

Joint Committee on the National Security Strategy

Oral evidence: National security spending

Monday 29 November 2021

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4.40 pm

Members present: Margaret Beckett (The Chair); Lord Brennan; Richard Graham; Baroness Healy of Primrose Hill; Baroness Hodgson of Abinger; Lord King of Bridgwater; Lord Laming; Baroness Neville-Jones; Sir Edward Leigh; Lord Strasburger; Lord Reid of Cardowan; Bob Stewart.

Evidence Session No. 1

Heard in Public

Questions 1 - 19

Witnesses

I: Rt Hon Simon Clarke MP, Chief Secretary to the Treasury; Catherine Little, Director-General, Public Spending, HM Treasury.

Examination of witnesses

Simon Clarke and Catherine Little.

Q1 **The Chair:** Welcome, Mr Clarke, and Ms Little, who is with us virtually. Thank you very much for coming to give evidence to us today. This is a one-off session to look at the role of the Treasury, particularly in national security spending. That is the focus of our interest, following our report on the machinery of the national security world in September. This particular issue has been of long-standing, almost continual, interest to this committee and its predecessor.

This is a hybrid meeting. Not only Ms Little but some members of the committee will be attending virtually. Chief Secretary, I believe that you want to say something briefly at the beginning, so please fire away.

Simon Clarke: Thank you, Dame Margaret, and the committee, for the invitation to be with you today. I want to preface the hearing with a short statement to the effect that the evidence I provide today will hopefully demonstrate the close alignment between the integrated review, the

spending review 2020 and the spending review 2021. The evidence I provide will also demonstrate close joint working between the Treasury and the Cabinet Office, and how, despite the disruption caused by the Covid-19 pandemic, funding settlements agreed at both spending reviews support the delivery of the priorities and objectives set out in the integrated review, from tackling threats from cyber and hostile states to delivering strategic advantage in science and technology.

The Government's commitment to realising the ambition set out in the integrated review and ensuring its successful delivery is demonstrated by the funding provided, which included over £24 billion over four years for the MoD, the largest sustained increase in the defence budget since the Cold War. The UK will also maintain our position as one of the largest development spenders in the G7, spending more than £10 billion this year, in spite of a temporary move to spend 0.5% of GNI, which was agreed in response to the exceptional fiscal and economic circumstances caused by the Covid-19 pandemic.

Overall, I am confident that this is a very good outcome for our national security and for the delivery of the integrated review. The total government spending is growing in real terms at 3.8% a year on average over this Parliament, an increase of £150 billion a year by 2024-25, which is the largest real-terms increase for any Parliament this century.

Q2 The Chair: Thank you very much. I am sure the committee will have taken that on board. You mentioned both the 2020 spending round and the 2021 spending review. There were two different National Security Advisers. What role did the National Security Adviser play in co-ordinating and helping to finalise the spending allocations under those two rounds?

Simon Clarke: The whole intention of our work was to make sure that there was total coherence between the IR and the SR, and the National Security Adviser sat at the heart of that process. There was regular director-general-level engagement between the NSA, the deputy NSA and our officials to ensure that SR20 and SR21 were in full alignment, to seek Cabinet Office views on bids and to update the Cabinet Office on funding decisions as they emerged. There was close interaction between the two buildings.

The Chair: That is very interesting. A recent report by the Institute for Government says that if there is a disagreement among senior Ministers about spending priorities, it is usually the Chancellor who gets his way. Do you think that is a correct judgment?

Simon Clarke: Obviously, the Treasury has a fair degree of final decision-making power in these situations, but it is certainly only one equity in the decision. Ultimate power rests with No. 10, and there is an interaction almost three ways in discussions between any department, the Treasury and No. 10 in apportioning both priorities and resources, according to the discussions that unfold. The Chancellor is a massively important figure in those discussions, but it is always a balanced discussion as well.

The Chair: There are at least 20 cross-government sub-strategies under the integrated review. Making sure that they are all fully funded with regard to the relative priorities of the Government under the IR is a key issue. How do you ensure that is happening?

Simon Clarke: The sub-strategies are an important part of our work. The Treasury has ownership of the economic security sub-strategy, which we are working on at present, and it is about making sure that each department takes responsibility for delivering against that. Cat may wish to comment further, but there is an ongoing process of assurance to make sure that those strategies are being delivered, and that will be a key theme of the spending review period that lies ahead, through to 2024-25.

The Chair: Would you like to comment, Ms Little?

Catherine Little: Yes, Chair. Following what the Chief Secretary said about the process and the close alignment between the Cabinet Office and the Treasury, right up front in the work we did with the NSA and the National Security Secretariat was the prioritisation of the sub-strategies. The way in which we worked to prioritise funding and make sure that resource was allocated was very much based on the overarching IR framework.

The assurance process that we have in place follows the process we have for both domestic and international policy. You have probably seen that in the spending review we published priority outcomes for government. We have aligned all the funding allocated in the SR to those priority outcomes. They had been updated for the conclusions of the integrated review, and they are now part of how departments go forward in producing their business plans. They are called outcome delivery plans. Every department has to report monthly on its progress against outcome delivery plans. We work with the national security and strategy unit to make sure that the outcomes of those reports are followed up and, as necessary, escalated to the National Security Adviser.

Q3 **The Chair:** This committee has long taken an interest in how considerations of national security influence the spending priorities and the spending review. I notice that both of you referred to the Cabinet Office. Fine, but in the past we have recommended that the National Security Council be given a more formal role in reviewing the decisions made about departmental settlements on national security. Is that something the Treasury has considered or would be prepared to consider?

Simon Clarke: The National Security Council, chaired by the Prime Minister, sets its agenda according to the priorities of the day. Clearly, the National Security Ministers' meeting, which sits underneath that as a sub-committee, convenes more frequently. It is chaired by whichever senior Cabinet Minister is most relevant, and is designed to ensure that there is greater ability for that body to convene. That may well be a more appropriate setting for some of the specific issues thrown up by the IR to

be considered. If the National Security Council wished to review those things, that would be within its ability to determine as a priority. It would certainly not be something we would resist. We would always want to make sure that the Prime Minister and the Cabinet had the ability to interrogate progress against our priorities.

The Chair: That was one of the things I wanted to know. That is not unhelpful. Thank you. You talked about priority outcomes by department rather than across government.

Simon Clarke: In the new architecture, in essence the NSM is a sub-committee. The Chancellor, for example, would chair meetings that pertained to economic security issues, and different Ministers would take the chair depending on the issue in discussion. That gives cross-cutting ability across the piece of government to make sure that there is coherence in our national security work.

The Chair: Chief Secretary, perhaps I should warn you that the committee is not necessarily thrilled by the new architecture to which you have just referred. The next question is from Lord King.

Q4 **Lord King of Bridgwater:** If I may say so, both of you have come fairly recently to your new responsibilities. The Minister brings previous experience in the Treasury, and Ms Little brings experience of the MoD as well. I want to ask you about our defence expenditure. The spending review sets out our national strategic priorities for the next three years. Having picked it up new and fresh, do you both agree with it?

Simon Clarke: Yes, I do. I am confident that we are giving a very strong settlement for defence. As I alluded to in my opening remarks, we have an additional £24 billion over four years, which is mostly in capital investment in new equipment. It is the largest sustained increase in defence spending since the end of the Cold War. It is not designed just to be a large number that we can cite on occasions like this. It is real, hard-edged equipment purchasing that has transformation potential, whether that be the new eight Type 26s and the five Type 31s, investment in renewal of the deterrent, or progressing our carrier strike capabilities with at least 48 of the F35s by the middle of the decade. These are serious changes and are complemented by some of the new investment in cyber, which is designed to reflect the changing nature of warfare.

I am confident that it is a strong settlement that sends a strong message that the UK is very serious about our role within NATO. It reflects the fact that the world is clearly more dangerous than it has been for some time, and the UK is determined to make sure that we play our full part in shaping that international order. This goes to the interaction with the wider IR. If we are to maintain global stability that continues to shape international order in a way we would want it to be shaped, rather than to have it shaped for us by others, we need a credible defence position, which is precisely what SR20 and the four-year, or multiyear, settlement was intended to give us. It gives all our armed services the long-term funding certainty they need to deliver key equipment programmes at

pace, to make sure that we are ready for whatever scenarios unfold over the years ahead.

Lord King of Bridgwater: I am pleased that you mention cyber, because that is a completely new dimension since my involvement in this field in ancient times. It is all very well having all the new weapons, all the new communications and all that, but they need to work. It obviously has considerable implications for our nuclear deterrent as well. Are we satisfied that we are committing enough in that area, which is a huge, new and challenging area?

Simon Clarke: You are absolutely right. This is undoubtedly an area where warfare is changing fastest, and it includes the difficult grey zone where war and peace merge, and there is clearly a contested space in which we need to engage. SR21 provides a £114 million increase in the national cybersecurity programme across the period, which is designed precisely to make sure that we continue to innovate and invest as a responsible and democratic cyber power.

In total, we are investing £2.6 billion in cyber and legacy IT over the SR period precisely to make sure that we are strengthening our resilience. That is in addition to the funding agreed for the national cyber force, which is a joint MoD-GCHQ enterprise, funding for which was provided through the SR20 settlement for the MoD. The new national cyber force will conduct cyber operations to disrupt hostile state activities, terrorists and criminals. It is an offensive capability to counterbalance our defensive capabilities based on resilience.

Lord King of Bridgwater: We hope that we never have to use all these wonderful weapons. Not to have to use them depends very much on the efficiency and effectiveness of the Foreign Office and the hope that diplomacy can triumph. The worrying figures, I thought, were the cuts in the Foreign Office budget at a time when, in such a troubled world, effective diplomacy at every possible level is never more important.

Simon Clarke: I agree completely that we always want to win out through the use of diplomacy. There is no question; the Foreign Office remains very well equipped to deliver for the UK in this space. We continue to have one of the largest diplomatic networks of any country. Our reach is unparalleled across a range of theatres, not just through NATO but the Commonwealth, our recent role in convening COP, and the G7 presidency. We continue to exercise an influence that is in the best traditions of British leadership in the world, and the Foreign Office is resourced accordingly. I believe I am right in saying that there was a 4.4% TDEL increase for FCDO across the SR21 period. That is designed to make sure that the Foreign Office has the resources it needs to continue to serve our interests.

Lord King of Bridgwater: I thought it was an actual cut.

Simon Clarke: There is a 4.4% TDEL increase across the piece. Cat will correct me if I am wrong on that.

Lord King of Bridgwater: What assessment did you make on leaving the EU that it was all the more important to establish our presence on things that might otherwise have been left to the EU to handle under the EU umbrella? Now we have to handle them on our own. Does that not indicate the need for even greater resources?

Simon Clarke: Across the SR, one of the themes of departments' bids—Cat will come in in a moment and complement this—was to look at the new sovereign functions that had accrued to any given department as a result of our decision to leave the EU. The UK already had an outstanding foreign service prior to our leaving. We remain confident in its capabilities. In so far as new responsibilities have accrued, and there are some that obviously pertain to the Foreign Office, the 4.4% increase in its TDEL is precisely designed to enable that to be part of its work.

Catherine Little: We funded over £9 billion in preparations for EU exit, as well as funding the new sovereign functions that inevitably are required following departure from the EU. That is a significant level of investment in preparing and planning, as well as in making sure that we can discharge our responsibilities going forward.

Lord King of Bridgwater: Are you talking about the Foreign Office budget?

Catherine Little: No. Across the whole of government, we have invested about £9 billion.

Lord King of Bridgwater: That is what it cost us in extra costs in leaving.

Catherine Little: It is a combination of preparing for EU exit and planning for various scenarios, but also taking on new sovereign functions. That has now been baselined as part of departmental spending plans.

Lord King of Bridgwater: Thank you.

The Chair: Could I interject for a moment, Chief Secretary? In the funding figures before me it appears that, although preceded by some increases, there has been an overall cut in the Foreign Office budget of 5%. I am under the impression that the MoD and the Foreign Office, where they have growth, are getting rather less than most other departments, which is an interesting insight into security priorities.

Simon Clarke: There was certainly a 4.4% increase in the total departmental settlement for FCDO. When it comes to the MoD, we need to consider this in the context of the four-year settlement that was agreed in SR20. Therefore, the figures for SR21 for the MoD can be somewhat misleading on the face of it, because the four-year settlement was heavily front-loaded for defence.

If you look at the figures for the period running from financial year 2020-21 through to financial year 2024-25, there is a 6.8% increase in the

capital budget—the capital ARG¹—for the MoD and a 2% increase in the TDEL—the RDEL and CDEL combined—over that equivalent period. Therefore, the outcome you get depends on where you slice the figures for MoD. Fundamentally, it is a four-year review with a lot of the investment up front, precisely designed to enable the equipment investment I touched on earlier. Measured only over the three years of the SR, there is a very slight fall in the ARG of 0.4%, but that does not capture the fact that there is a very big uptick of investment in 2020-21.

Q5 **Baroness Neville-Jones:** Minister, in your opening statement you referred to the importance of coherence in the operation of national security policy. Can I take a specific example? In 2020, the spending round was agreed while the integrated review was still in the process of being drafted. First, what were the Treasury's operating assumptions, given that you did not have the guidance of a review? Secondly, when the review came along, was there a discrepancy of any kind that would require modification because of the spending allocations already made?

Simon Clarke: This is an important area for us to reaffirm. It was always the intention that the integrated review and SR20 would run absolutely in lock-step, hence the IR was launched on 26 February 2020 and SR20 was launched two weeks later on 11 March. It was only the interruption of the pandemic that led to SR20 being first delayed until the autumn of 2020 and then made into a one-year spending review. Clearly, that was not how we would have done it had the pandemic not intervened, but it is equally important to reaffirm that the IR has informed both SR20 and SR21. The policy framework for the integrated review was completed in late July 2020, some four months before SR20 was published on 25 November. SR20 was heavily informed by the headline policy framework of the integrated review, as was the multiyear MoD settlement announced by the Prime Minister on 19 November.

We live in a world where we continue to refine all our assumptions, but we remain confident that that framework is the right one and, therefore, that the settlement was based on the right set of assumptions. The IR itself was published on 16 March this year.

Baroness Neville-Jones: As I understand it from what you are saying, there was communication between an as yet unpublished IR and Treasury allocations.

Simon Clarke: That is correct.

Baroness Neville-Jones: Could you parse "informed", which was the word you used? What does informed mean? Was there in fact a negotiation?

Simon Clarke: It told us the key policy priorities that should inform SR20 and specifically, given that it was the lead item, the four-year, or multiyear, MoD settlement. There was a very clear read-across between

¹ Where ARG refers to the Covid-19 Additional Restrictions Grant

those principles and the settlement that was then negotiated. Those principles were at the heart of the discussions between Defence Ministers, the Treasury and No. 10.

Q6 Richard Graham: Chief Secretary, can I come back to the FCDO budget for a moment? The total budget of the FCDO will be hugely affected by Treasury estimates of gross national income, given that our aid budget is 0.5% of GNI. What was the core spending of the FCO without the D, if you like? What was the percentage change there? I suspect it is rather different from the 4.4% increase that you covered for the whole department.

Simon Clarke: I do not have that specific figure in front of me, Mr Graham, but I can certainly write to you about it. Cat may have it with her.

Richard Graham: Would your colleague be able to look it up and confirm it while we are talking? Perhaps I could go into one other detail.

I declare an interest as chair of the Westminster Foundation for Democracy. My understanding was that HMT had insisted on flat cash settlement for all the non-departmental government bodies, which include, for example, the British Council, the Westminster Foundation, the Great Britain-China Centre and Wilton Park. If that was the case, how does it fit into our ambitions for global Britain?

Simon Clarke: SR20 was certainly held in the very difficult context of the pandemic and the wider fallout, which, as we know, has been extraordinary; it has been the worst recession in 300 years, with a commensurate impact. That informed in particular the short-term move to 0.5% of GNI spending on ODA, for example.

We were, however, in a position generously to support the British Council, to which you alluded. I think I am right in saying that we gave a very substantial quantity of loans over that period to support its work, and there is further support for the British Council in SR20-21 as well. Cat may wish to say more as to the wider nature of the settlement, but it was certainly intended to make sure that the FCDO was resourced to do all its work.

Richard Graham: Is it possible to hear from the Director General?

Catherine Little: Yes, of course. I can only endorse what the Chief Secretary said. We went through a very comprehensive process to make sure that funding was available to cover all the priorities we had agreed up front.

Richard Graham: Yes, but on the specifics, what was the percentage for the core funding of the FCO without the D?

Catherine Little: Apologies. Teams are just looking up that detail, and I will come back to you very shortly with the detailed figures.

Richard Graham: On the non-departmental government bodies, the Chief Secretary implied that there was a generous loan policy for the British Council, which is not quite the same as the budget, but I understood that there was a flat cash requirement for all the non-departmental government bodies. Is that correct? You pause.

Catherine Little: Yes. That is correct. Sorry, I was not sure whether that was directed to me or the Chief Secretary.

Richard Graham: Turning to a process point, Chief Secretary, my understanding is that the Cabinet Office is tracking the deliverables while the Treasury looks at the outcomes and performance metrics. So that we are clear, are the deliverables basically the outcomes that have already been determined in the performance metrics under SR21, or are they slightly separate things?

Simon Clarke: We are now in the process of clearing the outcome delivery plans for the period 2022 through to 2025, which enables departments to plan how they will achieve the outcomes set in the SR. In parallel, I am in the process of sending out settlement letters to each department, which set out the specific settlement and the conditions attached, but the ODPs are the key yardstick against which we assess delivery over this period.

Richard Graham: In some of the issues that affect our work on global Britain, particularly in the FCDO, the priority outcomes are potentially in contradiction with each other. Take, for example, a priority outcome of building economic diplomacy by seizing global opportunities; it implies increased trade and investment and so on. On the other hand, strengthening the security and resilience of the UK by defending our interests could imply a reduction in trade and investment.

Nowhere is that potential contradiction more apparent than in our relationship with China. If we were going to build trade and investment, we could be looking at a JETCO, not to be confused with an FTA; and we would be looking at continuing the increase in trade and investment that has happened with our third biggest individual country trading partner. On the other hand, if we were going to pursue more under the National Security and Investment Act and other restrictions that have been mooted on trade with China, or pursue a policy of less engagement, which some colleagues are very keen on, that would have precisely the opposite effect. How do you balance different metrics when they might be in opposition to each other?

Simon Clarke: This sits at the heart of our wider relationship with China and its complexity. We want a good, constructive relationship with that country; we want an active trading relationship that is to the direct benefit of both countries, provided it is conducted in a transparent and fair way.

What we cannot do is allow a situation where there are some risks to the UK or that compromises our values. There is no question; there are grave

concerns about some of the actions of the Chinese Government. We need only think of their treatment of the Uighurs, their actions in Hong Kong and their recent threats towards Taiwan to see that China is behaving in a way that is not always easy for us to reconcile with our values. I think we need to be clear-eyed as to the nature of the Chinese Government and not naive about the fact that there is a need for us to make sure that we have the right protections in place.

We have the National Security and Investment Act, which comes into force on 4 January and strengthens the Government's powers to scrutinise investments on the grounds of national security. That is an important protection. Equally, I would not want us to be in a position where we were turning away good investment by China in the UK that can act to the benefit of this country. That tension needs to be considered throughout the course of the wider work of the Government. It is not solely a question for the Treasury by any means, but I think it is a resolvable tension. We are almost in a position of trust but verify, and that remains the resting stance of the Government.

Richard Graham: Indeed, but the question that emerges is: which metrics do you use in order to adjust departmental spending up and down in the period up to 2025? For example, you could increase spending on security to combat some of the problems you rightly allude to, or you could increase some of the work by, say, the DIT to enhance trade and investment if things seemed to be moving positively in that direction. How will you look at the metrics to fine-tune the spending over the next two or three years? I only choose that as a particular example.

Simon Clarke: I am very pleased that we have been able to conduct a multiyear SR this year relative to what we were able to do in 2020. The whole value of that is to give departments certainty as to their budgets, so we will not be conducting wholesale reappraisals of those budgets. The relative priority that departments ascribe to particular themes of work has to be subject to an ongoing conversation with Treasury. If, for example, there is a wholesale change in the nature of our relationship with any given country, we would need at least to consider that, but the SR is intended to settle budgets and give certainty. We would not be looking to scale budgets depending on our particular relationship with China, unless there was a very radical development. To reopen the SR would be a very major step indeed. There is a very high presumption against us doing so.

Richard Graham: Thank you.

Q7 **Baroness Neville-Jones:** Minister, I want to ask you a bit about a different definition of resilience in relation to emergency planning. The Government have a national resilience strategy, which I hope we shall all see soon. I hope it will be cross-government. Its implementation relies on local authorities traditionally but also with the devolved Administrations. How do you reckon that package will be funded? Will there be extra funding to the devolved Administrations, or will they contribute from their existing budgets? How do you reckon to do that? It is a relatively new

area.

Simon Clarke: Resilience sits at the core of national security. I agree with that absolutely. We were in a position through this SR to give a record block grant settlement to the devolved Administrations. Since the onset of devolution in 1998 they have never received a more generous Barnett allocation than has just been delivered, so that will form the core of their support for additional challenges.

I have quarterly meetings with the finance Ministers of the Scottish, Welsh and Northern Ireland Administrations, and those are open fora for frank discussion about the challenges they face. We are confident that with a record Barnett settlement they are funded for the devolved aspects of the challenges we face. A great deal of the national security framework is still a reserved matter for Westminster, but insofar as it pertains directly to their work, we are confident that they are funded appropriately.

We are also in a position to give the best settlement for local government for many years this time around: £1.6 billion in each of the three years of the SR for the local government settlement. That is intended to address some of the challenges of resilience. My own local authority of Redcar and Cleveland was the victim of a hacking attack that was very damaging for the council and posed a real risk to its ability to look after my constituents. It is absolutely vital that local authorities are supported to put the right measures in place, particularly to protect their cyber networks, which are otherwise very exposed to risk. We would want to make sure that they have the same protection as central government.

Catherine Little: Could I briefly add something? Apologies for interrupting.

All the funding that we anticipate is needed to deliver on the resilience strategy was in the 2021 spending review settlement. We have been working very closely with the Civil Contingencies Secretariat on resilience across government. That includes funding both for the devolved Administrations and for local government, as the Chief Secretary set out. It also includes funding for things like flood defence where we had about £900 million-worth of additional investment; it also includes £2.6 billion-worth of investment in cyber and legacy IT. I am confident that resilience has already been fully funded as part of the work in the spending review.

Baroness Neville-Jones: If I may turn for a moment to the devolved Administrations, how does the Government ensure that the spending that takes place is in line with what they regard as the correct expenditure under the resilience strategy?

Simon Clarke: Barnett allocations are designed to reflect the priorities we ascribe to core functions. It is a measure of devolution that we have to leave a degree of implementation to the DAs, but our officials are constantly in contact with theirs, and there is very high commonality of standard setting across the four governments, if you like, to make sure

that we are working together. The fora that I convene quarterly are just one function of our relationship as the Treasury with the finance ministries of each of the DAs, to make sure that they are doing work that we think is a sensible use of public money. Insofar as issues arise, there is potential for conversations between those meetings, but that is the point at which we come together to discuss.

Q8 **Baroness Neville-Jones:** I can see room for argument but also agreement on priorities. I think my next question is difficult to answer, so see what you make of it. How do you judge value for money when it comes to preventive activity? If as a result of expenditure a flood does not take place, how do you assess the value of that? It is one of the things that is most difficult to assess.

Simon Clarke: Indeed. It is the value of something that does not transpire. The Green and the Magenta Books are our key Treasury metrics in understanding our options and the values that flow from those. That is all part of testing the investment case for any given proposition. You are quite right; in many ways, that underpins so much of the rationale for our spending on the security agencies and the military. It is absolutely an insurance policy against risk crystallising. I think we have what is widely regarded as a world-leading set of metrics to make sure that investment decisions are properly tested and capture the costs or the risks of inaction as well. Cat may wish to elaborate further.

Catherine Little: It is a very challenging area. I spent three years of my career at Defence justifying the value for money of insurance policies and contingent investments in capability that I hope we never need to use. Ultimately, we have to use a very sophisticated range of metrics and assessments to try to inform what value looks like, especially in preventive and deterrent capability.

Having said that, we have quite a range of different cases, whether on flood defences or on major defence capability, where we can use historical trends and outcomes to help inform our views. It is not always quantitative; quite often it is a qualitative judgment that we have to undertake, taking into account cost benefits and the risks involved.

Q9 **Baroness Neville-Jones:** Thank you. One hopes in a sense that successful preventive action is recognised and rewarded. When this committee wrote its biosecurity report, it recommended that there should be multiyear ring-fenced funding for horizon scanning and preparation for disruptive events. I hope the reasons for that are fairly obvious. Will you adopt an approach of that kind in the resilience strategy?

Simon Clarke: We apply ring-fences where we think they are appropriate. There is always a dynamic of wanting to make sure that departments and individual Secretaries of State have the discretion they need to manage their budgets and to be accountable for doing so. We try not to cut across that more than we need to, but clearly we impose conditions, including ring-fences, where appropriate, and were we to think it appropriate in the resilience sphere we would do so.

Line items of budgets are set for certain things. A certain proportion of the Defra settlement, for example, is precisely for flood defences and, therefore, is allocated for a specific purpose. Where tighter ring-fences are specifically required we utilise them. As I said, there is a balance in our work between trying to make it clear what agreed priorities are and tying the hands of departments. The Treasury has to strike a healthy balance in that regard across all of Whitehall.

Baroness Neville-Jones: I accept all that. In the end, however, I think that part of a successful preventive policy is to allow enough funding and attention to be paid to horizon scanning of a kind that ensures that you direct the money to sensible places. It is very easy to take money away from that kind of activity, so let us hope that we do not.

Simon Clarke: I can assure you that we are very conscious of the wider challenges we face. The last few years have taught us that the unexpected can happen. It has certainly been at the core of this SR to make sure that we are in a position where departments are resourced for challenges that we all hope, as Cat said a moment ago, never come to pass, but if they do we must be ready.

Baroness Neville-Jones: Quite right. The high-impact, relatively rare occurrence is one of the most difficult areas. Thank you.

Q10 **Lord Laming:** Chief Secretary, could we ask for your help on aid spending? We would be very interested to know which Ministers were involved in the decision to cut overseas aid spending to 0.5% of gross national income in 2020.

Simon Clarke: The decision to reduce our spending temporarily to 0.5% of GNI was taken by the Chancellor of the Exchequer, the Prime Minister and the Foreign Secretary. Obviously, it is a collective decision agreed across government, but they are the lead interlocutors in this space. It was they who signed off that decision. It is now policy, as it passed through Parliament, but that was the process during summer and autumn 2020.

Lord Laming: Were they involved in setting the two fiscal tests as you move forward?

Simon Clarke: The Chancellor determines the fiscal tests for the return to 0.7%. It is great news that we now anticipate that we will be returning to that by the final year of the SR settlement.

Lord Laming: Was any assessment made of the impact that this reduction would have on the services? For example, how many programmes had to be terminated?

Simon Clarke: As always, when you make a decision you have to assess what its likely impact will be. The Government had to make a series of very difficult decisions in the course of 2020 reflecting the extraordinary exigencies of the pandemic and the pressures that placed on the public finances. I think it was a proportionate measure to reduce our aid

spending at a time when we were spending of the order of £400 billion in our wider response to Covid. I think that is something the public very much accept.

Lord Laming: Those very senior Ministers understood at the time how many girls would be deprived of continuing education, for example.

Simon Clarke: All these decisions are for Ministers to balance, and it was understood that a reduction in our aid spending would have an impact on our wider work. It is important to remember that 0.5% of GNI still represents aid spending of £10 billion a year. Even under the 0.5% target, that will rise to £12.3 billion a year by financial year 2024-25. That leaves us as the third highest spender on aid in the G7. It is well above the OECD average of 0.41% in 2020. It is still a very substantial commitment by the UK and one of which I think this country can be very proud.

Lord Laming: Do you think the figure for 2024-25 is realistic? You are the expert on this, but, as I understand it, it would require an increase in a single year of £5.2 billion. Is that realistic?

Simon Clarke: It is precisely because we all hope that we will be returning to 0.7% at the end of the SR period that we have floated that prospect now, based on our forecast. There is a need for departments to plan ahead and provisionally allocate what they would do if that increase occurred. You are right; it would be a very sharp in-year increase as we returned to 0.7%. It is very important that we deliver best value from that, if indeed the GNI figures bear it out as we move through the course of the SR.

Alluding to the fact that we anticipate that—albeit without absolutely affirming that it will happen, because obviously it remains contingent on the wider economic situation as it comes to us over the next few years—allowing departments to plan on the basis that it is something they should be considering allows them to plan ahead of time how they will spend that increased budget.

Lord Laming: I am all for the increase. Let me be clear about that. I want to be sure that preparation is taking place to ensure that there is good value for money and that we achieve the impact of increasing the amount of money in one year.

Simon Clarke: Saying provisionally that we anticipate that this will happen is designed precisely to allow departments to do that planning. That is an important part of the FCDO's work, but a lot of departments have a stake in this through their own ODA spending. By signalling that we anticipate a return to 0.7%, albeit that everything remains uncertain, we are sending a very clear message to departments that they should plan for that eventuality, and make sure that they have scalable programmes in place that could be extended in the happy event that the economy is performing really strongly at that point and 0.7% can be returned to.

Q11 Richard Graham: I congratulate the Chancellor on this part of his Budget announcement. I think it was brave and was looking ahead. There are great opportunities—I would be interested in your comment on this—in using the new BII to help with both infrastructure development and the carbon transition needed, in the way we have announced for South Africa for example.

Do you feel that there are opportunities for departments to use the intended increase in spending in 2024-25, for example, to help failing states where it could be argued that large numbers of migrants who make their way to the EU and the UK could be considered a strategic threat to the stability of western democracies? Is that the sort of issue that you feel the increase mooted might be able to tackle, or do you have other things already in mind?

Simon Clarke: I think that is a very fair comment. It is absolutely the case that when looking at the value of our overseas aid spending we reaffirm the point that, insofar as we can promote more stability in country and prevent migrant flows, we can address some of the challenges they pose. That has been brought into stark relief in the light of recent events.

There is a further security dimension in that you can see how migrant flows can be weaponised by more or less rogue states like Belarus in their relationship with western Europe. It is absolutely in our interests to try to strengthen the situation in countries that are struggling, or are outright failed states, to try to make sure that we reduce the pressure on people to flee in search of a better life. That is one of the most important purposes of our aid spending.

The Foreign Secretary, as we speak, is leading the development across government of a new international development strategy, designed to ensure alignment between our aid spending and the integrated review. This will be a very important document when it is published, I anticipate in 2022, in informing the wider strategic sense of what our aid spending can unlock. I will not cut across that by setting out my own personal views, but the Treasury is there to support that work. We certainly look forward to seeing the strategy, which will continue the process of constantly making sure that when we are spending £12.3 billion on 0.5% of GNI, and more like £17 billion on 0.7%, we are delivering against the things that make the most difference.

Lord Laming referred to education for women and girls. I know that that is a personal priority of the new Foreign Secretary, but there is a variety of things that we need to do, all of which go towards the overarching goals of the IR: a more stable and predictable world, where western values of tolerance and democracy can be more easily both defended and disseminated.

Q12 Richard Graham: Perhaps I might ask a brief supplementary, Chair. I am sure that all of us would agree with everything the Chief Secretary has said.

The IR geographically is very much based around the Indo-Pacific pivot, which I wholeheartedly support for obvious reasons, but on this particular issue of challenge the areas of geographic interest are much closer to home. When it comes to looking at the Foreign Secretary's new priorities, and, a year or a year and a half ahead, the wider discussion about how the increase in money can most successfully be used, will the Foreign Secretary and the Treasury make sure that you also look at the impact of failing states rather closer to home, which may indeed include some in Europe by then?

Simon Clarke: I know for a fact that the Foreign Office is keenly aware of this as well. You are absolutely right in affirming the centrality of the Indo-Pacific tilt to wider government thinking; it is a key part of the global Britain agenda to recognise the opportunities that exist in that region. There are many wonderful opportunities from the extraordinary advances in Asia that we are seeing. The UK stands to benefit from those, as do hundreds of millions of people in those countries, but clearly it is not the only dimension of our foreign policy. Many of the problems stem from the wider horrors of Syria and the challenges in the Kurdish part of Iraq. We can all see that those areas are absolutely central for us, as well as all the challenges of north Africa. There is no question but that the Foreign Office is well seized of that, and that will be a key part of the international development strategy.

Richard Graham: Thank you.

Q13 **Baroness Hodgson of Abinger:** My colleague has already touched slightly on the first part of the question I was going to ask. To what degree do you look at the effects of cutting the aid budget? Lord Laming asked about the programmes. What degree of detail do you look at in what cannot be done by reducing a budget and will not be able to happen? For example, did you look at projects that could not be delivered and might thus cause more insecurity, which would then cause greater migration flows? How do you make the trade-off? To what degree do you look at the actual programmes that you will be withdrawing, or the causal effects when you make those decisions?

Simon Clarke: We had a process in place in 2020 that was referred to as the double lock, whereby the former Foreign Secretary conducted a cross-government process after the SR to review in detail how ODA was allocated against the Government's priorities, given the shift to 0.5%. That was very specifically designed for the former Foreign Secretary to reflect his role also as First Secretary of State, to make sure that we were delivering against our core priorities. That led to him setting out seven ODA priorities in November 2020 to ensure maximum cohesion in our spending.

You are right; if you need to make difficult decisions it becomes even more incumbent to get those decisions right and to have thought from a zero-based set of principles about what should be given the most resources. The new international development strategy that the new Foreign Secretary is working on is designed to make sure that we are

constantly testing what we invest our money in. It is an awful lot of money and there is an awful lot of need in the world, and it is very important for all sorts of reasons, not least to win the argument and make the moral and practical case for this investment to the British public, that we show that how it is spent is very well thought through.

Baroness Hodgson of Abinger: It is hard to finalise a forthcoming strategy, given the uncertainty about the funding. I am thinking particularly about the sustainable development goals by 2030 and how we will deliver against those, given this uncertainty.

Simon Clarke: As I alluded to earlier, by signalling ahead of time that we hope to return to 0.7% we have provided departments with a lead-in of two to three years when they can start to make their plans with a scenario of 0.5% of GNI and a scenario of 0.7% GNI.

There is no question; the economy has broadly outperformed expectations. One reason why we face a supply chain challenge is because the global economy has woken up much more vigorously than perhaps was anticipated. The UK economy, thanks to a series of pretty shrewd interventions, has certainly come through this in better shape than we would have hoped, ergo the outlook for 0.7% looks pretty good, but if we have learned anything over the last couple of years, it is that you cannot assume anything in the world of today. We have to be very cautious in our appraisal of some of the challenges that exist globally, but most notably the ongoing exit from the Covid pandemic. We have been reminded in the course of the last three or four days that there may be further twists and turns in the journey before we are through.

Baroness Hodgson of Abinger: We note the move towards capital spending over resource spending for the FCDO under SR21, which suggests an emphasis on, for example, building infrastructure over providing humanitarian assistance. What is driving this change of emphasis? How does it map against the integrated review's priorities for development?

Simon Clarke: We want to make sure that there is a balance of capital and resource spending. Both are valuable in the development space. There is absolutely no question but that the physical infrastructure of countries matters enormously. We need to support that work.

In many cases, departments actively ask to get more capital resource because they have long-term plans that they wish to commit to. In the aid space, certainly, there are many things that we want to support FCDO to deliver. Cat may well have further thoughts more specifically on this. There is no in-principle shift that is the conscious result of policy. It is just profiling the asks of different departments and making sure that we can meet them, not a wider philosophical shift by the Treasury.

Catherine Little: The one thing I would add is that it is not unusual in a multiyear spending review for departments to want to think about greater capital investment, given the medium-term planning and the opportunity

that a multiyear SR provides. There was no top-down direction given by the Treasury. It was very much based on the bids that departments put to us.

- Q14 **Baroness Hodgson of Abinger:** The last part of my questioning is to do with humanitarian assistance and support for women and girls, which is a cause very close to my heart. Both are government priorities for development under the integrated review and for the new Foreign Secretary. What sort of capital investment would help to advance them? Will sufficient capital investment be put in, considering that sometimes it is harder to demonstrate long-term investments as value for money to the general public because there is no outcome that allows you to say that you have educated 50 girls through school? I am sure that will be part of it, but what about the wider goals of empowerment of women and providing encouragement?

Simon Clarke: Those things take many more years to manifest themselves as gains than can be captured in the ordinary course of political discourse. You are absolutely right. That is a tension.

Perhaps the most powerful thing I can say is that, in our meetings with her as part of the spending review, the Foreign Secretary was crystal clear that support for women and girls was one of her absolutely top priorities and that she wants the UK to be an even more active presence in that space. She would certainly be at pains to say that it is at the heart of her vision of the UK's ODA strategy and how the FCDO can best deliver change in the world.

I suspect that where capital spending can best support that may well be school infrastructure, which is so vital. There is much wider work to be done. We need only look at the devastating consequences of the Taliban takeover of Afghanistan for the circumstances of young women there to see that there is nothing automatic about progress in this space. We will need to continue to show global leadership and really push that agenda if it is to maintain the momentum we all want to see. There are so many interlocking benefits from equality of educational opportunity that we need to make sure that it is a key part of our work. The Foreign Secretary could not be more passionate about that. She was pretty insistent on its being given top priority in the settlement. She certainly fought her corner hard.

- Q15 **The Chair:** You have referred more than once to the cash boost that you are giving to defence expenditure. As I understand it, in order to hit its immediate spending targets the MoD is still making quite important cuts in its capabilities. Are you not concerned that, as a result, those capabilities might fall short of the targets set in the integrated review, which were quite ambitious?

Simon Clarke: We need to ensure the wider affordability of the defence settlement and to make sure that defence is fit for the challenges of the 2020s and the 2030s. Those two processes both lead to some difficult, but I think defensible, decisions on the sunseting of various platforms

that are no longer the most relevant, such as the Warrior fighting vehicle and even some of the reductions to troop numbers.

None of these decisions is easy, but they are informed by wider shifts in what the defence establishment believes are the right things for us to prioritise. They allow us to make a series of very important investments. We are upgrading our tanks. We have the new Challenger 3s, which will be back among the most lethal and well defended in Europe. We will have the establishment of our new space command, the renewal of the deterrent and very substantial investments in both our carrier strike capability and the surface fleet. We are making sure that our cyber powers are as well advanced as they can be. We are developing a new combat air system for the RAF.

None of these things comes cheap. We cannot simply add things without looking at the parts of the wider defence base that may not be as relevant today as once they were. Obviously, we are shifting the profile of our forces as well. We are looking to do things to make sure that they are much more forward deployed. That also has impacts on the sort of equipment we need.

It is really important to emphasise that the MoD settlement has been thought through in a way that is genuinely challenging, because we are shifting from the legacy of the Cold War and the era of the war on terror being the main call on our defence capabilities towards a new era where state threats may be more pressing. That is quite a radical shift, and involves some quite far-reaching changes to our defence posture.

Our defence is certainly not being short-changed. We are very confident that we will have a more capable defensive capability now than we had at the start of the SR period. That is precisely what we need to do, given that the world is probably a more serious and sober place today than it has been for many years. If Fukuyama's theory about the end of history looked ambitious a few years ago, it looks even more difficult to sustain now. We are in a world where we need to make sure that we have the right defence settlement.

The Chair: I do not dissent from that, but I think you will be aware that the National Audit Office reached the conclusion that the defence equipment plan was unaffordable for four years in a row, partly because of an MoD track record of forecasting overoptimistically and overoptimism about efficiency plans. Why should it be different this time?

Simon Clarke: Partly because we have seen some of the challenges that flow from that, which therefore were a key focus of the four-year settlement that was agreed, and partly because we are building in the right assurance mechanisms to make sure that it is better reviewed. The National Security Adviser has a quarterly meeting precisely to evaluate our defence programmes. That reports back to Ministers, including me, so that we can have a regular update on progress against a number of our most important programmes.

I know that the Minister for Defence Procurement is absolutely seized of the importance of this and is applying total rigour in his work. I know that he would want to reaffirm that very strongly. There is a wider process now, with the quarterly stocktakes, which will enable much more regular monitoring, including by me, as the Chief Secretary, and by Cat, who brings considerable expertise from her former role in the MoD, to make sure that all these programmes are properly scrutinised. Cat may wish to add more.

Catherine Little: There were lots of lessons learned from SDSR15, in particular. There were the top three lessons that we were very mindful of as we entered SR20. First, we wanted to make sure that we did not bake in efficiencies that were not deliverable, credible or thoroughly tested. Secondly, and this goes back to the question about capability programming, SDSR15 did not undertake all the programming and prioritisation decisions that were needed to live within the settlement at the time. We were very keen in SR20 to do that at the same time as the IR framework was developed.

Thirdly, there was to be a very clear, transparent, open-book basis for understanding the financial baseline we were working to. In SDSR15 there were significant discrepancies in the figures between the MoD and, ultimately, how the overall forecast came together. This time around, we ran a very transparent shared understanding of all the financial metrics involved in agreeing the settlement right from the start.

Those were three important lessons. Obviously, there were many more we could go through, but that was very different from the way in which we established the SR settlement for the Ministry of Defence.

The Chair: That is interesting. For example, how do you expect the MoD to fund “persistent engagement” overseas and a greater presence, which Richard Graham was welcoming, in the Indo-Pacific, given that its resource budget will be cut by 1.4% over the next three years?

Simon Clarke: The resource budget is being reduced very marginally. The ARG falls by 0.1%, if you run over the period from 2020-21 through to 2024-25, precisely because the emphasis is on capital investment and new equipment. We are reducing the size of the Army by about 9,000. In practice, it is slightly less than that, because the Army has been undermanned, so the 82,000 was a fairly notional figure. Nonetheless, it is a reduction in overall troop numbers, but those troops are deployed in such a way that we are better able to engage in the world.

It fundamentally reflects the change whereby we continue to move away from having a large land army sitting in western Europe, based against the risk of a Russian invasion, although we continue to have significant capabilities in eastern Europe, precisely designed to reassure our NATO allies of our commitment to the defence of western Europe. We are trying to make sure that our presence is more forward leaning into parts of the world where so many of the other challenges we face may arise. We saw in the results of the recent exercise involving the Royal Marines, which

was widely praised, that those forward commitments are extremely capable. We should have great confidence that they will be of great value to this country over the years ahead.

The Chair: Can I press you a little more? Both of you have said how you will be able to monitor the delivery of the spending programmes. It is hard to deliver capability like the National Cyber Force, which will be jointly owned by the MoD and GCHQ. Can you say a little more about how you think you will be able to keep on top of that?

Simon Clarke: We continue to work very closely with all the security services. Obviously, this is one of those areas where it is hard to be too specific in open fora, but with the confirmation that the NCF will be located in Samlesbury in Lancashire, it is taking key shape. This will be a very important new string to our bow. We will have the ability to conduct offensive cyber operations against our adversaries, as well as to focus simply on deriving intelligence therefrom and, therefore, maintaining a defensive posture.

We are confident that all the intelligence agencies have been very well resourced in the course of the SR. There is a 3.9% per year average growth rate for the single intelligence account. We believe that will leave us in a very strong posture for the NCF and other new capabilities to take shape.

Q16 **Lord King of Bridgwater:** Can I put this question directly to Cat Little? Having come from the MoD and seen the problems in the past of getting the costs of the traditional kit right, how good do you think it is now at assessing the new challenges and technologies?

Catherine Little: There are quite a lot of lessons learned that apply equally to historical capability and future capability. We should not underestimate how much investment has been made in technology, cyber and research and development in the past. Over the last decade, certainly, it has not been an insignificant part of the equipment plan. In fact, in the last couple of 10-year equipment plans that I oversaw in the MoD, technology, research and modern forms of investment were the second largest investment after the nuclear enterprise. There is plenty of track record of how to improve and learn from the way in which we procure those activities.

Having said all that, there have recently been a number of reforms and reviews of the way the MoD procures and how it can move faster in a more agile world to make the most of the investments that it makes. Obviously, one of the challenges is that technology, research and science move so fast that you have to have incredibly agile decision-making. You also have to take more risk. That is inherently an uncomfortable place for both the MoD and the Treasury to be when it comes to some of the new, more advanced technologies we are investing in, but we openly accept that in order to move quickly and to keep apace of modern changes we need to take more risk. The critical thing is that we learn quickly and that we have continuous learning loops between procurement agencies, the

MoD and Ministers to make sure that we learn lessons quickly and adapt the way in which we procure.

Lord King of Bridgwater: Do we have in the MoD, in particular, persons with a completely different background from those the MoD might traditionally have had in those fields?

Catherine Little: Personally, I believe so. The MoD has different leadership from different backgrounds. For example, the chief information officer has come from the private sector. The chief scientific adviser is a very eminent academic who is very much a leader in science and technology and its application there. It is very much diversifying both leadership and the expertise that it has available to it. I know that it is working very hard to stimulate different partnerships with industry as well. One of the big challenges is that you actually have to change the market. The primes of tomorrow will not necessarily be the primes the defence supply chain utilises today.

Q17 **Baroness Neville-Jones:** Minister, could I turn to the question of the Treasury as a national security department? You said earlier that the Treasury looked after economic security. I want to take a specific area. In the first half of this year, £754 million was stolen from UK bank customers through scams of one kind or another. That is only one part of the picture of fraud, which is now a very big issue indeed, and growing. How do you think the Treasury is doing as an economic security department? How do you rate your own priorities as a department against the whole issue of harm? It is a question of what criteria you are operating on. This is something that has reached the general public. It is not something people are unaware of.

Simon Clarke: Indeed.

Baroness Neville-Jones: What priority are you giving it? How well organised are you as a department? What are you going to do about it? It seems to me that this is one, quite big, unanswered area, in both institutions and spending.

Simon Clarke: It is an enormous challenge. It will only grow as the years pass, because the shift to online banking and online retail is not a trend that is going to reverse. Of course, the pandemic has accelerated some of our reliance on those marketplaces. That poses material challenges.

In July 2019, we published our economic crime plan, which sets out 52 actions that the UK is taking to tackle economic crime and to prioritise risk areas in the gaps identified by the Financial Action Task Force assessment. Those are wide-ranging. They include reform of the suspicious activity reporting regime and, crucially, improving the supervision of anti-money laundering compliance in the regulated sector.

How are we doing as a nation? In 2018, our anti-money laundering regime was reviewed by FATF, the Financial Action Task Force. We

achieved the best ratings of any country assessed so far in this round of evaluations, outperforming all other states.

Baroness Neville-Jones: I am not sure how much that means, to be frank.

Simon Clarke: Obviously, these are all relative things. We are confident that we are in a position where we have a very robust anti-money laundering regime. That is very important.

We are continuing to tackle illicit finance across the piece. We are working to strengthen the capabilities of key bodies such as Companies House, which received an important settlement as part of the SR. We continue to develop our legislative base as well. The economic crime anti-money laundering levy is coming in through the Finance Bill. We will use secondary legislation next year to formalise any outstanding elements of our policy there.

There is ongoing work. We continue to consider new challenges such as cryptocurrency and ransomware. All these things are at the heart of the Treasury's thinking and are very closely informed by our wider conversations with the Home Office. You really cannot be too careful in this space. We want to reassure the public that the UK is a safe place for online retail, because it genuinely is, but people need to exercise care. We need to support all forms of government—including, as I said earlier, local government, where we need to be equally clear that there is a genuine risk to the integrity of data—to make sure that we are playing our full part in supporting the wider population and business to deal with this challenge, because it will not go away.

Baroness Neville-Jones: You did not mention the police in your answer.

Simon Clarke: I alluded to the Home Office and the work that it is doing. Obviously, we have the wider shift in resources for the police. The 20,000 extra officers by 2022-23 are an important part of that process.

Baroness Neville-Jones: You express confidence in the structures and what you are doing. I do a certain amount of work in this area. Frankly, I think we are in the foothills of our ability to cope with illegal financial activity, particularly fraud. There is a long way to go.

Simon Clarke: I would be very happy to continue a dialogue on this theme after the evidence session. I do not think anybody is saying that we are always in a position to counter every conceivable threat. We are doing our utmost to make sure that our capabilities match the scale of the challenge, but we fully recognise that, between state actors and criminals, we are faced with a variety of threats. Those continue to take new forms and to intensify. It is a genuinely open offer. I know that the Economic Secretary to the Treasury would particularly welcome that.

Q18 **Baroness Neville-Jones:** I would welcome that. Thank you.

Can I ask about a slightly different aspect? It also affects our reputation

as a clean country to operate and invest in, and the effectiveness of our foreign policy. There are still large flows of illicit finance coming into the City. Do you worry about that? As seen from outside government, if we do not get that under control, we send signals to Moscow and other Governments about our effectiveness, sincerity and general reputation as a serious player on the security front and in dealing with other aspects of their behaviour, countering their cyberattacks and using sanctions policy against Ukraine.

I am making a more general point. It seems to me that the effectiveness and relevance of our activities on the economic front, which are extremely relevant to the economic security and the prosperity of the country, also bleed into our reputation as a serious and effective foreign policy actor.

Simon Clarke: I quite agree. Obviously, we have the Bribery Act and the wider legislation that we have enacted in that space. At the Treasury, we have the sanctions and illicit finance team, which works closely to monitor flows of money and, in particular, to uphold our wider sanctions regime, to which you alluded a moment ago. In that regard, we have put in place, through the Magnitsky-style regime that the former Foreign Secretary took through Parliament, a very effective signal that we will not allow people to enjoy ill-gotten gains with impunity in this country and that we will track down and stop those flows.

Is it an ongoing piece of work? Of course it is. Does it require intensive resourcing? Yes, it does. FCDO is the lead department for our wider sanctions policy, and the Home Office will take the lead on illegal flows of money coming in for other reasons. We are confident that they are well resourced to do that. Again, in so far as there are specific issues to which you want to draw attention, I am happy to carry on that conversation.

Baroness Neville-Jones: This is a classic area of cross-departmental functioning. They are different aspects of policy, but they need to cohere, to use your word from earlier. Are you happy with the functioning of the NSM in this area? Do you reckon that it is a really up-and-running bit of machinery?

Simon Clarke: We are in the process of developing our economic security strategy, of which this is one dimension. The Chancellor would chair meetings of the NSM that pertained to these issues. He might, for example, invite the Secretary of State for BEIS to join such meetings to make sure that that department's voice was captured.

It is absolutely vital that this is seen as part of our wider work in the space of the national security strategy. We need to show the perpetrators of crimes overseas that they cannot then enjoy the proceeds of those crimes in this country. The UK is a hub of global finance, so we are particularly exposed to that risk. It is therefore doubly incumbent on us to make sure that our regimes are very robust. Everyone in the Treasury accepts that that is our key strand in wider security. It is the one that we own most directly. Obviously we have a wider role in underpinning and

evaluating performance against the totality of the strategy, but this is very much an equity that we own directly, and we need to step up.

Baroness Neville-Jones: I am glad to hear that you recognise that.

Q19 **Lord Brennan:** I want to ask a question about the security aspects of modern vehicles for finance, instead of simple money: digital currency, stable coinage—the first supported by states, the second by business and commerce—and cryptocurrency, which is not really supported by anything. What is the Treasury policy on the seriousness of the risk that these three forms of money pose for the future? What is proposed by way of control and regulation of these sectors in order to safeguard the security of the country, as well as its citizens?

Simon Clarke: This is a very challenging area. Cryptocurrencies have the potential to be a very successful part of a modern economy, but they represent challenges for regulators. If not regulated properly, they are a vulnerability in this space.

At the moment, we are working with the FCA to make sure that we can register crypto-asset firms for anti-money laundering supervision. This is an important piece of work. The FCA will be required to assess whether a firm and its officers, managers or beneficial owners are fit and proper with regard to the risk of money laundering or terrorist financing. It is the latest in our programme of work to try to make sure that this is a regulated space and that we can assure ourselves that we are protecting the integrity of our wider financial services from new challenges.

There is no question but that it is a double-edged sword. We are very conscious of that. The Economic Secretary to the Treasury does a great deal of work in this area. It is one where, as a department, we need to understand the very latest in what is happening. I do not know whether Cat wishes to add anything specific. It sits somewhat outside my direct portfolio of work, but it is certainly a risk of which we are aware, and where we are resourcing the relevant agencies appropriately to make sure that they can expand their activities.

Catherine Little: It is outside my direct policy area as well. However, I know that colleagues who work directly with financial services and the regulators are very seized of the risks. It might be helpful for us to provide a bit more information through correspondence after this hearing.

Lord Brennan: Yes, it would.

The Chair: That would definitely be helpful. Thank you very much. I think we have covered most things. If there is anything that has slipped through the cracks, I hope that you will not mind if we write to you afterwards.

Simon Clarke: Of course.

The Chair: Thank you both for coming and giving evidence to us this afternoon. It was much appreciated.