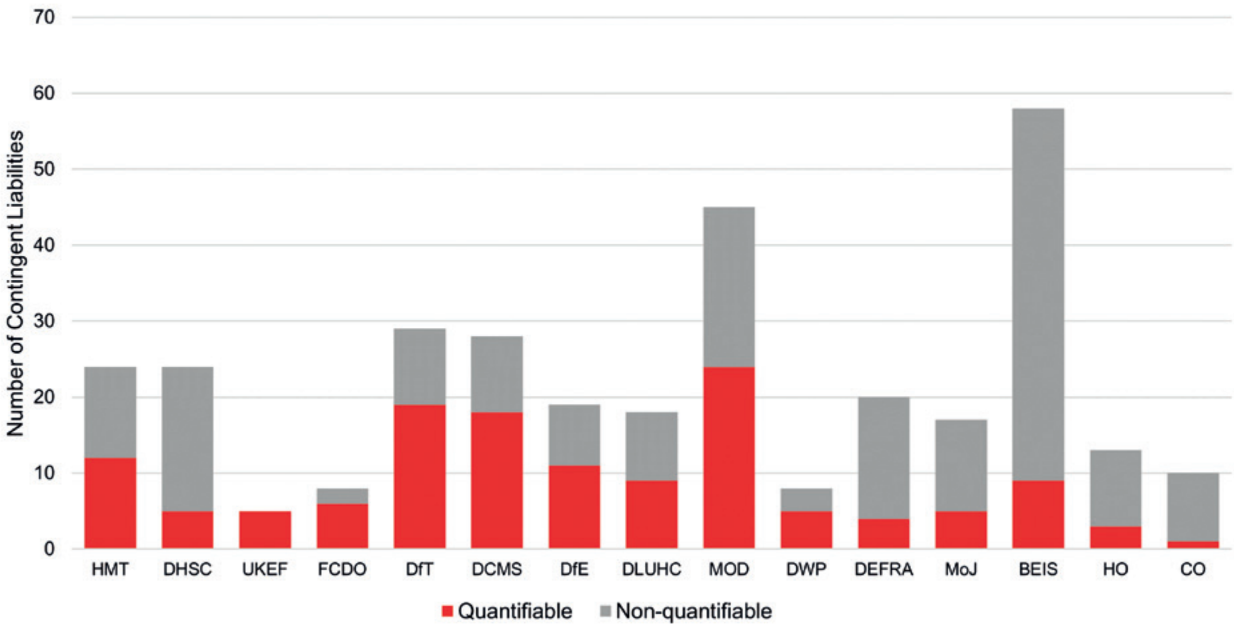
Figure A.1 – Value of quantified remote and non-remote contingent liabilities across departments per annual report and accounts (£'bn)[8]



Source: *CLCC analysis of department annual report and accounts 2020-21.*

8 Non-remote is when an outflow of resources is less than likely (<50%), and remote is when a future outflow is considered very small, however there is no strict definition.

Figure A.2 – Number of contingent liabilities across departments per annual report and accounts



Source: *CLCC analysis of department annual report and accounts 2020-21.*

However, it is worth noting that these figures, based on maximum exposure for liabilities which can be quantified, do not provide a full picture of risk:

- For an individual item, maximum exposure is helpful to understand, but when aggregated across the portfolio it can provide an inflated scale of the risk. As we develop our analysis, we plan to look at expected and possible losses in addition to maximum exposure and analyse correlations between risks in the portfolio.
- Values for aggregate contingent liability exposure exclude risks which are unquantified under the accounting standards. While the reporting complies with accounting standards, some analysis of potential losses can be carried out and communicated to support risk management.
- There is a skewed distribution of contingent liabilities, with a large number of relatively small risks plus a small number of large items. We intend to take a risk-based approach, identifying liabilities which merit deeper investigation.

What's next for the CLCC?

The CLCC is embarking on a multi-year programme to improve how government manages its contingent liabilities. In line with our three strategic objectives, we are aiming to:

- **Review and report on existing contingent liabilities,** developing a more comprehensive understanding of government's contingent liabilities, supported by regular cross-government data gathering. Due to the variable nature of the contingent liability portfolio across different government departments, we will take a risk-based approach to further data gathering and analysis. While we intend to build a basic understanding of all contingent liabilities, our more detailed analysis will be focussed on those which are higher risk, poorly understood or where risk mitigation may be improved.

- **Provide advice and analysis on new contingent liability proposals,** continuing to offer advice to departments entering into new contingent liabilities. Over time, our data on existing contingent liabilities will provide a source for estimating exposure of new contingent liabilities, so that future decisions will be informed by improved data which only a project of this scope can provide.
- **Promote best practice across government,** continuing to develop and embed the CLCC as a centre of excellence on contingent liabilities for government. We are developing guidance and tools to help ensure standard approaches are taken across government. This will enable HM Treasury and departments to better balance policy development, value for money and an understanding of the financial risks government takes on.

Contact the CLCC

We would like to take this opportunity to thank everyone who has collaborated with us in our first year of operation. The success of the CLCC rests on our engagement with the many colleagues in government departments dealing with contingent liabilities, and we are grateful for your support to date.

We are keen to hear any feedback, comments, and suggestions from those with an interest in this work. Please contact us at: CLCC@ukgi.org.uk

Data disclaimer

The financial information contained, and the analysis provided within this report is based upon data gathered from department annual reports and accounts 2020-21 and data relating to contingent liabilities approved by the government through the Contingent Liability Approval Framework. The CLCC has also applied its own categorisation of contingent liabilities to supplement this analysis, the details of which can be found in Annex 3 of this report. The data used by the CLCC in preparing the analysis included within this report is owned by the relevant departments. Data which utilises the Whole of Government Accounts are taken from 2018-19 and 2019-20 accounts. The analysis included within this report should be treated as unaudited administrative data and should not be considered as national or official statistics.

Chapter 1: The Importance of Contingent Liability Management to Government

The government's role as insurer of last resort involves taking on risk that the private sector is unable or unwilling to bear and covering the costs when that risk materialises, where there is a strong public policy case for intervention.

1.1 The importance of contingent liability management to government

By taking on these risks from the private sector the government can help:

Address market failure and improve efficiency, for example, by offering financial guarantees for loans to small and medium sized enterprises (SMEs). Often these companies struggle to access finance from commercial banks due to a higher risk profile, potentially hampering growth and market competitiveness.

Provide cover for situations where commercial insurance is either unavailable or if available is prohibitively expensive, for example, events which are low probability but if they occur have high financial impact, such as terror attacks.

Enhance consumer protection through innovative policy measures, for example, Flood Re ensures comprehensive access to flood risk insurance through a government and insurance industry initiative. In this example, its financial arrangements avoid the government incurring a contingent liability.

Managing this risk well is important for the long-term sustainability of the public finances. Through our analysis of departments' most recent annual report and accounts, the CLCC has identified an aggregate quantified maximum exposure of £79bn of contingent liabilities and a further £135bn of remote contingent liabilities[9]. Additionally, there are many contingent liabilities across government which are unquantified and therefore not included in these figures.

Contingent liabilities thus represent a significant financial risk to the government. It is imperative that when the government takes on risk, the risk is well understood and managed. The CLCC is here to help achieve that goal.

9 These figures are based on analysis of the 2021 annual report and accounts for: the Ministry of Defence, Department for Business, Energy & Industrial Strategy, Department for Transport, UK Export Finance, Department for Levelling Up, Housing & Communities, Department for Education, Department of Health and Social Care, HM Treasury, Department for Digital, Culture, Media & Sport, Foreign, Commonwealth & Development Office, Department for Environment, Food and Rural Affairs, Department for Work & Pensions, Ministry of Justice, Home Office and Cabinet Office.

The value of contingent liabilities

- Contingent liabilities can be the most appropriate and cost-effective solution, or the only solution, to a policy problem. Government is in a unique position to take on risk which the private sector and general public cannot.
- Financial guarantees where we have a reasonable expectation that loans will be repaid will be better value for money than using grants.
- Contingent liabilities do not impact departmental budgets at the point of creation, therefore when used appropriately, they can free up spending for public services.
- Contingent liabilities allow government to share risk with the private sector in ways that would not be possible if government were directly providing grants or loans. For example, by government charging for its particular share of the risk in a reinsurance policy where the private sector is offering coverage, or in providing financial guarantees.

Why contingent liabilities need to be managed

- As contingent liabilities are 'free' at point of creation, they can be subject to inadequate scrutiny. They can be high risk and the true cost may be opaque.
- Sometimes contingent liabilities are used to delay spending to some point in the future for the sole purpose of reducing spending today. This transfers the cost to future generations, which is not sustainable.
- Contingent liabilities can create a moral hazard, for example lenders may be more prepared to issue risky loans since they know the government is bearing the risk of default.

Chapter 2: The Inception, Role and Achievements of the CLCC

During the CLCC's first full year of operation, we have: built relationships across departments, undertaken analysis, provided advice, shared best practice, and initiated planning for a cross-government database of contingent liabilities.

2.1 CLCC within UKGI

UKGI is the government's centre of excellence in corporate governance and corporate finance. We work across government on some of its most complex commercial tasks, advising and interacting with ministers, Parliament and government departments. UKGI is a government company with HM Treasury as its sole shareholder. UKGI is accountable via its independent Board to Treasury ministers and – through the Chancellor – to Parliament.

UKGI was chosen to host the CLCC given its unique mix of private sector professionals and civil servants, a mix which is reflected in the make-up of the CLCC, and its experience providing expert advice to government departments.

Corporate Governance	Corporate Finance	Contingent Liabilities	Asset Realisation
Act as a shareholder for, and lead establishment of, UK government arm's length bodies	Advise on all major UK government corporate finance matters, including interventions into corporate structures and corporate finance negotiations	Analyse and advise on the UK government's contingent liabilities	Acquire, manage and execute the sale of all significant UK government corporate assets

2.2 CLCC team

The CLCC team was established in UKGI in partnership with the Government Actuary's Department (GAD). The CLCC brings together a unique combination of skills and expertise including actuaries seconded from GAD, credit risk experts, and Civil Service policy and analytical professionals.

Senior leadership

	**Siobhán Duffy** Head of the CLCC	Siobhan joined UKGI in July 2021 to lead the CLCC. Prior to joining UKGI, Siobhán spent over 25 years working in debt capital markets structuring and advising European corporates on debt issuance.
	**Emma Knott** Head of Portfolio Analysis & Engagement	Emma leads the Portfolio Analysis and Engagement team in the CLCC, and joined UKGI in April 2021. Emma is a Senior Civil Servant on secondment from HM Treasury, with a background in public spending.
	**Alexander Richarz** Head of Credit	Alexander joined UKGI in June 2021 to lead the Credit team in the CLCC. Prior to that, he spent over 25 years working in commercial and investment banking at Deutsche Bank, CIBC, and Credit Suisse.
	**Aidan Smith** Head of Insurance	Aidan joined UKGI in February 2021 and leads the Insurance team. Aidan has over 20 years' experience providing actuarial advice to the public sector and is on secondment from the Government Actuary's Department.

2.3 Inception and purpose of the CLCC

HM Treasury launched the Balance Sheet Review at the Autumn Budget in 2017 to identify opportunities to dispose of assets that no longer serve a policy purpose, improve returns on retained assets and reduce the cost and risk of liabilities.

Following this, HM Treasury published the 'Government as Insurer of Last Resort' report at the March 2020 Budget which recommended the development of a central capability to advise on the management of contingent liabilities across government. The report set out proposals for improving the management of government's contingent liabilities in line with four key aims:

1. Improve expertise in government to quantify and price risk
2. Improve compensation for risk taken on by the taxpayer
3. Establish the appropriate incentives to reduce both the probability of risk materialising and the cost when it does
4. Bring clarity to risk ownership to provide more certainty on how losses can be shared between the exchequer, departments and private sector

The CLCC assists departments and arms-length bodies with assessing, quantifying, and pricing risk from contingent liabilities, allowing departments and government to better understand the scale and distribution of their risk exposure from contingent liabilities.

Our mission is to strengthen contingent liability expertise within government and improve how government manages its portfolio of risk from contingent liabilities.

2.4 The CLCC's year 1 achievements

Objectives	What we sought to achieve	What we have achieved
Review and report on existing contingent liabilities	Develop and initiate pilot projects with government departments as a stepping-stone to cross-government portfolio analysis. Identify data currently captured on contingent liabilities and commence the development of a cross-government contingent liability database. Produce a progress report summarising analysis and insights on the government's portfolio of contingent liabilities.	• Pilot projects to review the stock of existing contingent liabilities with BEIS and DfT, with plans to expand the programme. • Analysed existing publicly available government data on contingent liabilities. • Assessed what data is currently available on contingent liabilities within government. This has allowed us to understand where gaps exist. • Formed plans to develop a contingent liability database. • Published 2022 progress report, with plans to produce further analysis of contingent liabilities in future years.
Provide advice and analysis on new contingent liability proposals	Support and advise on new contingent liabilities associated with the Contingent Liability Approval Framework, via referrals from HM Treasury and directly from departments.	• Advised on over 50 contingent liability cases referred to us by HM Treasury and government departments. • Our analysis and advice has covered: quantification, expected loss, ability to charge premiums, risk management and implementation practicalities.
Promote best practice across government	Promote services of the CLCC and produce best practice guidance.	• Account managers for 17 departments in place to directly build relationships. • Established a presence on the OneFinance (Government Finance Function) site, visible to more than 10,000 finance professionals across government and established a quarterly cross-government forum to discuss key contingent liability developments. • Produced expected loss guidance for departments and developed a prioritised plan for future materials to share across government.

Chapter 3: Current Landscape of Contingent Liabilities Across Government

To understand the scale of data and analysis required to build a comprehensive picture of government's risk exposure through contingent liabilities, the CLCC has assessed existing sources of contingent liability information, started to analyse publicly available data and worked with two departments to review their existing stock of contingent liabilities.

3.1 Sources of contingent liability data

The CLCC has identified a range of publicly available and internal-to-government data sources that include information on contingent liabilities. This includes the Whole of Government Accounts (WGA), department annual report and accounts as well as internal registers. Through a review of these sources, we have found that, while they are fit for their intended purpose, they do not provide sufficient information to carry out detailed analysis on the stock of government's contingent liabilities. Often these sources will report on groups of contingent liabilities as a whole or provide quantification linked to maximum exposure only. Information provided on charging, sensitive or immaterial liabilities as well as the probability of and expected loss from a risk materialising is often limited. For more information on contingent liability data sources, see Annex 2.

In light of this, we will need to work with departments to directly gather key metrics on contingent liabilities. We plan to support departments in bolstering their internal contingent liability registers, where possible incorporating expected loss estimates, clarifying boundary issues and producing range estimates of exposure for unquantifiable contingent liabilities. This should help departments to better understand contingent liability risk as part of their risk management processes.

Figure 3.A – Limitations to contingent liability reporting

	Boundary issues	Understanding risk	Unquantified contingent liabilities
Limitations	There are instances where an accounting contingent liability may be a stress-scenario or disclosure item in relation to a policy which is identified elsewhere on the balance sheet.	The value of contingent liabilities reported within departmental accounts and the WGA are generally maximum exposure figures. As a result, these figures are not comparable to balance sheet items which are closer to expected values. As maximum exposure is being aggregated across uncorrelated items there is a greater probability that an inflated value for overall risk across the portfolio is being provided.	Departmental accounts and the WGA reference unquantified contingent liabilities, however, due to their nature there is no figure associated with these and so only a partial picture of the risk is provided.
Example	The Whole of Government Accounts 2019-20 includes £50bn within non-remote contingent liabilities for clinical negligence claims, which are also accounted for in provisions. This is included as a disclosure item in order to account for the total exposure to government if all claims were successful – it is therefore a helpful additional disclosure item but could be misinterpreted as an additional risk item in its own right.	Within Whole of Government Accounts 2019-20, £17bn is included for export guarantees and insurance policies under non remote contingent liabilities. This represents the net value after insurance. Compared to this, expected losses on export guarantees and insurance policies are estimated at £1bn.	Unquantified contingent liabilities included within WGA include pension scheme deficits, civil nuclear liabilities and student loan sale warranties among other items. For unquantified contingent liabilities like these, it may be possible to quantify approximate risks.

***Source:** CLCC review of publicly available data sources including information on contingent liabilities (e.g. department annual report and accounts 2020-21, written ministerial statements and Whole of Government Accounts 2019-20).*

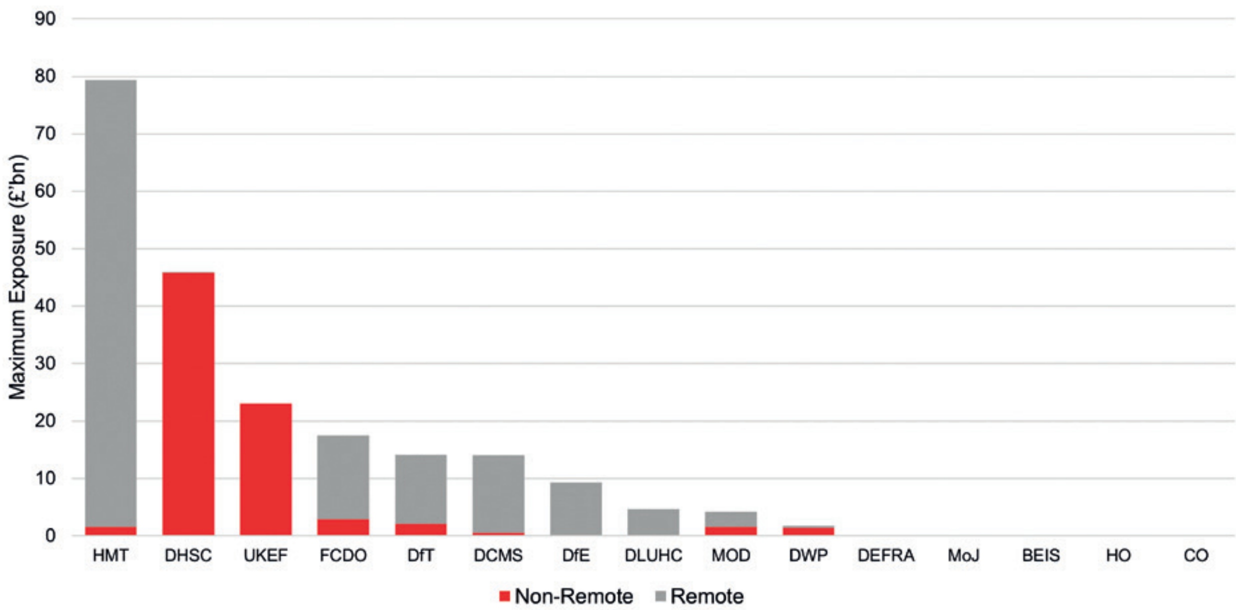
3.2 Contingent liability analysis using data currently available

The CLCC has started to analyse publicly available data to draw initial insights on government's portfolio of contingent liabilities. Whilst there are some limitations, our analysis will inform how future work is targeted to build a clearer picture of the highest risk or least well understood items.

Through a review of the latest annual report and accounts of government's 23 ministerial departments, we identified 15 that were within the CLCC's remit and held contingent liabilities[10]. These 15 departments hold 326 contingent liabilities, of which 137 are quantified and 189 remain unquantified[11].

In total, the maximum exposure of quantified contingent liabilities (both remote and non-remote) across departments equates to £214bn (9% of UK GDP at market prices as of 2021)[12]. Of this, £79bn represent non-remote contingent liabilities and £135bn remote contingent liabilities. Aggregate expected losses on these items are expected to be much lower than maximum exposure.

Figure 3.B – Value of quantified remote and non-remote contingent liabilities across departments per annual report and accounts (£'bn)



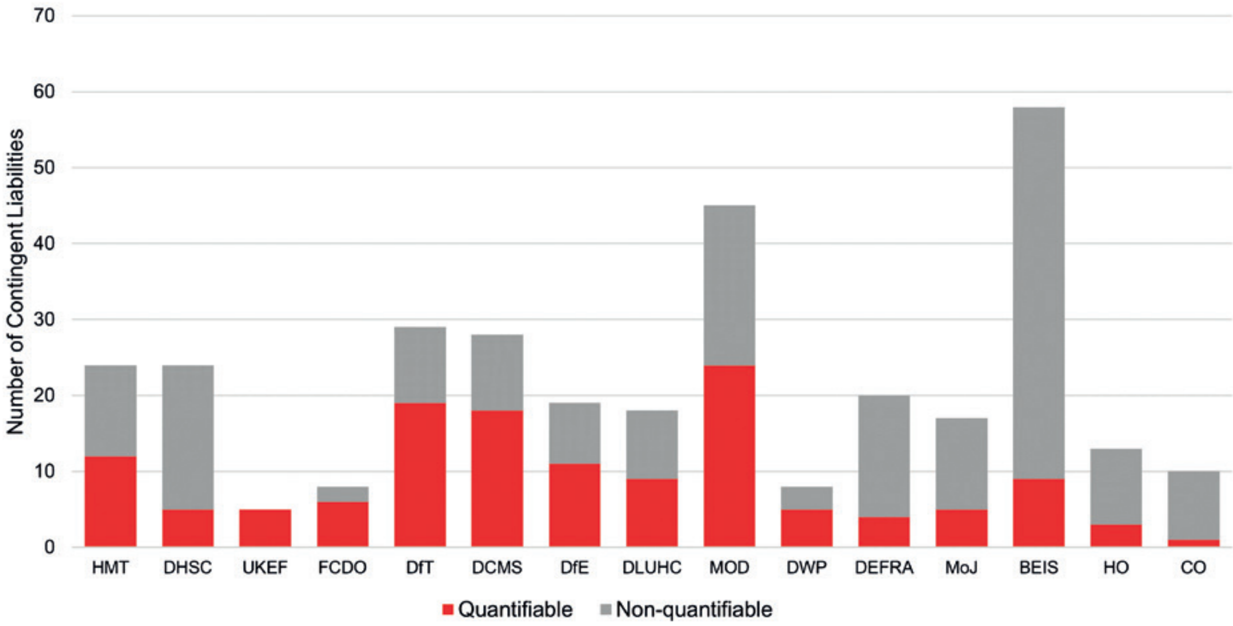
Source: *CLCC analysis of department annual report and accounts 2020-21.*

10 Devolved administrations are currently beyond the scope of the CLCC's remit and ministerial departments such as the Office of the Leader of the House of Commons do not hold contingent liabilities as per their annual report and accounts.

11 Information is sourced from the latest available published reports and accounts of 15 departments as at March 2022, for which links can be found here: https://www.gov.uk/government/publications/annual-reports-and-accounts-for-central-government-departments. As part of consolidating department annual report and accounts the CLCC also made adjustments to the information gathered. This included adjusting exposure to the net position where contingent liabilities have an associated receipt.

12 These figures do not include the Pension Protection Fund (PPF) which is included as a separate line item added directly to Whole of Government Accounts and not attributed to an individual department.

Figure 3.C – Number of contingent liabilities across departments per annual report and accounts



Source: *CLCC analysis of department annual report and accounts 2020-21.*

3.3 Concentrations and categories of risk

To understand the make-up of contingent liabilities across government's portfolio, the CLCC developed an assessment of concentration risk. We grouped contingent liabilities by economic sector (e.g. energy, housing, infrastructure, international finance), by type of contingent liability (e.g. guarantee, indemnity, purchaser protection) and by triggers that would result in the contingent liability crystallising (e.g. a default, third party decision, legal claim). By applying this approach, we found some high exposure areas such as:

- **Infrastructure:** 3 quantified contingent liabilities result in a combined maximum exposure of just over £10bn for DfT. While they would be triggered by separate third party decisions (e.g. legal changes or changes to regulations made by organisations other than the department) impacting rail contracts, there is also potential for them to all be triggered by adverse conditions in the construction sector (e.g. supplier insolvency).
- **International finance:** 10 contingent liabilities totalling a maximum exposure of over £50bn across HM Treasury, FCDO and DWP. These contingent liabilities take the form of guarantees linked to supranational organisations, guarantees linked to intergovernmental organisation contributions and potential changes to pension scheme value estimates resulting from the audit of an intergovernmental social fund. While circumstances in these cases differ, they may be all susceptible to adverse conditions in the international finance sector.

The highest number of contingent liabilities, both quantifiable and unquantifiable, sit across defence (43 contingent liabilities with a total maximum exposure of £4bn), and infrastructure (26 contingent liabilities with a total maximum exposure of £15bn). However, these monetary values only include quantified contingent liabilities.

The liabilities can also be examined based on type of contingent liability: guarantees, indemnities, purchaser protections, legal cases and other types (which includes contingent liabilities which arise from an uncertain future cost to government, and are not considered to be one of the other four types). A more granular breakdown of the types and categorisations within them is provided in Annex 3.

Figure 3.D – Maximum exposure against contingent liabilities by type across departments per annual report and accounts

Source: *CLCC analysis of department annual report and accounts 2020-21, utilising CLCC contingent liability categories (Annex 3).*

The categories with the largest maximum exposure are guarantees and legal cases, both of which have large exposures relating to a relatively small number of quantified liabilities.

This summary is indicative, based on limited information and an initial set of categories. The CLCC will continue to develop our categorisation of contingent liabilities to develop a standard taxonomy which can apply across government and help with the standardisation of policy and practice.

3.4 Charging for risk within the existing portfolio of contingent liabilities

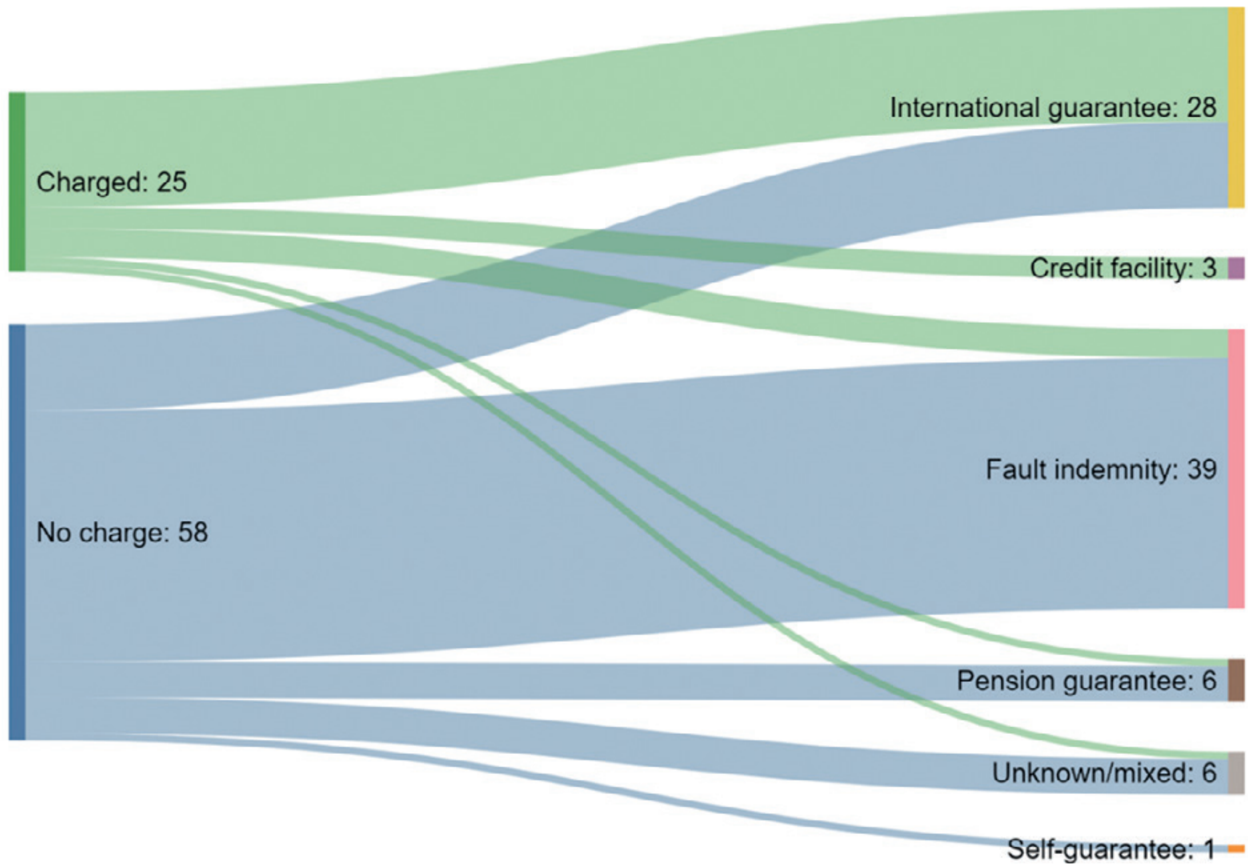
HM Treasury's contingent liability approval framework (CLAF)[13] requires departments to consider whether the Exchequer should be compensated for holding risk that is transferred from the private sector to the government. In line with Managing Public Money principles (March 2022), the starting point for the department originating a guarantee or indemnity which transfers risk from the private sector to the public sector should always be to calculate a risk-based charge.

However, most contingent liabilities are not charged for explicitly; based on HM Treasury records, 17% of contingent liability cases that have passed through the CLAF since 2017 have charged the private sector for risk. Sometimes this is because current approved and standard practice is not to charge explicitly, such as for purchaser indemnities and receivers' indemnities, because the risk should be reflected implicitly in the overall contract price. In other cases, policy objectives mean charging is not desirable. For example, guarantees provided to the housing sector to support low-income households are deliberate subsidies.

Excluding these categories of contingent liabilities where charging would not usually be expected, we have analysed 83 cases where charging might have been feasible. Figure 3.E illustrates the breakdown of charging by category.

13 Contingent Liability Approval Framework (CLAF) is guidance from HM Treasury to systematise the management of contingent liabilities through a standardised checklist.

Figure 3.E – Breakdown of charged and uncharged contingent liabilities, by category



Source: *CLCC analysis of contingent liabilities submitted through HM Treasury Contingent Liability Approval Framework since 2017.*

Many cases where there was no charge relate to indemnities provided for remote risks where expected losses are low. Nevertheless, there is potential to refine approaches to charging. This includes:

- Developing standard approaches for certain types of contingent liability
- Internal pricing of risks that aren't charged to the private sector might help in risk management
- In some cases, pricing could be increased to allow for the fact that the government is stepping in to replace commercial lenders or insurers and can justify a higher than break-even return
- Charging could be dynamic to change when risk changes
- Some older contingent liabilities that have not been charged for to date could be charged for in future (e.g. at renewal)

3.5 Departmental review of stock of contingent liabilities

The CLCC has been working with individual departments on a pilot basis to review their existing stock of contingent liabilities. We would like to thank the Department for Business, Energy & Industrial Strategy (BEIS) and the Department for Transport (DfT) for collaborating closely with us on our first two pilot stock review exercises. These two departments have relatively mature contingent liability monitoring and reporting processes and between them hold over 25% of government's contingent liabilities by count. These departments also have varied portfolios, with exposure to multiple sectors of the economy, and a mix of contingent liabilities linked to purchaser protections, indemnities, guarantees and legal claims.

The pilot exercises included a more detailed data collection by the department's central finance team (BEIS) and deep dives into selected contingent liabilities (DfT). For the data collection, CLCC provided updated templates which included additional metrics to better understand exposure, charging and crystallisation. A key learning from these pilots has been that CLCC can have the strongest impact when targeting high-priority contingent liabilities, for example where exposure is significant, unquantified, or relates to a historic liability that has not received recent attention.

Engagement with these departments is ongoing, and the CLCC will also work with other departments across government with large contingent liability portfolios, to review their existing stock of liabilities.

Key findings from pilot exercises

Department for Business, Energy & Industrial Strategy

Through this project the CLCC:

- Analysed the department's portfolio of contingent liabilities; including a mixture of 58 quantified and unquantifiable liabilities, with a total quantified maximum exposure of £80m (per 2020-21 accounts) that are designed to support a wide array of economic sectors including energy, science and technology and the environmental sector.
- Validated the department's contingent liability register and confirmed that no gaps in the data could be identified when cross-referenced with other materials produced by the department.
- Determined that the majority of the department's risk arising from contingent liabilities is concentrated in the energy sector and arises through indemnities provided by the department.
- Developed a methodology through which the CLCC can work with departments to 'prioritise' contingent liabilities.
- Determined where different directorates within the department could share experience and best practice linked to the management of specific types of contingent liabilities (e.g. director indemnities) and how this approach could be adopted across government.

Department for Transport

Through this project the CLCC:

- Examined the department's portfolio of contingent liabilities; including a mixture of 29 quantified and unquantifiable liabilities, with a total maximum exposure of £14bn (per 2020-21 accounts) concentrated in the infrastructure sector.
- Identified four contingent liabilities spanning the breadth of the department's core activities to review in detail.
- Explored underlying analysis and information linked to these contingent liabilities, and applied specialist credit, insurance and commercial expertise to provide estimates of exposure for contingent liabilities that were previously unquantifiable.
- Determined that in most instances estimates did not meet the criteria to be included within the department's annual report and accounts but could be utilised to improve internal risk management.
- Supported the department by providing advice on how to control and manage the risks arising from these contingent liabilities moving forward as well as where there may be an opportunity to charge for risk should similar contingent liabilities arise in the future.

Chapter 4: Future Work to Review the Existing Stock of Government Contingent Liabilities

To develop a comprehensive picture of the stock of contingent liabilities across government we have been developing a plan setting out how the CLCC will engage with departments to identify, collect, analyse, and store this data.

4.1 Goals when reviewing the government's portfolio of contingent liabilities

In developing a programme plan and key deliverables, we have considered lessons learned from similar cross-government data collection exercises such as those feeding into the *'National Infrastructure and Construction Pipeline'* produced by the Infrastructure and Projects Authority and the Office of Government Property's *'State of the Estate Report'*. We have also leveraged insights gathered from work undertaken with other government departments through pilot projects. Our plan has the following goals:

Goal One – embed a robust cross-government data collection process
We aim to develop a regular reporting cycle in which core data on the stock of contingent liabilities across government, and more detailed data on a sub-set of key contingent liabilities, can be obtained.

Goal Two – integrate cross-government data into a central database
Our goal is to develop a central repository to store data on government's contingent liabilities. This will ideally include the ability to benchmark policies in the early stages of development that may give rise to new contingent liabilities against the experience generated from the existing stock of contingent liabilities.

Goal Three – analyse and stress-test the contingent liability portfolio
Our long-term goal, following the collation of cross-government contingent liability data, is to produce a suite of models that can be used to analyse risks across government's contingent liability portfolio and appropriately stress-test the strength of the portfolio to potential shocks. This will begin with a focus on sub-sets of contingent liabilities that contribute significantly to government's overall risk exposure.

As the CLCC continues to engage with other government departments, we will use the insights gathered to regularly review our plans and assess whether the approach needs to be adapted.

Our phased approach to achieving these goals as currently planned is set out below.

Figure 4.A – Phased delivery against goals

Objective	Phase 1	Phase 2	Phase 3
1. Embed a robust cross-government data collection process	Achieve departmental buy-in through pilot projects and continuous departmental engagement Develop appropriate data templates and guidance from lessons learnt	Secure a mandate for a regular reporting cycle and carry out first cross-government data collection commission Produce initial analysis of the overall stock of government's contingent liability and key contingent liabilities	Regular reporting cycle achieved, leading to publication of contingent liability analysis, risk, and exposure reports
2. Integrate cross-governmental data into a central database	Scope out specification and requirements for a database Determine the preferred delivery option of a database	Database alpha and beta prototypes completed Accrued contingent liability data transferred into database Testing and quality assurance	Database operational – including benchmarking capabilities
3. Analyse and stress test the government's portfolio of contingent liabilities	Understand what analysis and modelling is required across portfolio and sub-sets of contingent liabilities Begin producing and testing descriptive and diagnostic analysis with key stakeholders	Identify scope of predictive and prescriptive models, including stress tests using key contingent liabilities Determine what data sources have application programme interface (API) capability and how to potentially automate analysis.	Development of stress-testing models Explore development of new models to better understand unquantifiable contingent liabilities

4.2 Goal One: Data collection

As set out in Figure 4.A, our first objective is to embed a robust cross-government data collection exercise. This is needed to provide a comprehensive picture of risk across government. Core metrics will help to better understand government's overall exposure and concentration risk, while more detailed information on key contingent liabilities will help inform future decision-making on particularly complex policies giving rise to new contingent liabilities in the future.

In order to achieve this, we will seek to:

- Gather standardised data on contingent liabilities across all government departments
- Embed this as an annual collection exercise, in a way that allows for tracking of liabilities over time
- Streamline data reporting, to reduce the burden on departments to collect and report this data

In addition, we will begin to set out the criteria through which we will determine whether a contingent liability warrants more detailed examination. Potential criteria include contingent liabilities which are:

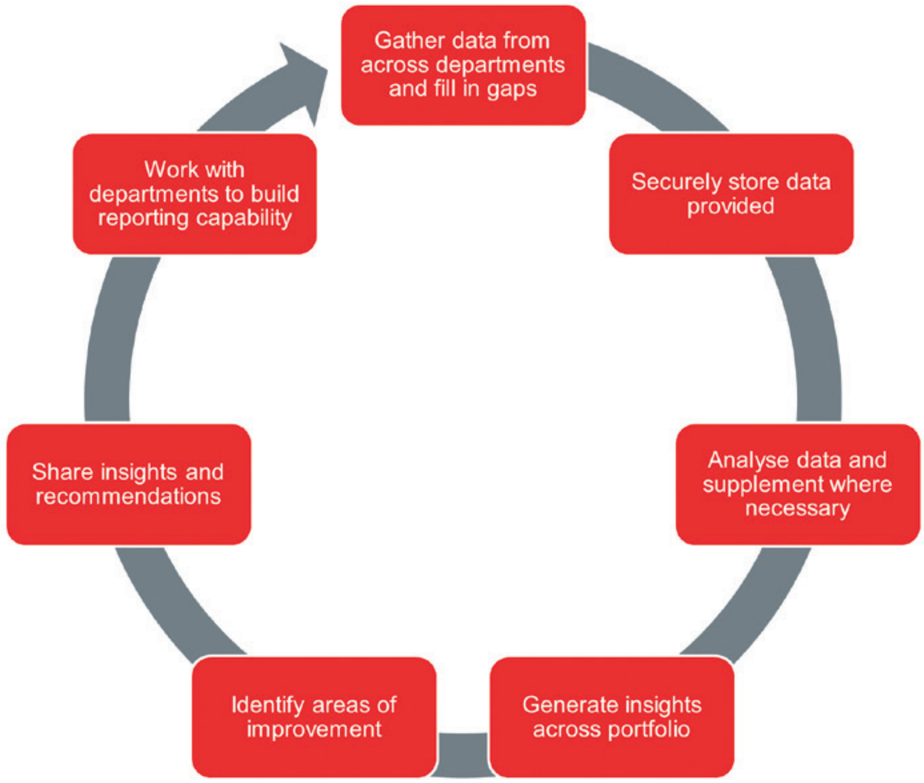
- Particularly novel and complex, contentious or repercussive
- Likely to crystallise and/or result in high expected losses, which may exceed what can be managed within a department's budget, and/or
- Essential to deliver on a priority government policy

We will continue to work with departments in order to finalise these criteria.

Department-by-department review of existing stock

To help embed this data collection exercise into the framework of government activities, we will continue to work with individual departments to review their existing contingent liabilities and better understand their reporting and monitoring capabilities. This work will allow departments to become familiar with and influence the approach we take, while improving CLCC's understanding of these departments' contingent liabilities.

Figure 4.B – Reviewing stock operating model



Through experience to date, we have found there are benefits to maintaining continuous engagement with departments. This is needed to ensure that we support departments to improve their ability to gather data on contingent liabilities. We will operate a continuous cycle through which we generate insights and recommendations for departments, provide support to build reporting capability and then use this to produce further insights.

4.3 Goal Two: Central database

Once the CLCC has established partnerships with departments to access data on a continuing basis, a central database will be required to store, access and analyse the data. Such a database is necessary for the CLCC to deliver analysis that will benefit government. In scoping this work, the CLCC is reviewing existing and bespoke solutions and will reflect departmental and other stakeholder feedback on appropriate data requirements. Benefits of holding this data centrally include:

- **Developing a complete picture** – we will begin to develop a complete view of government's exposure to contingent liability risk, allowing for comparisons between departments and driving consistency.
- **Monitoring and tracking** – by holding and tracking data on individual contingent liabilities we can monitor each contingent liability from inception to run-off, evolution to a provision or crystallisation.

4.4 Goal Three: Stress testing and portfolio analysis

Through analysis of publicly available data sources and engagement with key stakeholders on pilot projects, we have identified possible analyses that the CLCC will seek to undertake in the short and long term in relation to the government's contingent liability portfolio.

Figure 4.C – Scope of future analysis

Analysing data linked to government contingent liabilities			
Descriptive – what is the current state?	**Diagnostic – why is it happening?**	**Predictive – what is likely to happen?**	**Prescriptive – what do we need to do?**
• Frequency • Central tendency • Dispersion • Position • Interrelationships	• Root cause analysis • Isolate confounding variables	• Forecast models • Classification models • Outlier models • Time series clustering	• Recommend actions and strategies to mitigate risk • Benchmarking
Analysing how government reports on contingent liabilities			
Decision tree		**Process flows**	
• Definition of contingent liability • How departments determine premium		• Where relevant, reporting from Arm's Length Bodies to department group • Department group reporting to central finance • Department reporting to HM Treasury • HM Treasury feeding into OBR	

In future years, our analysis will seek to understand and breakdown **the government's exposure to contingent liabilities,** for example, by:

- predicting risk using forecast models that determine the scale and likelihood of large losses, and models that identify the risk of losses from a small number of individually material contingent liabilities; and
- diagnosing root cause and confounding variables by reviewing crystallisation risks due to sector, geography or industry as well as changes in the macro-economic environment.

Chapter 5: Valuing and Advising on New Contingent Liabilities

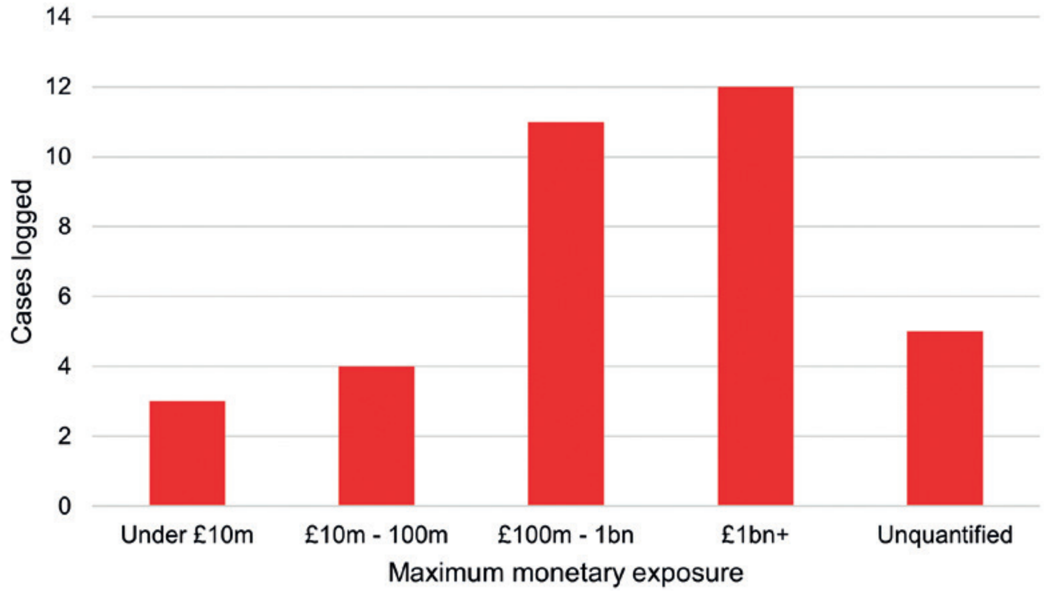
The CLCC provides advice and analysis on new contingent liabilities across government. New contingent liabilities are either referred to us by HM Treasury or directly from finance and policy teams within government departments. We encourage departments to approach us as early as possible during policy development to improve outcomes later in the process.

5.1 Referrals to the CLCC's expert insurance and credit teams

Officials responsible for initiating a contingent liability that has a maximum exposure of £3million or more and is novel, contentious or repercussive are required to complete a checklist in line with HM Treasury's Contingent Liability Approval Framework (CLAF). HM Treasury requires assurance on costs and risks associated with contingent liabilities. The CLCC is able to perform further analysis if required and advise departments and HM Treasury accordingly.

Over the course of financial year 2021-22, the CLCC has advised on a total of 56 cases, 35 of which correspond to specific contingent liability proposals while 21 were either early-stage policy development or cross-cutting policy issues. Of the 35 contingent liability proposals we advised on, over 65% had a maximum exposure greater than £100m.

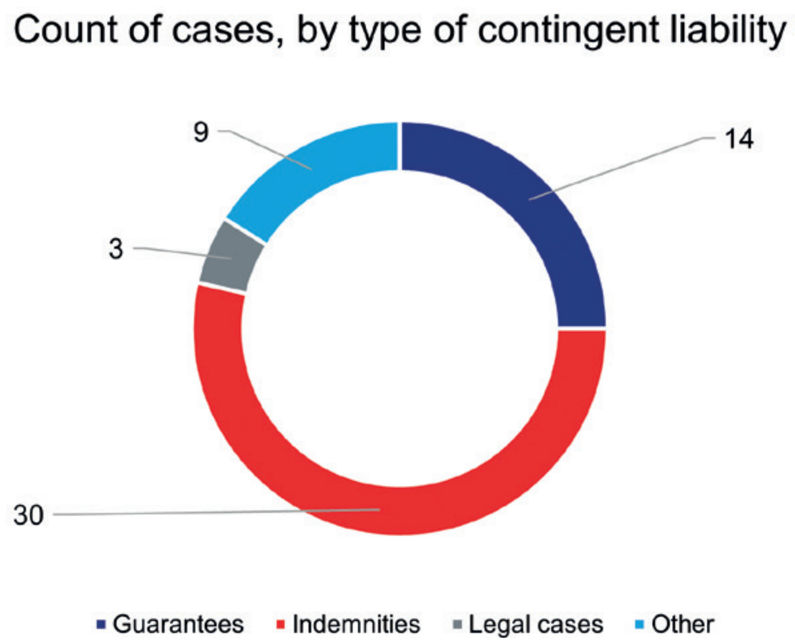
Figure 5.A – Maximum exposure of contingent liabilities proposals received during FY 2021-22



Source: *CLCC estimation of maximum monetary exposure of cases received in FY 2021-22*

Over 78% of cases received were in respect of indemnities or guarantees. Departments are encouraged to approach the CLCC as early as possible during policy development to improve outcomes later in the process when timescales are tight. The majority of our cases have begun with early engagements directly from departments, to advise on and help shape policy prior to the contingent liability going to HM Treasury for approval.

Figure 5.B – Workflow of contingent liabilities which the CLCC advised on in FY 2021-22



5.2 What analysis does the CLCC conduct on new contingent liabilities?

Credit risks

Drawing on the CLCC team members' expertise in assessing credit risk and using various third-party data sources (such as credit rating agencies, commercial banks, government data on historic contingent liabilities), we have supported departments with a risk-based approach to estimating expected losses (either on a 12-month or lifetime basis), both for new and existing guarantees. This analysis typically takes the form of providing estimates of the expected probability of default which can help inform departments around expected losses and pricing considerations.

We also provide guidance on whether a potential liability is a contingent liability or not and challenge departments as to whether they have compared the costs and benefits of providing a loan or guarantee with alternatives. These could include direct grants, regulations, or other mechanisms whereby risks are mitigated through risk sharing or collateral being provided.

Insurance and indemnities

Where data is available, we assist departments with estimates of likely frequency and severity of losses so they can complete the checklist components on maximum and expected losses. For some remote contingent liabilities, there is no history of losses, so estimates are necessarily imprecise. However, some indication of risk magnitude is still necessary and expected losses are often low in these instances.

We also advise on policy implementation issues such as charging, excesses, claims handling, insurance premium tax and incentivising private sector participation in risk sharing. In doing so, our aims are to reduce moral hazard and achieve an appropriate balance of risk between the public and private sectors.

5.3 Case Studies

Here are two examples of how the CLCC has given advice on new and existing contingent liabilities which the government hold.

UK Space Agency, Insurance and liabilities for the space industry

The government committed to review key concerns and proposals raised by respondents to UK Space Agency's consultation on insurance and liability requirements for the space industry.

The CLCC is working with UK Space Agency to develop these policies, providing views on structuring liabilities, insurance provision, and analysis of risk.

Specifically, the CLCC is advising on the in-orbit operator liability limit in relation to potentially reducing insurance requirements and liability limits of satellites in orbit. This would be achieved by replacing the fixed liability limit with a variable one, using a number of risk criteria to determine a limit which reflects the specific risk in each case.

The CLCC is also helping to explore alternatives to traditional third-party liability insurance to cater for various spaceflight related risks, including what the impacts of alternatives to traditional insurance could be on the insurance market and the space sector.

BEIS, Nuclear related incidents

In the highly unlikely event of a nuclear related incident, government has responsibility for third party liabilities. On 1st January 2022, the 2004 Protocols came into force which amend the rules embedded in the 1960 Paris Convention and the 1963 Brussels Supplementary Convention relating to nuclear third-party liability international conventions. As a result, an increased level of compensation is available to victims.

The 2004 Protocols increase the operator liability in the event of a nuclear incident from the current €140m to a maximum of €1.2bn over a period of 5 years and extend the period for which claims can be made from 10 to 30 years.

At present there is insufficient commercial capacity to insure this risk completely. Therefore, the government has agreed initially to provide an indemnity, for an economic charge, to operators to cover increased personal injury liabilities for the 10 to 30 year period.

The CLCC, using loss estimates provided by GAD, advised BEIS and HM Treasury on practical ways of dealing with these contingent liabilities, including fair allocation of risk and reward between private sector insurers and the government.

Feedback from departments

We have started collecting feedback from departments we have advised on new contingent liabilities. Feedback so far has been positive, with the CLCC commended for:

- setting expectations well by being clear about what could be achieved in a short timeframe and what further work could be undertaken if more time was available
- challenging in a constructive way by asking appropriate and probing questions

We will review feedback regularly and take appropriate actions in light of the feedback received.

5.4 Forward look for the CLCC's advisory work

With the CLCC still in the preliminary stages of building a database to collate information on the government contingent liability stock, we are not yet able to provide detailed risk-based pricing outputs. However, we have been able to leverage third-party sources (such as banks, credit rating agencies and insurers) to provide detailed estimations of expected losses for certain contingent liabilities which can help inform pricing decisions.

At present the CLCC's remit is focused on contingent liabilities where the government takes on risk that the private sector cannot, limited to financial guarantees and indemnities. We have received several requests to conduct credit analysis on items which are not contingent liabilities such as loan portfolios and advice on lending to local authorities. In the future, loans could be included in CLCC's scope of work given the similar expertise required for the analysis and assessment of loans and financial guarantees.

Based on what we have observed and learned so far about government's contingent liabilities, we have begun to consider a set of broader issues in addition to individual cases. These include:

- **Implicit liabilities.** In many cases, known contingent liabilities may be dwarfed by much larger implicit liabilities where there is an expectation that government will meet the cost. The CLCC is contributing to development of guidance for how such liabilities may be identified and effectively managed.
- **Government's role in risk pooling and plugging gaps in insurance markets.** Flood Re is a solution to the issue of uninsurable homes that does not in fact expose the government to a contingent liability. It shows there is scope for government to intervene by facilitation rather than putting up capital. The CLCC can advise on analogous policies in other areas that might avoid contingent liabilities. In other cases, where government needs to step in to plug gaps in insurance markets, there may be advantages to a more structured approach to facilitate efficiency and benefit from diversification.

Chapter 6: Promoting Best Practice

As a centre of excellence, the CLCC provides expert advice and training to other areas of government. This takes the form of bespoke training, development of risk frameworks and sharing case studies with the aim of improving departmental contingent liability management and bringing uniformity to the space.

6.1 A centre of excellence for contingent liabilities

Building on the work described in the previous chapters, the CLCC acts as a hub for sharing best practice on contingent liabilities and building capability across government. The CLCC helps to build capability by:

- challenging departments to ensure that risks of crystallisation are quantified and that the pricing structure reflects this (such as covering at least expected losses for guarantees and insurances, where appropriate);
- helping to establish standardised frameworks for reducing risks from new and existing contingent liabilities across government; and
- providing a proactive risk-based pricing framework which would include fees levied changing over time as the level of risk changes, incentivising good risk management.

In time, we plan to share best practice methods across government on a regular basis and via a range of channels. A number of initiatives are already in progress such as our first guidance note on calculating expected loss.

6.2 Engagement with government departments

As a new unit within government, the CLCC has prioritised engaging with departments and establishing new forums to build relationships.

To embed ourselves across government we have:

- Established 17 account managers to directly build relationships with departments. Account managers act as a single point of contact between the department and the CLCC. These working relationships with policy and finance teams help us better understand potential contingent liabilities, data availability and approaches to reporting.
- Created a presence on OneFinance (Government Finance Function intranet), visible to over 10,000 finance professionals across government, and used as a central repository for government finance and frameworks. We envisage this as a key platform to share information with our finance colleagues.
- Established the Contingent Liabilities Advisory Network

(CLAN) which is chaired by the CLCC and is a cross-government quarterly meeting for commercial, policy and finance professionals to meet and share experiences, challenges, and perspectives on contingent liability management across government.

- Delivered training sessions on contingent liabilities to several departments and presented to finance professionals and senior leaders across government.

We are seeking to continue to expand our presence to ensure that teams across government are able to benefit from our advice when considering policies which may involve government guarantees or indemnities.

6.3 Risk Framework Development

We are working with a number of departments on developing a framework for financial risk management and over time we intend to broaden this work to other departments subject to their requirements. Frameworks will need to be tailored to reflect the nature and portfolio of individual departments. As a minimum, we expect our work to include:

- Implementing a standardised framework for charging (where appropriate) risk-based fees to cover at least expected losses and ensure the Exchequer is appropriately compensated for risk taken on through contingent liabilities. This could for example include implementing risk sharing arrangements to ensure that first losses are absorbed by the beneficiary.
- Developing expertise to conduct detailed cost and risk analysis on departments' new contingent liabilities and on an ongoing basis be able to monitor and report on the stock of contingent liabilities.
- Considering tolerance limits on exposures relating to specific contingent liability categories (see Annex 3), or geographic locations. We have identified some departments such as DLUHC that have built up considerable experience in the area of assessing risk to adequately price fees and premiums and we plan to use their experience and frameworks to embed best practice across other departments.

6.4 Future reporting

Over time, the CLCC's capability to produce analytical reports will increase as we collect and analyse more data across government in order to form a comprehensive and aggregate view of risks and exposure. This initial report is our first step towards that goal.

Annex 1 – What is a Contingent Liability?

Reporting of government contingent liabilities is covered by the IAS 37 accounting standard, the government financial reporting manual (FReM) and HM Treasury's 'Managing Public Money' (MPM).

Under the accounting standard IAS 37, contingent liabilities which are considered to be remote are not required to be disclosed. For government accounts under the FReM both non-remote and remote contingent liabilities should be disclosed. Liabilities which fall within the scope of other accounting standards (for example, those covering insurance contracts or financial guarantees) are not within scope of IAS 37.

Advantages of using IAS 37 definition:

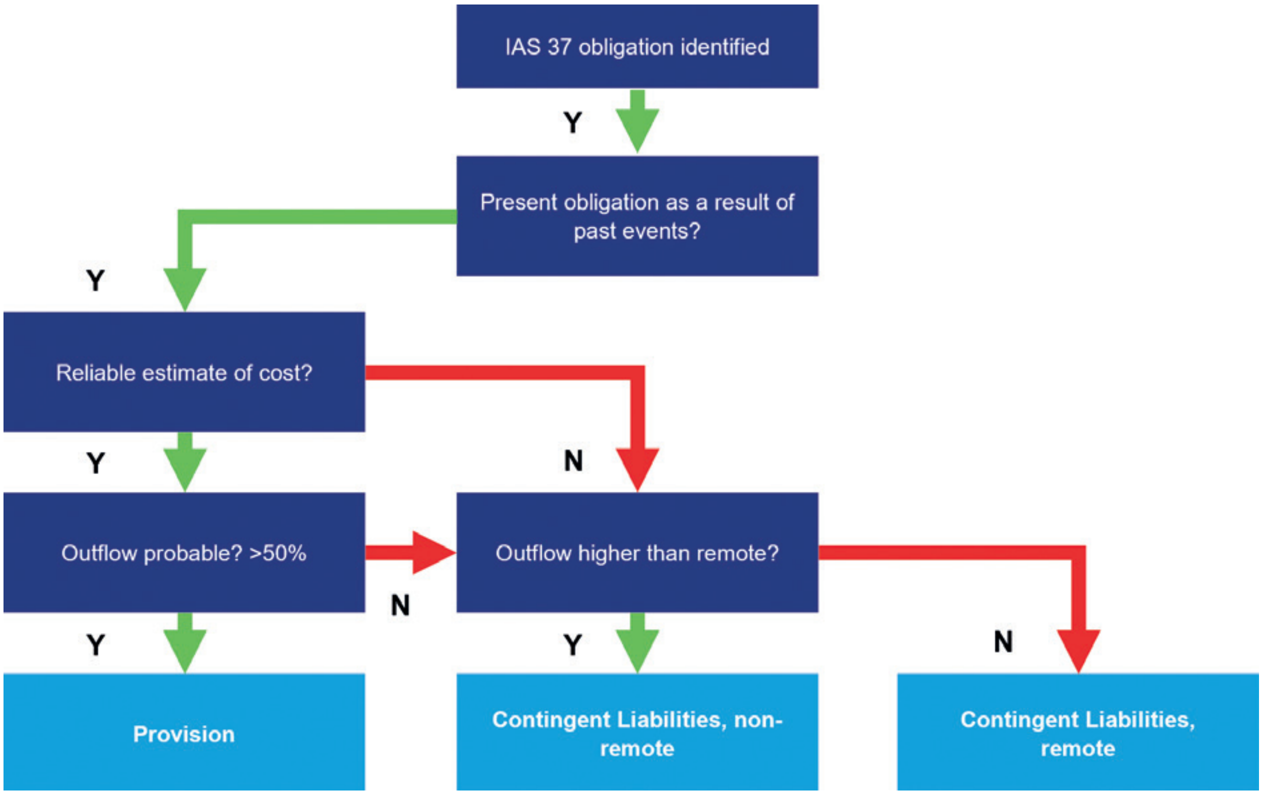
- Focuses on areas of risk which may not be well analysed at present – for example, because they cannot easily be quantified
- Consistent with (although wider than) the CLCC's agreed remit of indemnities and financial guarantees
- Consistent with reporting in accounts

Disadvantages of using IAS 37 definition:

- Does not provide insights into risks on the balance sheet, implicit liabilities or wider financial risks
- Inconsistent with the definition used in MPM[14]

14 MPM has a wider definition of contingent liabilities than IAS 37 to include commitments to future expenditure which are uncertain and where future expenditure may arise if future conditions are met or certain events happen, including >50% probability, therefore the CLCC's scope does not necessarily include all items covered by MPM.

It is also important to differentiate between a provision and a contingent liability where there is a present obligation arising from past events. A provision is applicable if a reliable estimate of cost is available and there is a probable outflow of resources (more likely than not – more than 50%). This is illustrated in the following diagram[15].



15 This chart is based on the Government as Insurer of Last Resort and Government Financial Reporting Manual

Annex 2 – Contingent Liability Data Sources

Summary of data sources providing information on government contingent liabilities

The table below is based on the CLCC's research to identify existing data sources linked to contingent liabilities. We have assessed the value and limitations of these sources as they pertain to CLCC's requirements, which may differ from the intended purpose of the sources.

Data source	Value	Limitations
Departmental internal contingent liability registers	• Largely presented on an individual liability basis • Includes all departmental liabilities, including ALBs and those not declared publicly[16] • Where possible liabilities are quantified • Detailed information on description of contingent liabilities, their status and changes that may have occurred since last reported	• Must be sourced from individual departments • Inconsistent reporting standards and processes • Not all liabilities are quantified • Limited information on items required to better understand risk exposure, likelihood of crystallisation and experience linked to charging and crystallisation
Whole of Government Accounts (WGA)	• Includes most government liabilities • Describes changes over the year • Standardised and accessible via OSCARII	• Most liabilities are grouped, with only large liabilities discussed individually • Sensitive or immaterial liabilities may not be included • Aggregate figures are based on the quantifiable liabilities only, and are limited to maximum exposure

16 Contingent liabilities which are particularly sensitive or have security implications may not be publicly declared.

Data source	Value	Limitations
Department annual report and accounts	• Includes contingent liabilities under IAS 37 and remote contingent liabilities under the FReM[17] • Describes changes over the year	• Level of detail on contingent liabilities (e.g. the number of data fields to be completed by officials) is inconsistent across departments • Sensitive or immaterial liabilities may not be included • Many contingent liabilities are classed as unquantified • Quantitative information is limited to maximum exposure
Written Ministerial Statements	• Includes detailed disclosures of large, novel, contentious or repercussive liabilities from across government[18] • Accessible via parliament website	• Only includes a subset of liabilities • Confidentially notified contingent liabilities may have limited audit trails • Inconsistent information and descriptions • Difficult to find all statements and extract the relevant information

17 The government Financial Reporting Manual (FReM) is the technical accounting guide for the preparation of financial statements within government

18 For further information see A5.4.26 to A5.4.35 of HM Treasury's, Managing Public Money

Annex 3 – Contingent Liability Categories

Summary of the quantifiable contingent liability portfolio by category of liability.

The table below is based on CLCC analysis of departments' annual report and accounts 2020-21, which included identifying quantified contingent liabilities and then placing them into categories of contingent liabilities developed by the CLCC.

Type	Category	Description	Count	Count quantified	Maximum exposure (where quantified) £bn
Indemnity	Insurance	An insurance contract or a portfolio of insurance contracts	3	3	14.5
	Procurement indemnity	An indemnity offered to a supplier as part of a procurement contract	58	19	14.5
	Self-insurance	An indemnity offered to another government entity (central or arm's length)	23	7	10.1
	Insurer of last resort	An indemnity offered because the private sector wouldn't, and the government wants there to be that option	16	8	5.5
	Decommissioning indemnity	An indemnity due to obligations to clear a site	15	4	0.1
	International indemnity	An indemnity arising due to agreements with other countries or intranational organisations	7	1	<0.1
	Fault indemnity	An indemnity offered to protect a non-government entity from damage due to government activity	14	5	<0.1
	Appointment indemnity	An indemnity against personal liability offered to an individual appointed to a role	24	2	<0.1

Type	Category	Description	Count	Count quantified	Maximum exposure (where quantified) £bn
Purchaser protection	Purchaser protection	An indemnity offered to an organisation purchasing or using a government asset	17	7	34.9
Guarantee	Callable capital	A potential obligation from holding callable shares in an organisation	5	5	48.4
	Guarantor of last resort	A guarantee offered because the private sector wouldn't, and the government wants there to be that option	14	13	15.1
	International guarantee	A guarantee arising due to agreements with other countries or intranational organisations	6	6	11.6
	Pension guarantee	An obligation relating to shortfalls in a funded pension scheme	15	8	8.6
	Self-guarantee	A guarantee offered to another government entity (central or arm's length)	2	2	0.2
	Credit facility[19]	An obligation to provide loans up to a certain amount to an entity	1	1	<0.1
Legal case	Legal case	A legal case or a portfolio of legal cases	49	19	48.0
Uncertain cost	Uncertain cost	A cost to government which is uncertain, such as employment costs or uncertain take up of funds	35	12	0.7
Unknown/ mixed	Unknown/mixed	There is not enough information to determine a category, or there are multiple categories of liabilities	22	15	1.8
Totals			**326**	**137**	**214.2**

19 For the purpose of this exercise, credit facilities are captured under guarantees


MORROW