House of Commons

Committee of Public Accounts

# The Shareholder Executive and Public Sector Businesses

## Forty-second Report of Session 2006–07

*Report, together with formal minutes, oral and written evidence*

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## The Committee of Public Accounts

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# Summary

The mission of the Shareholder Executive ("the Executive") is to act as an effective owner of businesses owned or part-owned by government. It was established in 2003 and is now an operational group within the Department of Trade and Industry. Its portfolio covers 27 businesses with a combined turnover of £21 billion, including businesses that are responsible for providing critical public services, such as air traffic services over national airspace. Whilst it is crucial that these public policy objectives are achieved cost effectively, the government, as shareholder, also has an important interest in protecting or enhancing value so that the businesses provide a satisfactory return on the public money invested in them.

It has delivered value for the taxpayer by putting a framework in place under which clear priorities are set for the businesses; performance is monitored; and management is held to account for delivery. The Executive's success is dependent on it having high calibre staff and the freedom to provide clear and independent advice on shareholder matters. It employs staff with a good mix of public and private sector skills and works within civil service pay limits. The Executive needs to market its services to publicly-owned businesses outside the Executive's portfolio because they are not required to use its services as the government's shareholder.

The Executive can hold management to account for the performance of businesses by using several "shareholder levers", which include: selecting the Chair and Board members; approving transparent business objectives that respect policy constraints; and agreeing finance for investment. The ability to access financing for investments is critical to the success of a commercial business. As long as a business is within the public sector, however, its investment needs are subject to fiscal policy constraints and compete with departmental and government-wide spending priorities. Because of these constraints, decisions on whether or not to invest in a business are not considered on the basis of commercial objectives alone, as in the case of private sector businesses, so the scope for using this important shareholder lever is reduced.

The Executive looks likely to meet its target of increasing the value of six businesses by £1 billion by 2007. This target is not, however, connected to the Executive's own performance, and is based on a single measure without any reference to other measures such as market valuations of the businesses.

On the basis of a report by the Comptroller and Auditor General,[1] the Committee examined the Department of Trade and Industry and the Shareholder Executive on the management of government's shareholdings and on the barriers to more effective performance.

1 C&AG's Report, *The Shareholder Executive and Public Sector Businesses*, HC (2006–07) 255

# Conclusions and recommendations

1. **Reconciling public policy with shareholder value objectives can be difficult because the cost of meeting the former can have a negative impact on the latter.** Currently, the Executive reports to officials in the Department of Trade and Industry and the Stakeholder Group who have policy interests in the Executive's businesses. The Department is setting up a Board to provide direction and accountability to which the Executive will report. The Board will need to articulate what it expects of the Executive, and how it proposes to assess the Executive's performance.

2. **The Executive lacks a mandatory role as the government's shareholder, but is dependent on the voluntary cooperation of the businesses and their sponsor Departments.** There should be a presumption that government businesses come within the Executive's portfolio and any exclusions should be specifically authorised by the Treasury.

3. **The Executive's advice is not being harnessed effectively across government.** Transactions which affect departments' ownership interests are continuing to take place without any input from the Executive. The Executive should market its services comprehensively and seek to be more visible across government as a whole.

4. **The Executive's effectiveness in its dealings with businesses is constrained by its limited ability to provide finance.** Investment by departments in their public businesses is subject to public spending constraints and competes with other priorities. But the availability of finance for investment can have a major impact on the value of a business. The financing of such investment cases could be assessed more consistently by giving the Executive an explicit responsibility for advising sponsor departments on the investment needs of their businesses.

5. **The target for increasing the value of six of its 27 businesses by £1 billion is not an adequate test of the Executive's effectiveness.** One or two large businesses, potentially affected by market conditions, can influence whether the Executive meets its target, regardless of the Executive's underlying performance. Its performance management regime needs to include wider measures that are based on the results of individual businesses, alongside an aggregated portfolio-level target.

6. **The Executive operates within departmental pay and grading limits which may inhibit recruitment of appropriately skilled staff.** The quality of the Executive's staff is key to its effectiveness. The Executive needs sufficient pay flexibility to continue to recruit high calibre staff in a market for commercially-related skills.

7. **The Executive has a range of responsibilities for the postal services industry, which extend beyond shareholder value issues.** The Executive's current location in the DTI means that, in addition to the shareholding in Royal Mail, it is responsible for DTI policy on the postal market and the Post Office network, and oversight of the market regulator and consumer watchdog. This arrangement could inhibit the Executive from articulating the case for enhancing shareholder value in Royal Mail.

The Department should identify options for relieving the Executive of responsibility for Royal Mail policy and oversight of PostWatch and PostComm.

8. **Between 2004 and 2006, the dividends paid have increased from £24.3 million to £45.3 million, while operating profits have risen from £1.1 billion to £3.7 billion.** The Executive should set business-level dividend targets, which take into account the risks faced by businesses, the capital invested in them and a credible estimate of future investment needs, so that over time a greater flow of dividends could be returned to the taxpayer.

9. **The Executive does not undertake valuations of all of the businesses in its portfolio.** Although it is not cost-effective to conduct valuations of all of its businesses on an annual basis, the Executive should systematically undertake valuations of the businesses in its portfolio every few years and use these to highlight the impact of policy on shareholder value.

# 1 The Status, Location and Profile of the Shareholder Executive

1. The Shareholder Executive ("the Executive"), an operational group within the Department of Trade and Industry ("the Department"), has a government-wide mission to be an effective shareholder of public sector businesses owned or part-owned by government.[2] It is responsible for the management of shareholdings in 17 businesses either on behalf of (in an executive capacity) or in co-operation with (in a "joint leadership" role) government departments. It advises departments on a further 10 businesses.[3] In 2005, these 27 businesses had a combined turnover of £21.45 billion, and had an estimated value in excess of £16.6 billion (**Figure 1**). It also advises departments on issues relating to corporate finance and assistance to non-government owned businesses.[4]

**Figure 1: The Turnover and Value of the Executive's Businesses**

| Business | Government ownership[5] | Type of Business (Legal Form) | Shareholding Department | Role of Shareholder Executive | Turnover 2005/06 (£m) | Valuation Range as of 30th June 2006 (£m) | |
|---|---|---|---|---|---|---|---|
| | | | | | | **Low** | **High** |
| Actis | 40%[6] | Limited Liability Partnership | DfID | Executive | 48 | 182 | 535 |
| BNFL | 100% | Companies Act Company | DTI | Executive | 1417 | 2322 | 2823 |
| British Energy | 0-65%[7] | Companies Act Company | DTI | Executive | 2593 | 4453 | 4453 |
| CDC | 100% | Companies Act Company | DfID | Advisory | 387 | 2617 | 2617 |
| ECGD | 100% | Government Department and Pilot Trading Fund | DTI | Executive | 88 | 1923 | 2057 |
| Northern Ireland Water Service | 100% | On Vote Executive Agency | Dept Regional Development, NI | Advisory | 41 | -463 | -27 |

2 C&AG's Report, paras 2.19

3 C&AG's Report, para 1.4

4 C&AG's Report, para 1.9

5 Source: Shareholder Executive Annual Report, 2005–06

6 Until 2009, H.M. Government retains an 80% economic interest in the LLP.

7 As of June 2006, through the Nuclear Liabilities Fund, the Government had a cash sweep of 65% of the annual adjusted free cash flow of British Energy, which was convertible into shares up to 65% of the equity of the company.

| **Business (continued)** | **Government ownership[8]** | **Type of Business (Legal Form)** | **Shareholding Department** | **Role of Shareholder Executive** | **Turnover 2005/06 (£m)** | **Valuation Range as of 30 June 2006 (£m)** | |
|---|---|---|---|---|---|---|---|
| QinetiQ | 19.3% | Companies Act Company | MoD | Joint leadership | 1052 | 1190 | 1190 |
| Royal Mail | 100% | Companies Act Company | DTI | Executive | 9056 | 1029 | 3184 |
| Scottish Water | 100% | Statutory Corporation | Scottish Executive | Advisory | 1019 | 2259 | 2994 |
| UK Atomic Energy Authority | 100% | Statutory Corporation | DTI | Executive | 361 | 172 | 185 |
| **Service Businesses [9]** | | | | | | | |
| ABRO | 100% | Executive Agency & Trading Fund | MoD | Joint leadership | 137 | | |
| Channel 4 | 100% | Statutory Corporation | DCMS | Advisory | 894 | | |
| DARA | 100% | Executive Agency & Trading Fund | MoD | Joint leadership | 166 | | |
| Dstl | 100% | Executive Agency & Trading Fund | MoD | Joint leadership | 353 | | |
| NATS | 48.9% | Companies Act Company | DfT | Joint leadership | 687 | | |
| New Covent Garden Market Authority | 100% | Statutory Corporation | DEFRA | Advisory | 11 | | |
| Ordnance Survey | 100% | Government Department and Trading Fund | DCLG | Advisory | 118 | | |
| Royal Mint | 100% | Government Department and Trading Fund | HMT | Executive | 115 | | |

8 Source: *Shareholder Executive Annual Report*, 2005–06

9 These valuations are provided in aggregate owing to reasons of commercial confidentiality surrounding the Tote figure.

| Business (continued) | Government ownership[10] | Type of Business (Legal Form) | Shareholding Department | Role of Shareholder Executive | Turnover 2005/06 (£m) | Valuation Range as of 30 June 2006 (£m) | |
|---|---|---|---|---|---|---|---|
| Tote | 100% | Statutory Corporation | DCMS | Advisory | 2208 | | |
| Workings Links | 33.3% | Companies Act Company | DWP | Executive | 55 | | |
| | | | Service businesses valuation range | | | 962 | 1238 |
| | | | **Valuation range for 20 businesses** | | | **16646** | **21249** |
| **Businesses for which values were not available** | | | | | | | |
| British Waterways | 100% | Statutory Corporation | DEFRA | Advisory | 191 | n/a | n/a |
| Fire Service College | 100% | Executive Agency & Trading Fund | DCLG | Advisory | 22 | n/a | n/a |
| Forensic Science Service | 100% | Companies Act Company | HO | Joint leadership | 158 | n/a | n/a |
| Met Office | 100% | Executive Agency & Trading Fund | MoD | Joint leadership | 170 | n/a | n/a |
| Partnerships UK | 44.6% (HM Treasury), 4.4% (Scottish Ministers) | Companies Act Company | HMT | Executive | 16 | n/a | n/a |
| QE II Conference Centre | 100% | Trading Fund | DCLG | Advisory | 11 | n/a | n/a |
| UK Hydrographic Office | 100% | Trading Fund | MoD | Joint leadership | 75 | n/a | n/a |
| **Total Turnover** | | | | | **21449** | | |

10 Source: *Shareholder Executive Annual Report*, 2005–06

**The data and methodology used to generate the valuations above were produced by the National Audit Office and their advisors. Neither the valuations nor the methodology have been verified nor endorsed by the Shareholder Executive nor any of the businesses concerned. The Shareholder Executive bears no liability to any party for the use or interpretation of this data.**

As stated in the NAO's Report 'The Shareholder Executive and Public Sector Business', the NAO commissioned advisors to develop valuation ranges of the Shareholder Executive's businesses at 30 June 2006 using a multiples methodology. The valuation ranges exclude liabilities that the advisors considered equivalent to debt obligations, such as pension liabilities and significant operating leases. These valuations are broad brush, based on multiples analysis using comparator businesses which, in a number of cases, are limited. The figures are therefore not an automatic indication of the market value of each business.

In carrying out the valuation exercise, the advisors identified a number of close comparators for seven of the businesses and moderate comparators for a further nine businesses. Two businesses have stock exchange listings, providing market valuations. Finally, seven businesses (marked 'n/a' above) did not have appropriate listed comparators.

2. Since its establishment in 2003, the Executive has improved the way in which government shareholdings are managed. Its approach is based on highlighting the importance of shareholder issues within Government, recruiting staff with commercial and financial skills from the private sector and closely scrutinising the performance of public sector businesses.[11] Its most notable success came from its role in the 2006 sale of Westinghouse which in part led to the taxpayer receiving an additional £2 billion more than was anticipated.[12] But there are a number of ways in which the Executive's status and profile in government could be strengthened so that it is in a position to provide independent advice on shareholder issues.

3. The Executive was initially set up in the Cabinet Office but was moved to the DTI as a condition of it being given executive responsibility for the Department's businesses. Whilst this move resulted in an expanded remit, the Executive gave up its central department location and relinquished its independence. It is now located within a Department which has policy interests in some of the largest—and most problematic—businesses in public sector ownership, and which need not heed the Executive's advice on shareholder matters if it conflicts with departmental policy objectives.[13] Greater independence would also enable the Executive to undertake other activity that would make use of its commercial expertise, such as advising government on how best to keep the National Asset Register up-to-date to make it a useful management tool.[14]

4. The Executive reports to a Stakeholder Group, consisting of senior officials from a few of the major shareholding departments, for the delivery of its overall objectives (**Figure 2**). The representatives on this body are not independent of policy considerations, making it

11 C&AG's Report, paras 2.6–2.13.

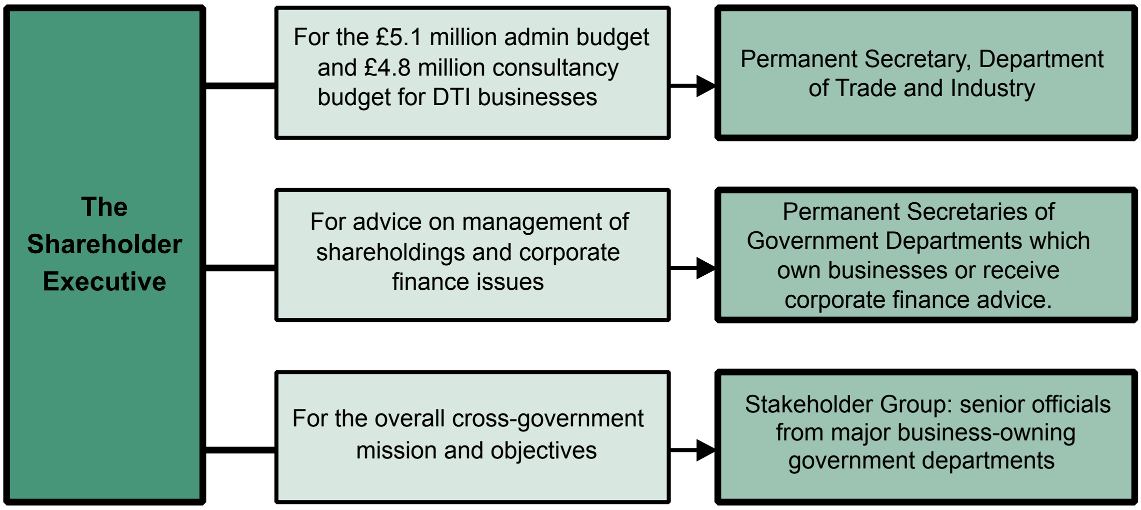
12 Qq 33–34, C&AG's Report, case study, p.19

13 Qq 9, 11–12, 113, 120–121

14 Qq 39–40

difficult for the Group to give the Executive strategic guidance and to hold it to account for its performance as a shareholder. The Department intends to appoint an external part-time Chairman and three to four directors to address this deficiency.[15]

**Figure 2: The Shareholder Executive's accountability**




*Source: National Audit Office*

5. There is a lack of clarity about the role of the Executive in respect of the postal services industry. The Department said that in the run up to the announcement to Parliament on the postal network on 14th December 2006,[16] the Executive advised the Secretary of State for Trade and Industry on the government's shareholder interests alone, with policy advice coming from other departments. Yet the Executive has conflicting responsibilities for the postal industry, which include DTI policy for the postal network and oversight of the government's shareholding in the Royal Mail.[17]

6. The Executive has recruited public and private sector staff with a mix of skills and expertise so that it can act as an intelligent and effective shareholder.[18] At the senior level, 70% of the Executive's Directors are external recruits and are employed within existing civil service pay bands.[19] Those recruited externally generally accept lower rates of pay in the government service than they could command in the financial services sector. The Executive believes that the remuneration it is able to offer appears sufficient to attract the right calibre of staff. It nevertheless recognises that it needs to keep pay under review because its success is dependent on having sufficiently skilled staff.[20]

7. External recruits tend to be employed on fixed-term contracts or are seconded from a private company. The resulting turnover among staff, particularly at the senior level, has the advantage of providing scope for the Executive to bring in people with up-to-date

15 Q 35; C&AG's Report, para 3.9

16 HC Deb, 14 Dec 2006, Col 1026–27

17 Qq 58, 116-117

18 C&AG's Report, para 2.11

19 Qq 68–72

20 Qq 24–25, 38, 110–112, 122–125

knowledge and experience. On the other hand, there is a risk that corporate knowledge and experience could be lost, and relationships with businesses need to be re-built following staff departures.[21]

8. The Executive has a government-wide remit but has no mandate to bring businesses into its portfolio, relying instead on marketing the services it has to offer to Departments. There is uncertainty about which public sector businesses should fall within its portfolio and currently the Executive is unable to explain all of the omissions from its portfolio which in total had a combined turnover well in excess of £4 billion in 2004–05.[22]

9. A number of government departments are involved in transactions with the private sector which result in the government taking on ownership interests. In carrying out these transactions, a department has to purchase advice on commercial and financing issues to ensure that the taxpayer gets the best value from the deal. The Executive provides its corporate finance and other services as a free good to government[23] and is able to demonstrate that it has brought about savings for the taxpayer.[24] The Committee has taken evidence at a recent session[25] on a case where the Executive could have helped with the creation of joint venture involving the Department of Health.[26] The Department spent over £1.7 million on external advice but was unable to demonstrate that the joint venture was the best structure to meet its needs, or that it represented good value for money. Whilst the Executive might not be able to advise on every case, it could help departments by negotiating tighter terms of engagement with professional advisors.[27]

21 Q110; C&AG's Report, paras 3.14–3.15, Figure 13

22 Qq 10, 23, 104–106

23 Q 51

24 C&AG's Report, para 2.14

25 Committee of Public Accounts, Fortieth Report of Session 2006-07, *Dr Foster Intelligence: A joint venture between the Information Centre and Dr Foster LLP*, HC 368

26 Qq 10, 23

27 C&AG's Report, paras 2.14, 2.22

# 2 Managing Public Sector Businesses for Value

10. Controlling shareholders use a number of "shareholder levers" to ensure that their businesses will deliver agreed objectives. These levers include setting clear business objectives, approving management remuneration, monitoring performance and holding management to account for performance. One of the improvements brought about by the Executive is that these levers are applied in a more timely manner, whereas in the past public sector businesses were allowed to make poor investment decisions without sufficient critical challenge, or to record several years' poor performance without consequences.[28]

11. The Executive has the ability to replace management, particularly when it is failing to deliver business objectives, and also has a role in approving management remuneration, on which it can take external advice to ensure that the correct reward structures are in place.[29] These levers mean that management can be rewarded for good, and removed for poor, performance. The Executive has also strengthened the role of non-Executive Directors, particularly for the Trading Funds. Non-Executive Directors bring a range of skills to the Boards of these businesses, provide greater management challenge and warn the Executive when there are problems. The Executive currently provides details of management changes it has initiated in its annual report.[30]

12. A crucial lever not available to the Executive, but one which is available to equivalent bodies in the private sector, is the ability to arrange for the provision of finance to businesses where there is a robust case for investment.[31] Having this ability provides shareholders with additional influence on management and overall business strategy. Under the current system, however, such financing comes from departments or the National Loans Fund[32] and is counted against Departmental Expenditure Limits; senior officials must weigh up the need for investment in businesses against other public spending priorities. Public spending priorities will sometimes take precedence over public sector business investment, with a resulting lack of finance for businesses when needed, which is aggravated by their lack of direct access to capital markets.[33]

13. The Executive has negotiated a variety of relationships with government departments for working with businesses (**Figure 1**), which offer a pragmatic solution when a department is unwilling to delegate full responsibility to an external body for shareholder issues. Under the joint working arrangement with, for example, the Ministry of Defence (MoD), staff at the Executive work closely with the MoD's Directorate of Business Delivery and have a seat on the Ministerial ownership council.

28 C&AG's Report, Figure 3, paras 1.15, 2.8

29 Q 49–50

30 Qq 13, 16, 23; C&AG's Report, para 2.7

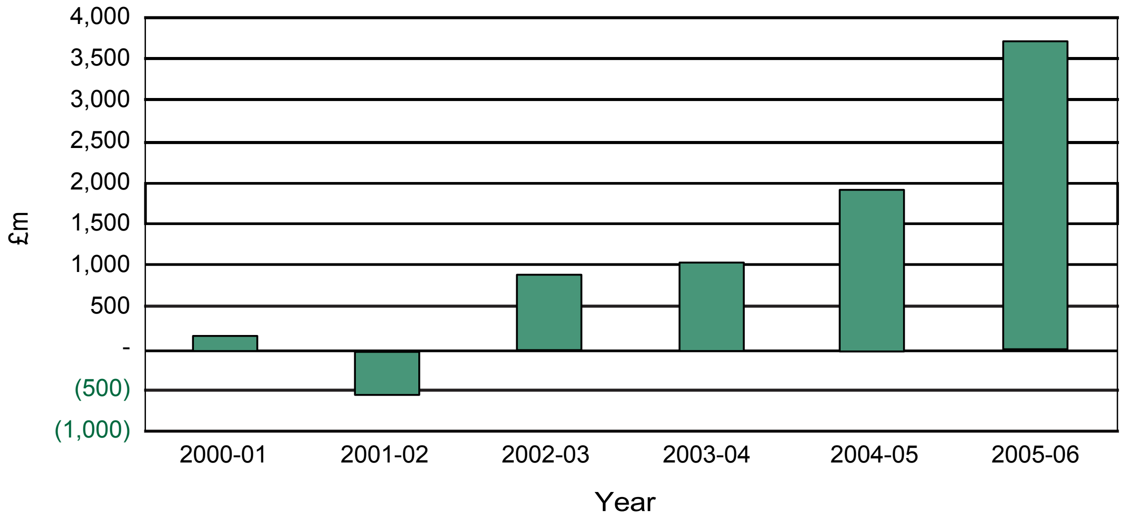
31 Q 8; C&AG's Report, para 2.24

32 C&AG's Report, para 2.25

33 Q 114

14. Whilst the Executive has improved the government's approach to managing shareholdings, the good performance of some of its businesses in recent years (**Figure 3**) could be ascribed partly to favourable market conditions. The Executive's own internal measures point to an increase in the number of businesses with balance sheet risks, and to have strategies in place that will enhance shareholder value.[34] Eleven of the businesses in its portfolio made losses at some point in the last three years (**Figure 4**), and a number of its largest businesses face strategic challenges in the near future.[35] Problems often arise because businesses are not adequately compensated for delivering policy objectives or do not have access to investment, or because the shareholder levers are not used in a timely manner.

**Figure 3: Total Operating Profits of the Executive's businesses 2000-2006**




34 C&AG's Report, Appendix 5, Figure 21

35 Q 20; C&AG's Report, para 3.2–3.3

**Figure 4: Loss Making Businesses 2003 -2006**

| £m Operating profit / (loss) | 2003/4 | 2004/5 | 2005/6 |
|---|---|---|---|
| ABRO | 13.4 | (4.0) | 6.2 |
| BNFL | (351.0) | (203.0) | 65.0 |
| British Waterways | (3.8) | (7.4) | 0.4 |
| DARA | 10.2 | 9.3 | (3.2) |
| Fire Service College | (1.5) | (0.2) | (1.7) |
| Met Office | (9.2) | 9.5 | 13.4 |
| Northern Ireland Water Service | (179.0) | (209.5) | (236.6) |
| PartnershipsUK | 1.9 | (0.4) | 1.5 |
| Royal Mint | 2.1 | (2.0) | (0) |
| UK Atomic Energy Authority | 0.8 | (1.8) | 0.4 |
| Working Links | 6.4 | (1.4) | 3.6 |

**Notes:**
1. As stated in the Shareholder Executive Annual Report 2005–06 (Annex A), the Shareholder Executive only advises on specific issues in relation to the Fire Service College and Northern Ireland Water Service. It does not therefore analyse the performance of these businesses in the Annual Report.

2. The figures for Northern Ireland Water Service show the net deficit on operations. This excludes the funding provided through money voted by Parliament, which accounts for the bulk of the agency's income, and will continue to do so until the introduction of charging in the context of the water reform programme.

*Source: Shareholder Executive*

# 3 Performance Management

15. The Executive has set itself an objective to increase the value of six businesses by £1 billion between 2004 and 2007. In 2006, the value of these businesses had increased by £2.6 billion, although the Executive anticipated that some of this increase might be reversed in 2007.[36] This target has focused attention on shareholder value but is not an adequate measure of the improvement that the Executive has made to the management of government shareholdings.[37] The performance of one or two large businesses can have a decisive influence over whether or not it meets its target—as the current level of achievement demonstrates.[38] The Royal Mail's value increase alone was over £1 billion and the Royal Mail and BNFL together accounted for 70% of the £2.6 billion increase achieved. A further two of the businesses covered by the target (NATS and CDC) benefited from benevolent market conditions. Business-level performance targets would provide a better means of measuring performance by measuring the proportion of targets which are achieved across the businesses in the Executive's portfolio.[39]

16. The Executive uses an Economic Profit methodology to track changes in value to measure performance against its £1 billion target. This methodology as applied by the Executive, however, is not able to provide an absolute value of the public sector businesses in the Executive's portfolio[40] and so it does not know what each business in its portfolio is worth. Equivalent shareholders in the private sector undertake periodic valuations of the businesses in which they have an economic interest and this gives them an idea of where their businesses stand in the market place and enables them to make decisions on what to do with their assets.[41]

17. An important indication of the Executive's performance is the value public sector businesses return to the taxpayer in the form of dividends. Dividends paid to departments increased from £24.3 million in 2003–04 to £45.3 million in 2005–06, but at the same time operating profits increased from £1.1 billion to its current level of £3.7 billion, resulting in a fall in dividends as a percentage of profits (**Figure 5**).[42] The Executive does not currently set business-level dividend targets, but instead has a broadly stated aspiration to achieve a progressive return to dividend paying.[43] Even though some of the businesses contributing to this increase in profits are not required to pay dividends, the Executive recognises that there is more it could do to ensure that the other businesses are not keeping cash on their balance sheets.[44] Businesses have an incentive not to pay dividends to departments because under the current system for obtaining finance for investment, there is a risk that future

36 Q 5; C&AG's Report, paras 3.2, 3.7

37 Q 5–7, 64; C&AG's Report, paras 2.3–2.4, 3.6–7

38 C&AG's Report, Figure 12

39 Q 128; C&AG's Report, Figure 8, para 3.7

40 Qq 77–78, 95–97

41 Qq 100–101

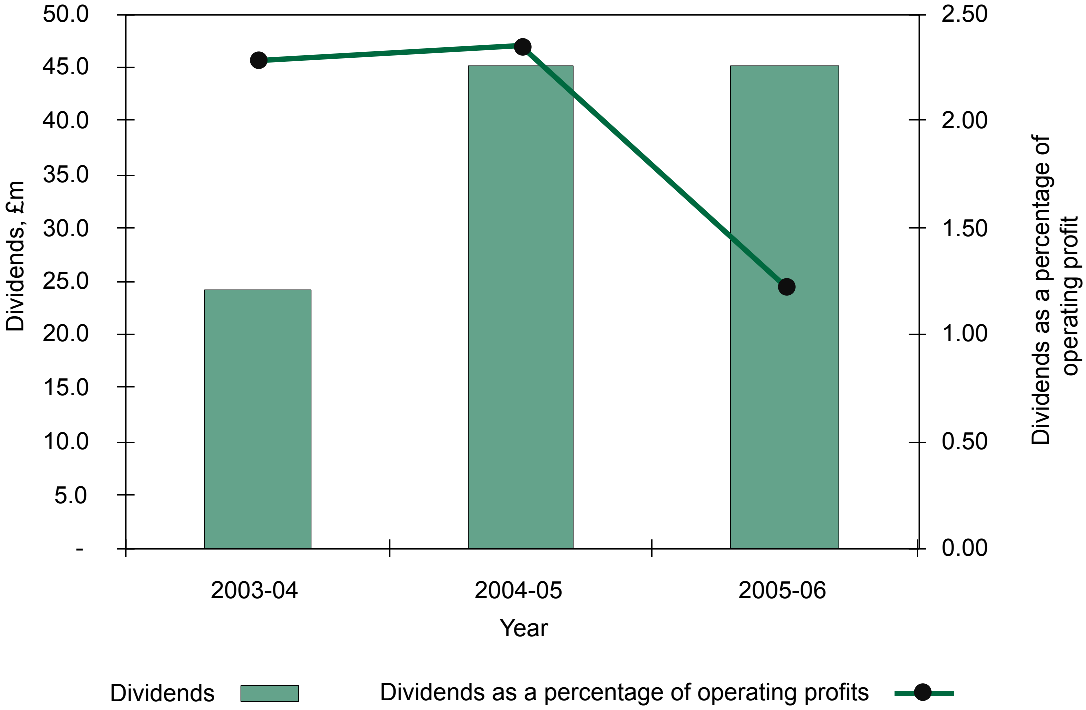
42 Qq 19, 22

43 C&AG's Report, para 2.1

44 Qq 19, 115

financing needs will not be met.[45] The cost of any increased access to finance should therefore be partly offset by an increased dividend flowback.

**Figure 5: Dividends Paid and As a Percentage of Operating Profit, 2003-2006**




*Source: C&AG's Report*

45 C&AG's Report, para 2.27

# Formal minutes

## Wednesday 27 June 2007

Members present:

Mr Edward Leigh, in the Chair

Mr Richard Bacon
Mr David Curry
Mr Ian Davidson
Mr Philip Dunne
Dr John Pugh
Mr Alan Williams
Mr Iain Wright

**Draft Report**

Draft Report (The Shareholder Executive and Public Sector Businesses), proposed by the Chairman, brought up and read.

*Ordered*, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 17 read and agreed to.

Conclusions and recommendations read and agreed to.

Summary read and agreed to.

*Resolved*, That the Report be the Forty-second Report of the Committee to the House.

*Ordered*, That the Chairman make the Report to the House.

*Ordered*, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Monday 9 July at 4.30pm

# Witnesses


**Monday 19 March 2007** *Page*

**Sir Brian Bender**, Permanent Secretary, Department of Trade and Industry, **Martin Bryant**, Chief Executive, and **Peter Schofield**, Director, The Shareholder Executive. Ev 1


# List of written evidence


Department of Trade and Industry Ev 16

# List of Reports from the Committee of Public Accounts Session 2006–07

| | | |
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| Second Report | Improving literacy and numeracy in schools (Northern Ireland) | HC 108 (Cm 7035) |
| Third Report | Collections Management in the National Museums and Galleries of Northern Ireland | HC 109 (Cm 7035) |
| Fourth Report | Gas distribution networks: Ofgem's role in their sale, restructuring and future regulation | HC 110 (Cm 7019) |
| Fifth Report | Postcomm and the quality of mail services | HC 111 (Cm 7018) |
| Sixth Report | Gaining and retaining a job: the Department for Work and Pensions support for disabled people | HC 112 (Cm 7019) |
| Seventh Report | Department for Work and Pensions: Using leaflets to communicate with the public about services and entitlements | HC 133 (Cm 7020) |
| Eighth Report | Tackling Child Obesity—First Steps | HC 157 (Cm 7020) |
| Ninth Report | The Paddington Health Campus Scheme | HC 244 (Cm 7076) |
| Tenth Report | Fines Collection | HC 245 (Cm 7020) |
| Eleventh Report | Supporting Small Business | HC 262 (Cm 7076) |
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# Oral evidence

## Taken before the Committee of Public Accounts

## on Monday 19 March 2007

Members present:

Mr Edward Leigh (Chairman)

Mr Richard Bacon
Mr Philip Dunne
Helen Goodman
Mr Austin Mitchell
Mr Don Touhig
Mr Alan Williams
Mr Iain Wright

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**Sir John Bourn KCB,** Comptroller and Auditor General, and **Patricia Leahy,** Director, **Mr Tim Burr,** Deputy Comptroller and Auditor General, National Audit Office were in attendance and gave oral evidence. **Paula Diggle** and **Jeremy Pocklington,** Treasury Representatives, were in attendance**.**

**REPORT BY THE COMPTROLLER AND AUDITOR GENERAL: THE SHAREHOLDER EXECUTIVE AND PUBLIC SECTOR BUSINESSES (HC 255)**

*Witnesses:* **Sir Brian Bender**, Permanent Secretary, Department of Trade and Industry, **Martin Bryant**, Chief Executive, and **Peter Schofield**, Director, The Shareholder Executive, gave evidence.

**Q1 Chairman:** Good afternoon. Welcome to the Public Accounts Committee, where today we are examining the Comptroller and Auditor General's Report, *The Shareholder Executive and Public Sector Businesses*. We welcome back to our Committee Sir Brian Bender, Permanent Secretary at the Department of Trade and Industry, and Mr Martin Bryant, Chief Executive of the Shareholder Executive.
Mr Bryant, if Sir Brian will forgive me, I shall address most of my questions to you. I am sure you do not mind, Sir Brian, do you? I will ask you one, because I know you enjoy answering these questions. Do you accept the recommendations in the Report, Mr Bryant?
***Martin Bryant:*** There are a great many recommendations in the Report. Would you like me to talk explicitly about—

**Q2 Chairman:** Generally, to sum it up, the Report seems to think that you are doing a good job, but the National Audit Office wants to give you a higher profile and greater powers. Presumably you are pretty happy with all that, are you not?
***Martin Bryant:*** Broadly, we are happy that the NAO Report finds that we have been doing a good job so far, but we recognise that there are still areas in which we can and should improve.

**Q3 Chairman:** So the answer to my question is yes, you do accept most of the recommendations.
***Martin Bryant:*** There are some recommendations that need further work.

**Q4 Chairman:** But the essence of them—the spirit of them—you accept?
***Martin Bryant:*** The spirit of us doing a good job so far, we are pleased to accept.

**Q5 Chairman:** Fine. Although there is absolutely nothing wrong with anything that you have attempted to do, how much difference have you actually made? To illustrate this, you have this target of achieving £1 billion, but if you look at figure 12 on page 26, I wonder whether you are on course to meet your target largely because of market conditions rather than anything that you yourself are doing. Look at the massive increase, for instance, in the value of Royal Mail.
***Martin Bryant:*** The NAO Report points out that there a number of contributory factors to achieving the £1 billion target, and as of the end of last year we were at £2.6 billion.

**Chairman:** Please speak up a bit, because the people sitting behind you have to hear what you say.
***Martin Bryant:*** We were at £2.6 billion at the end of the second year. A number of our business are facing changed market circumstances. You mentioned Royal Mail, and this is the first year of working under price competition in the mail market[1]. It is by no means certain that the performance that we have achieved for year 2 will be sustained through year 3. The NAO also Reports, I think correctly, that some of the markets in which our businesses operate, most notably CDC and National Air Traffic Services,

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[1] *Note by witness*: The UK postal service market was fully liberalised on 1 January 2006 by the independent regulator—Postcomm. The decision means that, since 1 January 2006, licensed companies other than Royal Mail have been able to collect, transport and deliver all letters (for business or social mail) and charge customers for the service. Prior to this, from 1 January 2003, Postcomm had opened 30% of the postal market by allowing licensed companies to provide bulk mail services over 4,000 items in addition to consolidation services and defined activity licences.

have had some beneficial environmental effects. On the whole, we think that the measure we use is reasonable.

**Q6 Chairman:** That is not quite what I asked you. Figure 12 says that: "changes in the value of one large business (in this case Royal Mail) can have a massive influence over the performance of the portfolio as a whole". So what I am saying is that you have met the target, but is it really down to what you have achieved or because of what has been happening anyway in the marketplace?
Let us look at paragraph at 2.15, which explains a bit of that, and more importantly at figure 8 on page 20, which states: "A number of profitable businesses have competed in benign market conditions." Look, for instance, at the first column, on the emerging markets price index, and see when you were established and what is happening to the index. That is what I am asking you about. I am not denying that what you are trying to achieve is right, but, to put it another way, had you not been there, would life would have been very different for these businesses?
***Martin Bryant:*** I agree that two of our businesses that I mentioned, CDC and NATS, have operated in attractive market conditions, as the chart illustrates. However, I would point out that the collection of businesses prior to the set-up of the Shareholder Executive made a significant net operating loss of over £2 billion and, in the period post set-up, have made an operating profit of over £5 billion. There has been a significant shift in the performance of the whole portfolio.

**Q7 Chairman:** Yes, and what difference have you made?
***Martin Bryant:*** We believe that the difference that we make is in bringing in the combination of a good framework for the management of the shareholder role—positive stuff such as clear and transparent targets, setting stretching objectives and ensuring that business plans are in place, and then monitoring performance against those things—with a group of people who have the right level of expertise to be able to work with our companies.

**Q8 Chairman:** But those are quite small powers. Let us compare your powers to those of a similar body in the private sector. Paragraph 2.24 states: "The Executive, however, lacks the full use of an important lever which is available to investment management bodies in the private sector—the ability to arrange for the provision of financing to businesses when they have a good case for it, such as an investment that will increase the value of the business over a medium to long" term.
That is pretty crucial, is it not? That is what happens in the private sector with your equivalent organisation. You do not have that power. How can you ensure that the businesses are managed for value when you do not have the power to make finance available? That is a pretty crucial shortcoming, and that is why we want to assist you in this hearing and through the publication of this Report and our own Report perhaps to get you that power so that you can make a real difference. We are trying to help you—I am being helpful.
***Sir Brian Bender:*** Part of the role involves putting clear choices to Ministers and if you were to apply that to the DTI portfolio, as you may later on, I would have misgivings about delegating a part of the DTI Departmental Expenditure Limit—one of the recommendations of this Report—to the Shareholder Executive. It seems to me to be valuable that the Secretary of State can take a decision on value for money, advised by me, across the range of DTI issues, without having it parcelled up. I think that there is a balance between getting the right policy decisions, which provide best value for money and shareholder value for the organisations, without creating, if you like, a Shareholder Executive silo that looks solely at one aspect.

**Q9 Chairman:** That leads me straight on to what I wanted to ask you anyway, Sir Brian. Have not expectations been raised too high? This executive is located within your Department. I rather thought the point of that was to be there as the voice for shareholders within the Government, but you seem to be saying, "Well, no, it's very different because they are located in our Department." Who calls the shots? Ultimately, you are telling us that, whether that body exists or not, it is the policy makers—Ministers, yourself, your Department—that own and perhaps control the executive who call the shots.
***Sir Brian Bender:*** Ministers call the shots and they will be the Ministers for whichever businesses the Shareholder Executive is advising on. If you take an example like Royal Mail and the Post Office, what is important is that the Shareholder Executive presents the options, in terms of shareholder value and policy, costs and benefits, and that Ministers make a decision on the back of that. I do not regard myself as interceding on that in the slightest. Its influence across the rest of Whitehall will depend, in part, on the quality of its advice. Certainly, having talked to one or two Permanent Secretary colleagues, it has a high reputation elsewhere in Whitehall.

**Q10 Chairman:** You say that, but we had a recent hearing on the Dr Foster joint venture and the Department had not involved you, Mr Bryant. That is a clear case of where it might have done so, but did not. There was some anecdotal evidence, as the National Audit Office team went around, that entire Departments, let alone the public, have not even heard of you, or do not want to involve you. Does that worry you?
***Martin Bryant:*** I cannot comment in detail on the Dr Foster example. I have read the transcript of the hearing. As we have found in most of our work, you need to get really into the detail to know whether we could add specific value in that area.
Regarding the general point on marketing ourselves to other parts of Government and ensuring that they are aware of what we can do, that is an area where we can improve. We have to do that in the light of the resources that we have—we are not infinitely

resourced. For the Committee's interest, I met the Department of Health subsequently to explain what skills we have.

**Q11 Chairman:** Some of your major businesses are in the DTI. Would you not be in a happier, more independent state, if you were in the Treasury, say, or the Cabinet Office?
***Martin Bryant:*** I think that our location is entirely an issue for the Prime Minister and any changes to the machinery of Government that he wishes to make.
***Chairman:*** That is obvious.
***Martin Bryant:*** But I found no evidence that our location within the DTI has inhibited us from working effectively.

**Q12 Chairman:** As an independent voice? Even though Sir Brian is sitting down the corridor from you and is, ultimately, your boss.
***Martin Bryant:*** Sir Brian's businesses are about 70%. of the turnover of our portfolio, so he is a very important constituent in our lives, but we have no evidence that we have not been able to broaden and deepen our shareholding relationships with other Departments of State. Indeed, since we have moved from a purely advisory role in the Cabinet Office into the DTI, we have picked up a large number of executive relationships with businesses and have expanded to a number of other Departments. As you know, we operate across 12 Departments of State.

**Q13 Chairman:** Figure 3 on page 12, "Controlling shareholders exert control over a business through various levers", gives us the powers that you have. It compares you to levers in the private sector. Give us some examples of where you promptly brought new management in.
***Peter Schofield:*** You are absolutely right. Getting the right management teams in to run our businesses is one of the key levers. Each year, in our annual report, we publish details of changes to the composition of boards. That has details of arrivals and departures. To give some specific examples, in the case of the Royal Mint, the Government brought in an interim management team with experience of business turnaround. That was after the business had missed its financial targets for consecutive years. In the case of the UK Hydrographic Office, a more commercial management team was brought in—not because the business itself was underperforming, but because it faced some major strategic challenges ahead. One final set of examples, if I may, is the case of trading funds, where we have improved corporate governance arrangements by appointing non-executive chairmen for the boards.

**Q14 Mr Wright:** Mr Bryant, when you were appointed in October, I have a quote from the *Financial Times*, which says: "Mr Bryant said he saw the job as steadily privatising, or moving to the market, parts of the portfolio". Could you explain that, please?
***Martin Bryant:*** As you are aware, the Chancellor has set a target for certain asset disposals, so that where businesses no longer fulfil a public policy purpose those assets can be realised. My quote to the *Financial Times* was to say that the Shareholder Executive has that capability—an example of such a disposal is the Westinghouse business—but it was not intended to say that that was our unique role, because clearly our role is to make sure that the businesses that stay in public ownership are better managed and deliver a more effective return for the shareholder.

**Q15 Mr Wright:** But do you see yourselves very much as the Government arm of the private equity business, which is that you invest to sell—you have a three to five year strategy, you add value and then you sell on? Is that how you see the Shareholder Executive?
***Martin Bryant:*** I do not see our role as that. I see our role as very much being to achieve higher value for the Government shareholder through managing their businesses better. In circumstances where the policy choice is that a business should not reside in the Government, we can help to achieve that valuation.

**Q16 Mr Wright:** Reading this Report, I was struck, very much like the Chairman, that you have had favourable market conditions, which have helped. It struck me that this was almost the equivalent of that Sarah Beeny programme, where you slap on a bit of paint and your house price goes up by £100,000, or something like that. I am struck by paragraph 2.17, where it says: "They point to an improvement in the relationships with businesses and in the approach to managing shareholdings; but they also point out that most of the businesses have yet to deliver healthy financial performance on a sustainable basis." You have improved relationship management, but in terms of the key figures—the bottom line—you have not done enough, have you?
***Martin Bryant:*** It is a truism to say that all businesses face changes in their competitive market. Our businesses are no different in that regard. Therefore, there is always more that we can do to help sustain their performance.

**Q17 Mr Wright:** Can I take you to page 42, figure 21, which has the balance sheet and risks and the balance sheet strategy? That concerns me, because it seems that the number of green rated businesses is going down. I know that there is an increase in the overall number of businesses, but green businesses are going down and the red and amber rated businesses are going up. Why is that?
***Martin Bryant:*** I would agree that our focus needs to be on moving the number of red and amber businesses up. May I just say that these are a set of internal metrics? One has to be a little bit careful in terms of the exact scoring against which the individual questions are raised. These are not published metrics, as far as discussions with our businesses are concerned.

**Q18 Mr Wright:** But I would have hoped that internal financial performance and the indicators would have meant that you were in a better position to drive the performance of the business in a healthier manner. Whether they are internal or external is largely irrelevant, is it not?
***Martin Bryant:*** Indeed. The standard part of our process is to agree a set of performance deliverables for each business and then review those on a monthly or quarterly basis with the management.

**Q19 Mr Wright:** I had a look at the annual report for 2005-06 and it says that the: "performance of the portfolio improved significantly . . . Excluding BNFL, net income for the remainder of the portfolio rose 86% to £3.3bn." That is a tremendous achievement, but the return on net operating assets had just increased from 9.4% to 23.6% and the Government share of dividends went up by a pathetic amount—it was £40.4 million. Why is that? Why are we not seeing additional dividends? You say in the annual report that: "overall the number of businesses paying dividends, and the level at which those dividends are made, remains disappointing." If you are trying to extract value for the Government, and ultimately for the taxpayer, that is not doing a very good job, is it?
***Martin Bryant:*** You are right to point out that dividends are one of the critical measures of success. In the prior period we had a dividend return of £18 million compared with the £40 million. So there has been progress. As a percentage it is lower. We have acknowledged throughout that it is an area where we need to improve our performance and agree more stretching dividend targets with our individual businesses.

**Q20 Mr Wright:** Why should we be confident? Why should this Committee have any confidence when it says in paragraph 2.16 of the Report that: "there are other reasons to be cautious about future financial performance: 10 of the businesses in the portfolio did not record operating profits in each of the last three years"? The Report goes on to say that major strategic challenges and decisions need to be made in the next few years—for example, Royal Mail needs £1.2 billion of investment to help enhance its competitive advantage. Why should we think that you will be able to perform, given what you have already said?
***Martin Bryant:*** I come back to our primary way of working, which is to establish a framework of clear objectives and then to make sure that we have rigorous and well argued business cases that give us confidence that these businesses will make appropriate improvements and returns.

**Q21 Mr Wright:** Can I go back to dividend policy? It seems to me that the Report is quite good in saying that you have very little control over dividend policy and that future investment decisions are based upon Departments' own budgets. Therefore, they are quite reluctant to expend in terms of a dividend policy. Given that we are going through the comprehensive spending review and given that that is acknowledged to be tighter than ever before, there is an inbuilt reluctance, is there not, among Departments to allow dividends to increase? What on earth can you do about that?
***Martin Bryant:*** Again, our role is to ensure that the capital tied up in our businesses is properly rewarded through paying dividends, and, as I said earlier, to set more stretching dividend targets and to work with the departmental finance teams to ensure that those are enacted.

**Q22 Mr Wright:** But given that net income has risen by 86%, we are not seeing a corresponding increase in dividend policy. It seems to be quite weak in that respect, does it not?
***Peter Schofield:*** Perhaps I can help. One of the things to bear in mind, which you will find in footnote 37 on page 22, is the fact that some of our businesses are under real constraints. There may be legal or policy constraints which affect their ability to pay out dividends rather than to reinvest in the business. That is one of the constraints we work within. But that said, you are absolutely right that we need to do more in all of this. One of our big challenges is to make sure that within the Treasury's budgeting rules, the weighted average cost of capital that is taken into account, and the targets that are set for each businesses, are set at a testing and appropriate level. When you talk about the comprehensive spending review, that is one of the things that we obviously have to make sure that we do.

**Q23 Mr Wright:** Going back to what the Chairman was saying earlier, I was also struck by figure 3 on page 12. You do seem to have an awful lot of power. You can remove poorly performing management boards. This is a similar degree of power to that of private equity firms. Yet I was also struck by paragraph 2.22, which states: "More importantly, there is no obligation on departments to involve the Executive at all with their shareholdings and other commercial activity." The Chairman has already mentioned the Department of Health. Again, why should we have any confidence that financial performance, value for the shareholder, which is in this case the taxpayer, will be provided, given that there is no obligation for Departments to consult you?
***Sir Brian Bender:*** First, the Department of Health example is slightly different, because, if I understand the situation correctly, had they used the Shareholder Executive expertise, it might have helped in what they were doing. That is slightly different from Government-owned businesses, where there is a marketing exercise that the Executive needs to do across Whitehall about what they bring to the party to try to persuade more Departments to use them, and to use the skills and expertise that they bring to bear. That is something that Mr Bryant and I have in mind in the weeks ahead.

**Q24 Mr Wright:** In my time remaining, may I talk about the personnel of the Shareholder Executive? I had a look at the annual report and I was very impressed by the experience of your staff; it seems extremely good. However, these seem to be fixed-term secondments. Given the vibrancy of the City of London at the moment and the fact that the previous chairman went to Cass and could be recruiting people, what are you doing to provide appropriate recruitment and remuneration policies to get the best possible staff at the Shareholder Executive?

***Martin Bryant:*** I can assure you that the chairman will not be recruiting from us. This is a very important part of how we regenerate our capability. We are actively recruiting at the moment; we recruit within the agreed pay scales for senior civil servants within Government, and so far we find that the intrinsic nature of the work is such that people are willing to come to us even though the pay rewards are lower than they might achieve outside.

**Q25 Mr Wright:** But the pay structure must be a barrier to recruiting the most appropriate type of staff.

***Sir Brian Bender:*** We have not yet seen that it is. If that becomes the case I certainly would want to talk to the Treasury and others about what to do about it. So far it has not been a barrier because the intrinsic interest and nature of the work has enabled some excellent people to want to come and do it. It is certainly something we do not take for granted.

**Q26 Mr Wright:** I have one final question. Mr Bryant, from 2004 to 2006 you were director of strategy at the Home Office. Should we be worried?

**Martin Bryant:** Perhaps you should ask my former colleagues at the Home Office.

**Q27 Mr Wright:** I know that I said that in a flippant and disrespectful way, for which I apologise, but ultimately, given the problems that the Home Office has had with its strategic direction, to the point where it may be split up, should we be worried?

***Martin Bryant:*** I really do not want to comment on issues in the Home Office.

***Sir Brian Bender:*** All I can say, Mr Wright, is that as part of my due diligence in recruiting for this post, we talked to various employers that Mr Bryant had had in the recent and more distant past and that encouraged us to proceed, rather than the reverse.

**Q28 Mr Touhig:** I notice, Mr Bryant, that you were managing director of Boots Opticians, so perhaps you are man of vision after all.

Looking at the Shareholder Executive relationships on page 11, I see that you have three roles: an executive role, a joint leadership role and an advisory role. I note, too, that you have a joint leadership role with the Ministry of Defence for the Hydrographic Office and the Met Office. When I was a Defence Minister I was owner of the Met Office; all the good weather was down to me and the bad weather was my predecessor's fault. We had a major problem of reorganisation and I was not conscious of your contribution to solving it.

***Peter Schofield:*** To answer the question about how the joint team works, the shareholding function within the Ministry of Defence is carried out by a team called the directorate of business delivery, which has two directors, one of whom is a Shareholder Executive person and the other is a long-term MOD official. When it comes to the division of those roles, the portfolio of MOD businesses is basically divided between the two directors. The third element of my answer is that I am a member of the owner's council. When you were a Minister I was a member of your council, so I contributed at that level. It is contributing within the MOD and on the owner's council.

**Q29 Mr Touhig:** Perhaps I did not put my question very well. I was not conscious that there was a stand-alone body of advice from this executive to me as the Minister on these matters. Was that my fault or was it the way the system operates? Sir Brian made it clear that in effect he has ownership of this executive. Is that because it is how the civil service operates?

***Sir Brian Bender:*** There are different ways of operating within different Departments. Do you want to say a little bit more about how it operates?

***Peter Schofield:*** Yes, within the MOD in particular. The way it is operated is that the advice that you would have received from the lead officials—the directorate of business delivery—would have had our input into it. That was one element of the advice. The second was having direct input into the meetings as a member of the owner's council. It was a sort of twin track.

**Q30 Mr Touhig:** You know the problems we have with the Met Office—the stop and start and out to consultation, and so on. I was not conscious of a stand-alone body of advice from this executive, which might have helped me to solve the problem.

***Peter Schofield:*** It is the nature of our joint team working. When it is joint team working, we work within the Department to give seamless advice. With the advisory remit, we step back. We are very much a separate party, and you will see separate advice. But the point of membership of the owner's council as well is that, in addition to the seamless advice, you can also get more direct advice from the shareholder executive member of the council.

**Q31 Mr Touhig:** I was also the Minister for the UK Hydrographic Office. Did you have a role in our decision to acquire that German company? It was a potential competitor—we beat the Americans, in fact, to acquiring it.

***Peter Schofield:*** Yes, SevenCs. We were very much part of that. We talked it through with the management team. The other element is that we were on the selection panel for the chairman and chief executive of the Hydrographic Office.

**Q32 Mr Touhig:** To compare the Hydrographic Office and the Met Office, the Hydrographic Office always seemed to me to be hugely commercially focused, and the Met Office less so. When we were seeking a chief executive for the Met Office, everybody was saying, "You must have a scientist" and so on, and I said, "We want a commercial man." I was right, was I not?

***Peter Schofield:*** In terms of development, the next stage is to go through the process of finding a new chief executive for the Met Office. We have an interim chief executive at the moment. But you are right. It faces commercial challenges, and the Hydrographic Office faces very large challenges as well.

**Q33 Mr Touhig:** I was impressed by the Westinghouse case study on page 19. You managed to treble the initial expected income from the auction, much against the Treasury's advice—well done there. Is that the exception or the rule?
***Sir Brian Bender:*** There were exceptional circumstances brought out in that case. I do not think that the Shareholder Executive itself had expected quite as much value as was created. That plainly had to do with the nature of the auction and of the market at the time.

**Q34 Mr Touhig:** You see that as a good example to take around Whitehall to say, "Look how much our advice helped."
***Sir Brian Bender:*** Yes. We certainly used it with the Treasury as well.

**Q35 Mr Touhig:** With the Treasury as well. That is good.
I notice that in the NAO Report, recommendation A1 on page 6 says: "The Executive's performance could be enhanced if it had independent status and funding, and flexibility to set remuneration, with attendant accountability" and so on. You do not seem enthusiastic about that, Sir Brian, and Mr Bryant seemed a little bit careful in his response, but is that not the way forward?
***Sir Brian Bender:*** One thing that has not come up yet is that we are looking to appoint a part-time chairman. A later section of the Report talks about the governance of the Shareholder Executive. At the moment, it has a stakeholder group that really consists of a few other Departments. As the NAO says, it is probably not a broad enough stakeholder group, but we are now looking to take someone with an independent investment banking-type background who can help to give that body a strategic direction that it probably would not get from someone within any one Department, wherever that Department is, and a small board of three or four other people, perhaps plus the Treasury, to give it strategic guidance. I know that does not answer your question directly—
***Mr Touhig:*** It does not at all, no.
***Sir Brian Bender:***—but that would give it more independence in terms of strategic direction than being located anywhere in Government.

**Q36 Mr Touhig:** But the Report also warns us that your secure funding is going to run out, so you are going to be at the mercy of whatever the Department wants to dish out to you in terms of financial support and sustainability. Will that not be a huge danger?
To return to the points that I made to Mr Schofield a moment ago, the most perfect view is always the one looking back, and I think that I would have benefited greatly if I had understood better that there was a substantial body of expertise—I was hugely impressed by the recruitment of the people whom you have got—to give me commercial advice where I felt that I needed it. I do not mean to take anything away from the civil service in that respect, but there are gaps, as we have seen before in this Committee, where we do not have the commercial strengths in the civil service.
***Sir Brian Bender:*** That was the rationale for creating it in the first place—to provide a core set of expertise in that sort of corporate finance and investment banking skill. On the future financing position, the guaranteed ring-fenced funding will expire, but I cannot believe that either DTI or the Treasury in particular would want that body to cease to exist.
***Mr Touhig:*** I can.
***Sir Brian Bender:*** I do not think that the Treasury would.

**Q37 Mr Touhig:** They can answer for themselves. I am not so sure about the funding. If you do not have the funding and the wherewithal, you will effectively cease to exist, will you not?
***Sir Brian Bender:*** If it doesn't have the funding it would cease to exist, but I do not think that that is likely to happen. The question is what resource it has, not whether it has resource.

**Q38 Mr Touhig:** Mr Wright touched on a number of questions about your ability to recruit people and about the levels of remuneration and so on. Do I take it that the levels of remuneration are basically civil service levels, so that you are not able to recruit the hungry young men who still want to make their mark in the world, because we are not offering the right kind of financial package and incentives?
***Martin Bryant:*** We have found that we are able to recruit a very talented array of people, and you seem impressed.
***Mr Touhig:*** Yes, I am.
***Martin Bryant:*** We have been able to do that within the banding that the senior civil service pays, and as bonus schemes allow us. As I said earlier, we are actively recruiting at the moment and are finding good candidates coming forward.

**Q39 Mr Touhig:** I was very interested in the New Zealand example that the Report shows: they have a Minister with overall responsibility for the matter. We do not seem to have that as such. Sir Brian indicated earlier that various Ministers will decide on the basis of advice from their officials whether they want to be involved in certain things, and so on. One of my hobby-horses is that we created the national asset register in 1998, but what in hell have we done with it? It seems to me that we should be managing it more effectively. Could your Executive help to advise the Government on managing the national asset register? I see the asset register as being able to exploit things and dispose of what we do not want to raise the funding for things that we do want, and to manage commercially effectively the things that we want and need to retain.

***Martin Bryant:*** It is not something that heretofore has been part of our remit. I am not sure that we have the relevant resource or expertise to be able to manage that better.

**Q40 Mr Touhig:** But it might be something that you could go into.
***Martin Bryant:*** It might be something that we could look at, yes.

**Q41 Mr Touhig:** But do you feel neglected because you do not have a particular Minister that has complete overview of everything that you do, and has a remit that runs across government, as in New Zealand?
***Martin Bryant:*** You mentioned the New Zealand model, and it is always dangerous to think that one can transplant international models across boundaries. However, what I would say is that we are clearly held to account by each of our responsible Departments, both by Ministers and senior officials there, for delivering against the businesses for which they have responsibility.

**Q42 Mr Touhig:** I can only talk about my experience, and it is really my fault, but I was not hugely conscious that you existed when I was a Defence Minister, yet I know the valuable input that you have.
***Sir Brian Bender:*** We take that lesson away as we move to the next phase, if I can use the phrase, of marketing the Shareholder Executive. As a former Minister, if you were not aware of it, in a Department where the Shareholder Executive was active, we need to take that away and think about what it means.
***Mr Touhig:*** I think it needs a higher profile.

**Q43 Chairman:** Do you accept recommendation A3 on page 6, which says: "There should be a presumption that all publicly owned businesses should fall within the remit of the Shareholder Executive. Departments should comply with this presumption or explain the rationale for exceptions to the satisfaction of the Cabinet Office and Treasury"? Do you think that there should be an opt-out rather than an opt-in?
***Sir Brian Bender:*** I am attracted by that, subject to one thing, which is a sense of prioritisation and resourcing. I forget how many publicly owned businesses there are—100 or more—and what I would not want to have happen is the Shareholder Executive's resources being deployed for dealing with things where actually there was not much value added. I personally accept the principle of doing this for the right priorities, rather than for every single publicly owned business. Doing it right across the piece for every publicly owned business, including all the trading funds and executive agencies, may, I suspect, turn out to be a misallocation of the resource expertise that the Shareholder Executive has. It is a sort of yes-ish answer to your question.

**Q44 Chairman:** Does that reply make sense to you, Sir John?
***Sir John Bourn:*** Yes.

**Q45 Mr Dunne:** The Department was set up in September 2003 after the initial sale of shares in QinetiQ. Would it be fair to say that it was in part in response to the sale of shares in QinetiQ, and the way that that was conducted, that the Government felt the need to improve its performance in this way?
***Sir Brian Bender:*** Mr Schofield was involved in the origins, so perhaps I can ask him to answer that.
***Peter Schofield:*** Yes, I would not put it down to any particular situation with QinetiQ. The discussions within the Treasury at the time were very much thinking more along the lines of the performance of the portfolio of businesses as a whole. The statistics are graphically included within the NAO Report as to how the portfolio of 18 or 20 businesses had performed in the years leading up to the creation of the executive.

**Q46 Mr Dunne:** Has your team reviewed the manner of that disposal and formed views as to whether there are lessons to be learned?
***Peter Schofield:*** The National Audit Office is doing a review at the moment.

**Q47 Mr Dunne:** I am interested in whether your Department has looked at it.
***Peter Schofield:*** I was involved in the flotation of QinetiQ last year and I have been involved in advising the Ministry of Defence on its holding in the company since I arrived in the Shareholder Executive in January 2004.

**Q48 Mr Dunne:** In that case, did you advise on the reward structure incentivisation of the senior management of QinetiQ?
***Peter Schofield:*** No, I was not involved in that.

**Q49 Mr Dunne:** Having seen what happened in that case, are you advising on incentivisation arrangements—similar or different—in relation to other assets of the Government?
***Peter Schofield:*** Absolutely. As the Report makes clear, the incentivisation of management is a very important lever for us. We make sure that we have management teams that are appropriately incentivised. That is a key lever.

**Q50 Mr Dunne:** Do you take external advice in looking at incentivisation arrangements?
***Peter Schofield:*** Yes, we do. We have a range of skills in-house, but we have in the past taken on specialist HR advice.

**Q51 Mr Dunne:** The crux of the problem that you seem to be grappling with is finding the right role which does not duplicate the roles of professional advisers, and extracting value for money for the Government from your existence. It seems from the Report that there is still some confusion over the issue. For example, paragraph 1.9 identifies that you are carrying out corporate finance advisory work for

central Government. On what basis are you doing that? Do you charge Departments or branches of agencies for your work?
***Sir Brian Bender:*** Not at the moment. One of the questions that we will want to address looking forward is whether, if the Shareholder Executive is to extend its remit beyond the core Government-owned businesses, it would be sensible for the Shareholder Executive to charge for that service. At the moment, within Government, it is a free good.

**Q52 Mr Dunne:** Are you duplicating the role of professional advisers, and are you able in part to reduce the fees that they charge?
***Sir Brian Bender:*** Yes. There is a passage somewhere in the Report that gives an estimate of what the reduction might have been.
***Peter Schofield:*** It is paragraph 2.14.

**Q53 Mr Dunne:** Where the Government remain the Shareholder and are also the client, there is an inevitable conflict of interest. You might argue that that is a policy issue rather than a value creation issue. Can you talk us through the role that you play in the context of an example? Let us take as an example something that both Mr Touhig and I are a bit familiar with—the role of QinetiQ in the recently awarded Defence Training Review contract. Did you play any role in that decision?
***Peter Schofield:*** We played no role at all in that, and nobody within the Ministry of Defence who was involved on the Shareholder side had any involvement whatsoever in the defence training review award.
***Sir Brian Bender:*** Can I give you another example: the run-up to the announcement that Alistair Darling made before Christmas on the post office network?

**Q54 Mr Dunne:** I will come on to that, because I have a similar question on it. Is it not part of your role to seek to maximise value for the investments that you have?
***Peter Schofield:*** It is, absolutely.

**Q55 Mr Dunne:** Therefore contracts in which the Government have a commissioning role are issues of great importance to some of the contractors. For example, we read today in the newspapers that QinetiQ might be bidding for a defence contract on the south coast. Would you see it as part of your role to encourage companies to bid for any Government contracts that you are aware of?
***Peter Schofield:*** Absolutely. All of our businesses should be looking to win contracts and to maximise their positions. However, I would also add that it is vital for there to be a clear Chinese wall within Government between the shareholder function and the customer function. In all of our work we have been careful, indeed keen, to ensure that that division is clarified.

**Q56 Mr Dunne:** In the context of the Defence Training Review, can you assure us that that Chinese wall was rock solid?
***Peter Schofield:*** Yes, I can.

**Q57 Mr Dunne:** I am very pleased to hear it. Can we move on to the Post Office, because that is another good example of the problem that you have in maintaining your role versus the Government one, in particular where you appear to have a management responsibility for the consumer body, Postwatch. Is that correct?
***Sir Brian Bender:*** May I say what I was going to say? It may not answer the question that you have just moved on to. If you take the run-up to the statement that Alistair Darling gave before Christmas on the post office network, there was clearly a range of options being examined by the Shareholder Executive. The Secretary of State got advice that had to balance, tease out and let him make a decision on where the public policy interest lay as against the pure shareholder value. A commercially viable post office network would be significantly smaller than the one that was the basis of the Government's consultation.
The role of the Shareholder Executive in those circumstances was to ensure that the costs and benefits of different options were spelled out so that Ministers could take a decision eyes wide open, so to speak, that if they invested so much money, for example, in the social policy aspects of the costs of maintaining a post office network, that is what they could have. If they wanted a purely commercial network, the company advised us how it would be in the moving market. It was really to ensure that Ministers had those facts in front of them transparently and were able to make what they believed to be the right policy decision in full knowledge of the facts. That was a way in which the policy versus value issue was used, in a very current example.

**Q58 Mr Dunne:** Indeed, and what value did your team add to that process? That was surely something that the post office network or Royal Mail itself ought to be in a position to advise the Government on.
***Sir Brian Bender:*** The Shareholder Executive was providing the advice to Alistair Darling and itself taking advice from Post Office Ltd and Royal Mail. No other part of the DTI was directly involved in that. The NAO Report identifies an issue, at paragraph 3.4, about whether there ought to be a separate part of the DTI involved, but there was not in this particular case. It was the Shareholder Executive and obviously my finance people, because of the potential cost to the taxpayer, but no other part of the DTI.

**Q59 Mr Dunne:** Have you had any involvement with Network Rail?
***Peter Schofield:*** No.
***Mr Dunne:*** Thank you.

**Q60 Chairman:** Mr Dunne mentioned QinetiQ as a possible link to the establishment of this executive, but figure 1 on page 9 is entitled: "A number of developments, both within the UK and overseas,

played a part in the establishment of the Shareholder Executive." The PAC figures largely in that, so this is your chance, Sir Brian, to give us a pat on the back. This is a difficult question for you.
***Sir Brian Bender:*** It is very difficult. There is no doubt that the issues on which this Committee has reported over the years have highlighted some of the problems and the lack of appreciation of shareholder value that contributed to the Government deciding to set up this organisation. Is that good enough for you?

**Q61 Chairman:** Is that from your brief?
***Sir Brian Bender:*** No, no, I am looking at the table. Did your Clerk provide me with a brief? I don't think he did.

**Q62 Chairman:** No Permanent Secretary would ever admit that a mere Select Committee actually resulted in a change of Government policy, would you?
***Sir Brian Bender:*** It was bound to be a contributing factor, as indeed was some of the stuff that you have done on failed IT projects and successful IT projects.

**Q63 Helen Goodman:** Sir Brian, paragraph 3.13 is on changes to the financing regime. You were rather cautious about that in answer to questions from the Chair. Are you saying that if we went down the path of the first bullet point, it would privilege these organisations and make it more difficult for Ministers to take a decision between investing in them and investing in, say, rural transport, schools or anything else? Is that your basic point?
***Sir Brian Bender:*** That is essentially it. As you are implying, a Minister in charge of a Department ought to be able to have a view about prioritising resource allocation. If that were ring-fenced, it would imply some sort of privileged treatment. That is my anxiety about it.

**Q64 Helen Goodman:** I am very sympathetic to that. I do not know whether this is your responsibility or Mr Bryant's, but there is a target in here of increasing the value by £1 billion. Why did you alight on that number?
***Martin Bryant:*** It was a combination of some bottom-up analysis of six of the major businesses that had been established in the portfolio and for which we had good information and, to be honest, a bit of a top-down target to create something eye-catching about shareholder value. The target is measured as the change in economic profit year on year. You will see in the appendix of our annual report a detailed exposition of how that is done. The purpose is to attract attention to the target, and I was pleased to see the NAO Report reflects the fact that while the target has some limitations, it has achieved that objective.

**Q65 Helen Goodman:** Whether or not the target has been achieved depends on whether those calculations are right. Appendix 3 sets out three possible ways of valuing the companies, one of which is discounted cash flow. Sir Brian, this is an issue which we have discussed before. When you came to the Committee last year, I asked you about the nuclear liabilities of British Energy. I said: "I wonder whether you could possibly provide the Committee with a note on the basis which is recommended in the Treasury Green Book?" To which you replied: "We shall do that." However, you have not. Why not?
***Sir Brian Bender:*** I thought we had provided it.

**Q66 Helen Goodman:** No, you provided us with a note setting out why you did not want to do that, but not, as we requested, with the numbers on the basis in the Green Book.
***Sir Brian Bender:*** I apologise. There was clearly a communications breakdown. It was not a reluctance to answer questions. I had understood—I re-read the transcript of that hearing last week—that the basis of your questioning had been why we had used one discount rate versus another. That is what we sought to answer. However, if the Committee would like the other material, we will provide it as soon as we can after this hearing.

**Q67 Helen Goodman:** That would be helpful. It would also be helpful if we could have the nuclear liabilities for the other businesses that are your responsibility on the same basis. I will read them into the record to avoid further confusion. They are the United Kingdom Atomic Energy Authority, British Nuclear Fuels Ltd and the Nuclear Decommissioning Authority.
***Sir Brian Bender:*** We will do that. If there is any doubt, we will liaise with the Clerk to ensure we provide what the Committee wants.

**Q68 Mr Bacon:** I should like to start by asking you, Mr Bryant, about recruitment and pay. On page 28, it says that because "High calibre staff are essential to the Executive's work" and "Given the range of commercial issues dealt with", a significant proportion of your staff "are recruited from industry and the financial services sector, currently on fixed-term contracts or on secondment." First of all, how many staff do you have?
***Martin Bryant:*** The total number is 45.

**Q69 Mr Bacon:** How many of those are on secondment?
***Martin Bryant:*** I can give you the ratios. Of the total 45, 30%. is external, 70%. is internal. Perhaps more helpfully, that ratio is reversed for senior staff. At the most senior level, 70%. is external and 30%. is internally recruited civil servants.

**Q70 Mr Bacon:** Therefore, most of your senior colleagues are external?
***Martin Bryant:*** External.

**Q71 Mr Bacon:** And are on short-term contracts or on secondment?
***Martin Bryant:*** Correct. They are typically on three or four-year employment contracts.

**Q72 Mr Bacon:** How many people come under the category of senior staff?
***Martin Bryant:*** Twelve.[2]

**Q73 Mr Bacon:** Would you send us a note of who they are, where they have come from and how long they are staying with you?
***Martin Bryant:*** I can, although we mention who they are in the back of our Report.[3]

**Q74 Mr Bacon:** If you send it to us, it will be in the back of our Report as well, which will be very helpful.
How many businesses do you have in which you have shareholdings?
***Martin Bryant:*** Twenty-seven.

**Q75 Mr Bacon:** Is there a complete list in the Report? The one in table 2 on page 11, covers your businesses by the different ways in which you interact, but is that a comprehensive list?
***Martin Bryant:*** It is.

**Q76 Mr Bacon:** The turnover of them all is £21.449 billion. The chart on page 16 lists some of them, with the valuation—or at least the lower end valuation and the higher end valuation. Presumably you have a lower end and a higher end valuation for all 27?
***Peter Schofield:*** Table 5 on page 16 is the National Audit Office's valuation, carried out with Accenture. They used a multiple-based valuation technique. I think that covers only 18 of the 27. They could not find a commensurate business, which they could use as a comparable for the purpose of finding a multiple, for the remaining nine.

**Q77 Mr Bacon:** Do you have a valuation for the others, even if it is only a range, as here—lower and higher?
***Peter Schofield:*** We do not value on an absolute valuation basis. As Mr Bryant has described, and as set out in the Report, we use a valuation that looks at the change of value—a change of economic profit. We have economic profit models for 19 of our 27 businesses, six of which are covered by the target that is in the table in the Report.

**Q78 Mr Bacon:** Presumably, in the national asset register, to which Mr Touhig referred, to enter in that the amount for each of the businesses in which you have an investment and which you own, you cannot just put in the change value, you have to put in the value.
***Peter Schofield:*** When we were developing our target, one of the key issues that we had to deal with was that all our businesses have a range of different Government objectives. They are not just about value maximisation.

**Q79 Mr Bacon:** I did not say that. I used to act for a mutual building society and I spent a lot of my time during the demutualisation campaign trying to persuade newspapers to run articles about the value of not demutualising. Mutual building societies are not profit maximising entities. They are trying to achieve other objectives for their members. That does not mean that a valuation could not be placed on the building society. Presumably, by the same token as the picture on front of the Report clearly illustrates in a rather worrying way, there are competing and sometimes conflicting objectives. That does not alter the underlying fact that you ought to be able to come up with an underlying valuation.
***Peter Schofield:*** Our purpose in setting a target was to focus on what we would achieve and, in a sense, by focusing on the value uplift, because one assumes that the policy and non-financial objectives would remain constant throughout the period, we would have a much clearer idea about what we are delivering and what difference was being made than we would have if we focused on an absolute valuation which, by relative comparison with the peers of the businesses, will be depressed for precisely the reason that you have described—the non-value objectives that the businesses have to achieve. That was very much the thinking that went on back in 2004, as we were developing the target, and I guess that our internal processes were set up to deliver that.

**Q80 Mr Bacon:** Can you come up with a valuation for each of the businesses? I want to know what you would cash up at. Whether or not you are going to cash up, I want to know the value, within a range, of what the Shareholder Executive owns—not some of it but all of it.[4]
***Peter Schofield:*** The National Audit Office has done its own analysis. I have no reason to disagree with the work that has been done. They had Accenture look at it.

**Q81 Mr Bacon:** It says that the total value is £20.784 billion, but that is only of those 18 or so businesses, is it not? What about the others?
***Sir Brian Bender:*** The reason why we are going round in circles is—

**Q82 Mr Bacon:** Because you do not want to answer the question.
***Sir Brian Bender:*** The answer is that the information is not currently available for the Shareholder Executive. I think that that is right.

**Q83 Mr Bacon:** You must have some idea.
***Sir Brian Bender:*** And therefore it is a non-trivial task. If it had been easily available, the NAO would not have had to got Accenture to help it do it.

[2] *Note by witness:* Twelve is the figure recorded in the NAO Report but that includes the previous Chief Executive who, at the time of publication of the NAO Report, was part-time Chairman. The current complement is eleven.
[3] Ev 16–17

[4] Information provided, not printed.

**Q84 Mr Bacon:** Surely you must have some idea of what it is worth. I direct you to figure 5, Mr Schofield. I take it that £991 million and £1.209 billion are the total figures for the service businesses and others. Is that right?
***Peter Schofield:*** I believe that that is what the NAO table says.

**Q85 Mr Bacon:** Ms Leahy, is that right? On page 16 at figure 5, it says: "Service businesses and others" and refers to NATS, Channel 4, Ordnance Survey, Working Links, DSTL, Royal Mint, Covent Garden Market Authority and Tote. It gives a total to the right of £991 million being the lower end of valuation and £1.209 billion being the higher end of valuation. Is that for all those businesses?
***Patricia Leahy:*** It is for all of them.

**Q86 Mr Bacon:** So in order to get the valuation for NATS, Channel 4, Ordnance Survey, Working Links, DSTL, Royal Mint and Covent Garden Market Authority together, you must first have had a valuation for each of them separately.
***Patricia Leahy:*** We did.

**Q87 Mr Bacon:** What is it?
***Patricia Leahy:*** Are you asking about the value of each of them?

**Q88 Mr Bacon:** Yes. There are 18 businesses, but the only valuations listed are four totals. What are they each worth?
***Patricia Leahy:*** We could divide it out.

**Q89 Mr Bacon:** You could have done. You could just have had an extra column, so we could have seen how they added up.
***Patricia Leahy:*** There were concerns about attributing individual values to the businesses on the part of the Shareholder Executive, which is why we rounded them up.

**Q90 Mr Bacon:** Why? On the basis of what? Commercial confidentiality? You are not about to float them on the stock market. Even if you were, the market would end up finding the level, would it not, Mr Schofield?
***Peter Schofield:*** There are certain sensitivities about the listed companies. NATS has a tradeable bond—

**Q91 Mr Bacon:** Hang on a minute. The listed companies? It is perfectly possible to work it out for the listed companies. You just look it up in the paper.
***Peter Schofield:*** No, you are absolutely right.

**Q92 Mr Bacon:** So you retract that statement?
***Peter Schofield:*** There are certain sensitivities over what we say about NATS, because it has a tradeable bond. We could happily look into it. I cannot remember the detail as to why we were concerned about it.
***Sir Brian Bender:*** The cavalry behind us says that we did not object.

**Q93 Mr Bacon:** Excellent. I just do not see how you could have come up with those numbers without coming up with the subtotals that make them up.
***Sir Brian Bender:*** It was the NAO that provided them. The question was whether we objected to a breakdown. As we understand it, we have not.

**Q94 Mr Bacon:** But for the avoidance of doubt, the NAO—"made it up" is probably not a phrase that it would care for. But you derived the figures following a study that you did with Accenture.
***Patricia Leahy:*** We did. It was based on multiples and probably gives a reasonable indication of value, but it is not very precise. Events can overtake the figures. It is a good indication, but—
***Sir John Bourn:*** If the Committee would like to have them, we will let you have our calculations.

**Q95 Mr Bacon:** What I would really like is a precise blend of tables 2 and 5, giving all the information in one place about what each organisation does, what business type it comes under, what its turnover is, what its profit is if there is one, what the lower end valuation is and what the higher end valuation is. Put in as many footnotes as you like to explain why it is all hedged around and that if you sold it, it would fetch 70% or 90% more than that—except, of course, that you are not going to sell it—but I would just like to see in one place a chart showing what you own, what they do, what their turnover is and what they are worth. Is that too much to ask?
***Peter Schofield:*** On the valuation, as I said, the point is that we do not value our businesses in the way that you are proposing we should. We use economic profit. The Report in the appendix talks about the three different potential methodologies.

**Q96 Mr Bacon:** I waded around in appendix 3 for quite a while. It reminded me of a class that I sat in on at the Harvard business school about capital asset pricing models, at the end of which I wanted to take myself out and put my head in a bucket of water, to be honest.
***Sir Brian Bender:*** We can do most of what you want. We cannot ourselves provide our own valuation. We can plainly incorporate—

**Q97 Mr Bacon:** But you must have it none the less. That is what I find odd. They are your assets. You own them. You must have some idea of what you think they are worth. Do you not?
***Peter Schofield:*** We focus on the economic profit.

**Q98 Mr Bacon:** Yes, I know. You have said that four times. Do you really have no idea? Have you never done even a back-of-the-envelope calculation to give yourself an idea of what they are worth? Have you never been curious? I am. Most of the public are.
***Peter Schofield:*** If what you are seeking is a market valuation for each of the businesses, as Sir Brian says, that is a non-trivial piece of work, because each business will be valued in a different way. In some cases, the appropriate market valuation—

**Q99 Mr Bacon:** On the other hand, as we know, you have corporate finance and investment banking expertise in-house, which you or Sir Brian described as available to the public sector as a free good.
***Sir Brian Bender:*** As a free good for managing those businesses rather than doing that sort of exercise, unless there is a real intrinsic value in it. I am happy to talk to the NAO to see what we can provide by combining the two, but I am reluctant to ask the Shareholder Executive to do a task that does not seem to have an intrinsic value.
***Chairman:*** I have to say that I do not think that that is the view of the Committee. We cannot understand why you do not think that there is intrinsic value in we, the public, the shareholders, ultimately knowing the value of the businesses that we own. I cannot understand your objection.

**Q100 Mr Bacon:** How do you make a decision in the long term—how do you plan forward about what you might keep and what you might sell—if you do not have a clue where it might stand in the marketplace?
***Chairman:*** Mr Dunne wants to ask a supplementary on precisely that point.

**Q101 Mr Dunne:** In the context of comparing yourselves with the private sector, which the National Audit Office does in this Report, every private equity firm has to value its portfolio regularly to comply with BVCA valuation guidelines. If you are not doing that, I think you ought to put yourselves under the same sort of rigours and strictures that the private sector is encouraged to do by Government.
***Peter Schofield:*** Yes, we do value our businesses in the way described. What we do not do, which is the point that Sir Brian was discussing, is a market valuation for all 27 businesses. That is a non-trivial piece of work. We can debate with the NAO about how to do that.
***Chairman:*** You said that several times, but we do not agree with you.

**Q102 Mr Bacon:** It is not trivial. What the Chairman is saying is that we would like you to do it, because we would like to know the answer.
***Sir Brian Bender:*** Can we take this away and see what we can do? One thing I am sure that the Committee would not want is that we then have to employ advisers at great expense to provide some of the answers.

**Q103 Mr Bacon:** We are confident that you have the in-house skills.
***Sir Brian Bender:*** We will take this away and perhaps we can talk to both the NAO and the Clerk to ensure that we can meet the Committee as far as we can.

**Q104 Mr Mitchell:** I am just trying to understand what you have and have not got, what you have half got and what you are handling in conjunction with the Department. It looks like a typically British compromise, which could otherwise be described as a mess. What is the rationale behind the exclusions? On page 21, table 9, there is a list of Government-owned bodies outside the Shareholder Executive's portfolio. Why should those not be in and would it not strengthen your authority and effectiveness if they were?
***Peter Schofield:*** There are a variety of different reasons for each of those businesses listed in table 9 on page 21. Some are the responsibility of local authorities or devolved regions—you see Transport for London, Manchester Airports Group and Blackpool Airport Ltd. Because of the unique status of the Trust ports, the Government have very little in the way of what you might call shareholder levers. We have talked about the Department of Health in the context of Dr. Foster, but Partnerships for Health, for example, until very recently was a joint venture with Partnerships UK, a business—

**Q105 Mr Mitchell:** But the NAO says that it has not found a sensible rationale behind the exclusion of any of them. Is there one?
***Peter Schofield:*** I like to think in terms of concentric circles. We started with a list of businesses, in terms of the original discussions with the Treasury, the Cabinet Office and Permanent Secretaries, that were part of our portfolio. Over time, as we have seen the opportunity to add value to shareholdings from other Departments, we have approached Departments and said that we think we can add value and help.

**Q106 Mr Mitchell:** Has it weakened you? The NAO also says that this inconsistency, this lack of central authority to bring business into the portfolio, is incompatible with the executive's Government-wide mission. Would it strengthen you if they were all in? Or would it make life so much more complicated that you do not want them?
***Martin Bryant:*** First, on context, the NAO had a figure of £25 billion as the turnover of businesses in Government ownership. We currently have £21 billion-worth of turnover in our portfolio, so we have the lion's share of businesses currently. On your question as to whether it would help, the issue is if we can be helpful and useful. That is the big challenge.

**Q107 Mr Mitchell:** It is also if you can handle them.
***Martin Bryant:*** At the moment, as the NAO Reports says, we are resourced to handle the current portfolio. If we were to expand significantly, particularly under comply or explain, we would have to re-look at our resourcing.
***Sir Brian Bender:*** The first one of those, as you will have spotted, Mr Mitchell, is a DTI body, the Nuclear Decommissioning Authority. The starting point there was that the Shareholder Executive did not have a role because we wanted to keep the shareholder functions of BNFL and UKAEA separate from the NDA, because there was competition for contracts going on. I have now asked the Shareholder Executive to have further dialogue within the DTI, giving the Executive a role on the commercial aspect of the NDA. So, I am

trying to get the Shareholder Executive to have more of a role in that body, alongside the Energy Group of the Department.

**Q108 Mr Mitchell:** I just wonder, always having a penchant for things New Zealand, whether there would not be virtue in the New Zealand structure, which is detailed on table 18 on page 39? There are two Ministers mainly responsible: that is State-Owned Enterprises and a Minister for Crown Research Institutes. There are also some sectoral Ministers. If you had a Minister responsible in the same way, would that work in this country?
***Sir Brian Bender:*** Let us take the post office network as a useful example, and the statement that my Secretary of State made in December. There were some quite difficult policy and shareholder value issues to be decided. The decision that led up to his announcement was a collective one. Clearly the Treasury had a strong role as part of that. It is not clear what would have been added from Alistair Darling's or the Shareholder Executive's point of view if they had had a Minister sitting alongside him looking at the complicated issues involved in a decision like that.

**Q109 Mr Mitchell:** That is one decision is it not? As it was, it took over a year to make. I take it from the cumbersome situation that you have just described that that is the explanation about the decision. My question was really, would having a Minister overall—those negotiations would still have to take place—strengthen the mission?
***Sir Brian Bender:*** Mr Bryant and Mr Schofield may want to speak for themselves, but I would be concerned if that detracted from the ownership responsibility, if I can put it that way, that an individual departmental Minister has, whether that is Alistair Darling for British Energy, BNFL and so on or the Secretary of State for Defence for the Met Office. I would be a little bit concerned if another Minister in effect enabled the lead Minister to relax because someone else was looking after it. This comes back to the question of the balance between policy and value. If it was only a value issue, it would be much more straightforward, but as most of these things involve a combination of the two, I would be uneasy about a situation where another Minister had a role that might detract from the lead Minister's role. This is against the background that Treasury Ministers, because of their overall interest in these issues, are involved in virtually all these cases.

**Q110 Mr Mitchell:** You have a mixture of staff drawn from the private and public sectors, and the NAO seems to be trying to make the mixture virtuous. I wonder whether you will have problems with paying them, competing with the City and the higher level of salaries there. I saw an extraordinary statement in the Report that your people have unique opportunities such as, for example, working to Ministers. That is probably one of the most exciting challenges that they could possibly have, but I am not sure that it is a staff recruitment opportunity.
***Martin Bryant:*** The good news, Mr Mitchell, is that they take quite a substantial discount to enjoy the pleasure of working with Ministers. I shall just repeat my earlier answer. We are actively recruiting at the moment. We work within the pay scales of the senior civil service, and so far we are able to attract people of the right talent and calibre because of the intrinsic interest in this job.

**Q111 Mr Mitchell:** You have turnover at the moment.
***Martin Bryant:*** We have some turnover.

**Q112 Mr Mitchell:** City salaries are very high. Do you anticipate problems?
***Martin Bryant:*** At the moment I do not anticipate problems.
***Sir Brian Bender:*** As I said earlier, Mr Mitchell, if we see any on the horizon, we will want to act. We do not feel complacent about this area of questioning. It is something that we keep under regular review.

**Q113 Mr Mitchell:** The Report says that another thing that could affect recruitment is the Shareholder Executive's perceived proximity to the centre of Government. I do not know whether that means access to titles or whatever, or whether it is part of contact with Ministers. Decisions on future location will be important there. Does that mean that you would have an advantage in being moved out of the Department of Trade and Industry?
***Sir Brian Bender:*** I can talk about the advantages I see in being in the DTI, but maybe my colleagues could talk about whether they see them.
***Mr Mitchell:*** Well, you go first.
***Sir Brian Bender:*** First, there is an advantage for the DTI in the Shareholder Executive being there, because the range of both corporate finance skills and relationships with investors is a great asset to have in the Department. The Shareholder Executive has incorporated the old Industrial Development Unit, and that has brought a wider mix of skills to bear when we have looked at corporate finance for ailing companies or companies that are looking for grants. The real question is whether its weight in Whitehall is diminished by being located inside a Department, rather than centrally. I have seen no evidence of that, and talking to three or four permanent secretary colleagues, they have not either. But there is a real issue about the marketing, to go back to Mr Touhig's question.
***Mr Mitchell:*** Let's ask them.
***Martin Bryant:*** Can I pick up on Sir Brian's point? The issue that Mr Touhig put to us is one of marketing and making sure that there is wide awareness of what we can do. I do not think it really matters whether we are operating out of the Department of Trade and Industry, the Cabinet Office or any Department. It is about making sure that people know what skills and capabilities we have.

The evidence heretofore is that we have been able to expand the number of Departments we have worked with quite significantly since moving from the Cabinet Office to the DTI.

**Q114 Mr Mitchell:** I cannot see why NHS foundation trusts have access to capital markets but you do not. Does having no access to capital markets put you at a disadvantage?
***Peter Schofield:*** I can probably answer part of the question, but maybe the Treasury would be best placed to answer the rest of it. We operate very clearly within the Government's fiscal rules and spending aggregates, which focus on the public sector as a whole, which includes public corporations and therefore most of our businesses. There are very clear Treasury rules about the way in which Government-owned businesses can finance their activities.
I guess that the question then is, is there a shortage of financing—a point addressed very clearly in the Report. As to the situation with foundation trust hospitals, that is more a question for the Treasury.

**Q115 Mr Mitchell:** There is the suggestion in paragraph 3.8 that the executive could examine each case on its merits and construct a dividend target for each business so they are not stashing away surpluses to hide them from the Department. Do you see advantage in a dividend target?
***Peter Schofield:*** I think we need to improve our targetry—that is very clear from the NAO Report. At the moment we have a dividend target, which is to improve the dividend performance, but we do not have specific numbers around it. I think we definitely need to move in that direction.

**Mr Mitchell:** So the mission will be the same—shareholder value, in a sense, as opposed to a target.
***Chairman:*** I think Mrs. Goodman has a supplementary question.

**Q116 Helen Goodman:** I do. Sir Brian, I want to check whether I heard correctly what you said in answer to a question from Mr Dunne. Was it that all the advice that Alistair Darling received on the policy in relation to the post offices came from the executive?
***Sir Brian Bender:*** I cannot recall any advice coming from another part of the Department. When he was looking at the post office network, or the parallel but different issue of the re-financing of Royal Mail, the Shareholder Executive were the people who provided him with advice. That advice was cleared with the DTI Finance and Resource Management team, because plainly some of the options involved a hit on the DTI DEL. But I do not recall a situation in which the Secretary of State got advice from another part of the DTI.

**Q117 Helen Goodman:** Those of us with rural constituencies would say that that confirms our experience.
***Sir Brian Bender:*** But can I say that Jim Fitzpatrick as the junior Minister, and indeed Barry Gardiner before him on this issue, had a lot of bilateral discussions with other parts of Government? For example, there were bilateral meetings with the Department for Environment, Food and Rural Affairs on the rural network and a lot of discussions with the Department for Work and Pensions on the Post Office Card Account. The final decision was taken in the normal collective Cabinet discussion. I am interpreting your question rather literally.
***Helen Goodman:*** That was my question. Thank you.

**Q118 Chairman:** So we do not have your executive to thank for the scale of the post office closures, Mr Bryant? You are not responsible for trailing a blaze of destruction across my constituency, are you?
***Martin Bryant:*** I could not possibly answer that, sir.
**Chairman:** Sorry?
***Martin Bryant:*** As Sir Brian said, we put advice to Ministers on the attraction or otherwise of different proposals on the size of the post office network.

**Q119 Mr Williams:** I am now literally picking up past crumbs that have been left over. Coming back to the issue of the place in Government for the executive, the NAO background briefing says that, "the Executive lacks statutory authority . . . and could benefit from a closer institutional link to the centre of Government." What do you mean by that, and what do you think the beneficial point closer to the centre of Government would be?
***Patricia Leahy:*** When the Shareholder Executive was set up, it was within the Cabinet Office, and it moved to the DTI in 2004. There was, we gather, a Reporting link retained between the Cabinet Office and the then chief executive, Richard Gillingwater. We felt that that relationship was very important for winning over other Departments to seeing the benefits of using the Shareholder Executive and getting them involved. We thought that there was a little misunderstanding in some parts of Government over the link, and perhaps there was the impression that it was an institutional link. That sort of link was probably quite helpful to the Shareholder Executive in developing its portfolio.

**Q120 Mr Williams:** This links in with the point that Sir Brian was making about what the point of having a Minister sitting alongside a Minister is. However, the point is that if he is a Minister in a different Department, he has access to the Cabinet separately. There is all the difference in the world for the executive between being in the DTI and being in the Cabinet Office, which has no direct interest in any of the organisations or assets but has an overall Government viewpoint.
What has happened is that a power struggle has been lost somewhere in the Cabinet. I came through the Department of Economic Affairs in the 1960s and we had an ongoing fraternal war with the Treasury. Where in Government did the decision originate to take it from the Cabinet Office, where there is a Minister with access to the Cabinet? Was it from the

DTI or from the Treasury, as in our case, when eventually the Treasury won and got rid of the DEA?

***Peter Schofield:*** It followed the conclusions of our start-up review, which are recorded in one of the annexes of the NAO Report. At the time, our role was an advisory one. We sat in the Cabinet Office and provided advice to Departments. One of the conclusions of our start-up review was that we did not need more advisers. In terms of the shareholder function, we needed to bring the right skills mix directly to bear. We then talked to other Government Departments about whether that was something that we could do, and the obvious place to start was the DTI, because that is where the largest businesses in our portfolio were situated. We had a discussion with the permanent secretary at the DTI and the pragmatic decision that came out was that we should move ourselves to the DTI, and at the same time take executive responsibility for the DTI businesses.

**Q121 Mr Williams:** So, you had a discussion with the DTI. Did you not think of mentioning it to the Minister at the Cabinet Office?

***Sir Brian Bender:*** Any such decision is submitted by the Cabinet Secretary to the Prime Minister for final approval, so whatever went on beforehand, the Prime Minister will have approved the change.

I know that this is not quite what you are asking, Mr Williams, but I am convinced that there is more of a marketing job that the Shareholder Executive needs to do. On the back of the Report, and now that Mr Bryant has been in post for three or four months, it is our plan that he makes a presentation to other permanent secretaries to ensure that there is no hiding place for not knowing what the Shareholder Executive can bring to their operations.

**Q122 Mr Williams:** I come back to the point about bringing people in from outside on special contracts. Back in the old days of the DEA—and then the Department of Industry which took it on when the DEA was abolished—you had your special industrial advisers. They were great assets and brought in an expertise that you did not have within Government. How far is it correct to suggest, as the NAO does, that there is a limitation in the quality of people you are able to attract because of the remuneration framework in which they have to operate? Does someone on secondment, for example, come into Government paid at his old rate by his old firm rather than having to accept the DTI rates?

***Martin Bryant:*** We have two bases of employing people. One is on fixed-term contracts.

**Mr Williams:** Yes, I noted that.

***Martin Bryant:*** Typically, those people are placed within the existing bands of the civil service senior pay scheme, and the majority of our senior people are employed on those fixed-term contract arrangements. Secondees often come in for a shorter period, sometimes 18 months to two years. In those cases we normally pay them at the appropriate level within the civil service structure, but their employer may top up their pay.

**Q123 Mr Williams:** A charitable contribution to the Government?

***Martin Bryant:*** We examine each circumstance that arises. As I said, at the moment we are confident that we can start up with the right level of people, but as Sir Brian said, if that happens to—

**Q124 Mr Williams:** It is an interesting thought, just at a tangent, that you recognise that you need people from outside whom you cannot recruit within the Government service, but you cannot afford to pay the money to get them in, so the Government rely on literally charitable support from the private sector to make available a human asset that you could not afford to buy.

***Martin Bryant:*** There are two parts of the answer to that. First, I would like to think that if an investment bank or whoever is seconding someone and topping up their salary, they feel that there is a career development for that individual, so they are not doing it for charity.

**Q125 Mr Williams:** You mean they are getting something out of it?

**Sir Brian Bender:** They will get someone who will grow out of it. I am not sure that we are talking about getting something improper out of it. They get an individual whose career would benefit from having had 18 months or so in this area. For the people we are recruiting on fixed-term contracts, the charity, so to speak, is from them, in the sense that they are accepting a lower rate of pay than they would get on the market, presumably for the very reasons cited in the NAO Report—they see an attraction in the job. That is what we need to watch very carefully.

**Q126 Mr Williams:** Coming back very briefly to the dispute about valuation, I am still a bit lost on your rationale as to why you cannot give us a valuation. According to table 3, you have so many common functions with the private equity firm, but you do not seem to have the basic information available that they would have in order to make judgments on the same subjects. How do you justify that?

***Peter Schofield:*** I am not saying that we do not have the basic information available. We have all the basic information available, and we publish it in our annual Report each year. The specific question was on valuation, and in that case, in order to address Mr Bacon's question, we would have to do a market valuation for each of our 27 businesses. If we were to be in the process of selling them, the market valuation would be done on a different basis. We have a common valuation technique across all our 27 businesses.

**Q127 Mr Williams:** Hold on. Now I am a bit lost. You are saying that you have a common valuation basis across the lot, but it is not really a correct valuation, because the correct valuation is the valuation that you have decided not to do, but that would be done by a private company.

***Peter Schofield:*** No, I am not saying correct, I am just saying that if you were to sell these businesses, each one would be sold in a different way. The basis of carrying out the market valuation would be different. What we developed for our internal purposes was a single methodology that could be applied to the portfolio as a whole so that we could measure our performance on a portfolio level basis. That is a point that the NAO have looked at, and their view was very much that our target was appropriate at the time, but going forward we need to develop and refine it. That is something that we have undertaken to do.

**Q128 Mr Williams:** When you say refine it, what do you mean by that? You say that you have undertaken to do something. What precisely are you envisaging doing in future that you are not doing now?

***Peter Schofield:*** To respond to the specific recommendations on the target that the NAO have produced, as set out on page 6 of the Report. We have also undertaken to respond to Mr Bacon's question and to see what we can do.

**Q129 Mr Williams:** You will be letting us have a note.

***Peter Schofield:*** Exactly. We will let you know.

***Sir Brian Bender:*** I am sorry, but I misled Mr Williams a few minutes ago. I am advised that while we have the capability for people to be topped up by their seconding organisations, at the moment we have no one in the Shareholder Executive paid outside the senior civil service band. I am afraid I misled you, and I just wanted to correct the record.

***Mr Williams:*** No problem.

**Q130 Mr Bacon:** My question relates to paragraph 2.16 on page 18. It says that "there are reasons to be cautious about future financial performance: 10 of the businesses in the portfolio did not record operating profits in each of the last three years (2003-04 to 2005-06)." Could you send us a note saying which those businesses are, and what operating loss each presumably recorded in each of those three years?

***Martin Bryant:*** Yes.[5]

***Sir Brian Bender:*** Will do.

**Chairman:** We have had an interesting hearing. We are very grateful to you and for your answers. Clearly, Mr Bryant, you are adding value. We just want to help you unlock the shackles, so that we as shareholders can get more from our business dealings in Government. Thank you for what you are doing, and we want to help you to acquire more powers and more influence. Thank you, Mr Bryant and Sir Brian.

[5] Ev 17

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## Supplementary memorandum submitted by the Department of Trade and Industry

Question 73 (Mr Richard Bacon): *Names and background of senior staff in the Shareholder Executive*

| | *Directors* | *Basis of Appointment* | *Start date* | *Career background* |
|---|---|---|---|---|
| *SCS Pay Band 3* | | | | |
| | Martin Bryant | Permanent Civil Servant | November 2006 | Martin Bryant was Director of Strategy at the Home Office from September 2004–November 2006. Prior to that Martin spent two years as Interim Chief Operating Officer at BP Retail Ltd. From 1989–2002, Martin worked for The Boots Company Plc. He developed his career in senior general management roles being successively Managing Director of Boots Opticians, Operations Director of Boots the Chemists, Managing Director of Boots Retail International and Director of Corporate Development. |
| *SCS Pay Band 2* | | | | |
| | Stephen Lovegrove | Fixed Term (to April 2008) | April 2004 | Stephen was previously a Managing Director and head of European Media Group at Deutsche Bank. Prior to that he worked in strategy consulting in the media sector. |
| | Mark Russell | Fixed Term (to April 2010) | November 2004 | Mark was previously a corporate finance partner at KPMG London and Frankfurt. Prior to this Mark worked at PwC Corporate Finance, Robert Fleming & Co, Lazard Brothers & Co and AT Kearney. |
| | Peter Schofield | Permanent Civil Servant | January 2004 | Most recently, Peter was on secondment to 3i where he worked with the London Buy-Out Team. Between 1991 and 2002 Peter worked for HM Treasury in a variety of roles including Private Secretary to the Chief Secretary. He also led the Treasury team responsible for government-owned businesses. |
| *SCS Pay Band 1* | | | | |
| | Liz Baker | Permanent Civil Servant | September 2005 | Liz is a professional administrator whose career has focussed on setting the policy framework for business, framing UK and European law in range of areas including competition and utility regulation, company insolvency and employment rights. She has been a director in DTI since 1992. |

| Directors | Basis of Appointment | Start date | Career background |
|---|---|---|---|
| Ruth Hannant | Permanent Civil Servant | October 2004 | Ruth has worked at DTI since 1996. Her previous posts have focused on the energy sector, including the restructuring of BNFL, a secondment to the Energy & Utilities Corporate Finance team at HSBC and leading on the Government's interests in the restructuring of British Energy. |
| Tim Johnson | Permanent Civil Servant | September 2003 | Tim worked previously in the Treasury team responsible for government-owned businesses where he had responsibility for the NATS PPP, the government's shareholding in Royal Mail, and developing and implementing the Shareholder Executive concept. |
| Tim Martin | Consultant* | September 2005 | Tim worked previously for the Office of Rail Regulation as Director of Economics and Finance. Before that he was an investment banker working for Hill Samuel, BZW and latterly JP Morgan Chase. |
| Hugo Robson | Fixed Term (to November 2007) | September 2003 | Hugo was previously a Managing Director and head of ABN Amro's M&A advisory team. Prior to that he was a director at Barings. |
| Susannah Storey | Secondment (to May 2007) | January 2006 | Susannah is on secondment from Citigroup where she is a Director in the UK M&A advisory team. She has worked in investment banking since 1995 when she joined Schroders. |
| Mark Turner | Fixed Term (to April 2008) | April 2004 | Previously Mark was a senior Corporate Development Executive at Rexam Plc, responsible for a wide range of strategy and M&A projects. |

* Following a recent recruitment exercise, Tim Martin has been appointed on a fixed term basis from 1 April 2007–March 2010.

Question 130 (Mr Richard Bacon): *Shareholder Executive portfolio businesses that have made an operating loss in any of the last three years*

1. Paragraph 2.16 of the NAO's Report "The Shareholder Executive and Public Sector Businesses" refers to ten portfolio businesses which have recorded an operating loss in one of the last three financial years. Following the PAC hearing on 19 March, the NAO have advised us that the reference to 10 businesses should in fact have been 11. These are listed below:

| *£m Operating profit / (loss)* | *2003–04* | *2004–05* | *2005–06* |
|---|---|---|---|
| ABRO | 13 | (4) | 6 |
| BNFL | (351) | (203) | 65 |
| British Waterways | (4) | (7) | 0 |
| DARA | 10 | 9 | (3) |
| Fire Service College | (2) | (0) | (1) |
| Met Office | (9) | 10 | 13 |
| Northern Ireland Water Service | (179) | (209) | (236) |
| PartnershipsUK | 2 | (0) | 1 |
| Royal Mint | 2 | (2) | (0) |
| UKAEA | 1 | (2) | 0 |
| Working Links | 6 | (1) | 4 |

2. As stated in the Shareholder Executive Annual Report 2005–06 (Annex A), the Shareholder Executive only advises on specific issues in relation to the Fire Service College and Northern Ireland Water Service. We do not therefore analyse the performance of these businesses in the Annual Report.

3. The figures for Northern Ireland Water Service show the net deficit on operations. This excludes the funding provided through money voted by Parliament, which accounts for the bulk of the agency's income, and will continue to do so until the introduction of charging in the context of the water reform programme.

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