



House of Commons
Public Administration Select
Committee

**Public Administration
and the Fiscal Squeeze**

Oral and written evidence

Thursday 3 December 2009

*David Halpern, Andrew Haldenby, Professor Colin Talbot, and
Tony Travers*

Thursday 21 January 2010

Steve Bundred, Amyas Morse, and Michael Whitehouse

Thursday 25 February 2010

Rt Hon Liam Byrne MP, Ben Jupp, and James Richardson

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The Public Administration Select Committee

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Oral evidence

Taken before the Public Administration Committee on Thursday 3 December 2009

Members present

Dr Tony Wright, in the Chair

David Heyes
Kelvin Hopkins
Mr Ian Liddell-Grainger
Julie Morgan

Mr Gordon Prentice
Paul Rowen
Mr Charles Walker

Witnesses: **Mr David Halpern**, Institute for Government, **Mr Andrew Haldenby**, Reform, **Professor Colin Talbot** and **Mr Tony Travers** gave evidence.

Q1 Chairman: Let us welcome our witnesses. It is a great pleasure to have you come along. What the Committee wanted to do was to basically explore the challenges for the process of government over what is being said to be the fiscal challenges of the upcoming years. I do not particularly want to argue about the actual sort of numbers, as it were, on what has to be done, we know that it is of a high order and we know broadly over what time period things have to happen. It is what this means for the process of government; what it means for doing it; how does government actually set about the task of meeting this challenge. That is really the focus of this Committee, and that is why we wanted you to come and help us with that. Would any of you like to say anything, just very briefly, by way of introduction? We have read some of your collected works on this. Or would you like us to just fire off?

Mr Travers: First, thank you for inviting me, and us, I am sure. The only point that I would strongly reiterate from what I wrote in this short note is to make the fairly simple point that if the past is to be any guide, it would be unlikely that the processes of government and the way in which government is configured will be the first order priority if and when there needs to be a radical reduction in the size of public expenditure and/or an increase in taxation, that is, changing the way the state operates may well be an element in that, but it would be an element of cost-cutting rather than a carefully thought through way of delivering some significant change. That is all I would really stress.

Q2 Chairman: I am sure we will go on to explore that.

Professor Talbot: Thank you for inviting me, Chairman. The only thing I would say is that government over the last 12 years or so has put quite a lot of effort into trying to create more strategic decision-making capacity in the central government, with things like spending reviews and public service agreements and the strategy unit and so on. Ironically, at precisely the moment that that is probably going to be needed, in that whatever size of reduction in public expenditure is agreed upon by whatever the next government is, the best way to do it would be more strategically and more medium

term. The irony is probably that those decision processes that have been attempted to be put in place are being eroded, and it is not at all clear what the commitment is, by either of the major parties at the moment, to try to make those sorts of strategic decision-making processes work. The consequence of that is almost certainly going to be that one will resort to what has always happened in these sorts of crises in the past, which is we just slice 10 or 5% or whatever off everything, with the dire consequences that leads to.

Q3 Chairman: That is very much what we will come back to.

Mr Halpern: Thank you for inviting me. As you know, the Institute for Government has taken a very similar focus to yours, not looking at the big numbers but to look at what are the characteristics of our systems of governance and how it will interact with the fiscal consolidation. We know the headline figures and so on, but in just a few seconds, the punchlines are: there is good reason to think that British government is rather good at doing headline fiscal consolidation, they will reach the numbers, and we can be quite confident about that. It is a bit more of a mixed story as to whether you politically survive it, which is one of the reasons why we looked, of course, at success stories where they both managed a consolidation overseas but also got re-elected, notably Canada and Sweden. But the big challenge, where we have most grounds for concern, is: what kind of consolidation do you run? The characteristics of a system which make us good at doing the headline figures are the same ones which make us tend to operate in a relatively silo-based way, which means that we will not make a smarter set of efficiency gains or whatever, that is not what we will do, we will generally lead to general degradation of service quality. So the key thing, I think, in this sort of eye of the storm, before things really hit, is to identify certain key structural reforms which would change the character with which we would conduct a consolidation. I think that is a very timely focus to have.

Mr Haldenby: Just to add to that, I very strongly agree with that, and if those comments were perhaps focused on the centre of government and Whitehall,

exactly the same arguments apply to the rest of the public sector. In fact, it is more important to address the management of the rest of the public sector, because that is where the costs are. Although the Civil Service has absorbed most political attention recently, and both the Government and the Opposition have been looking at changing the Civil Service, actually all the costs are in public services, particularly health and education, so it is structural reforms in those areas which have to be achieved if this deficit is going to be reduced. I am perhaps a little bit more optimistic than the others on how it can happen, because when we speak to public sector managers, the good ones are already doing it; whether it is chief fire officers who are reorganising fire stations, closing fire stations in order to make those services more efficient, changing staffing patterns and so on, whether it is PCT chief executives who are closing some inefficient hospitals in order to open new units, these sort of difficult, politically contentious things that have to be done to improve management in the public sector are happening, but they are happening without sufficient political leadership and without the kind of structural framework that is needed to encourage it. So I think good managers are there in the public sector to do this, but they do need better political leadership and wider structural reform.

Q4 Chairman: Thank you. Could I just ask you to start with: where do we sort of situate where we are at from a historical perspective? Have we been in this kind of position before? How does the challenge for government now look, compared with how it looked, say, in the 1970s or in the interwar years? Can we learn something from how government responded to deficit reduction issues in those periods that might help us now? Without going into huge historical detail, is it possible to say something useful about that, Colin?

Professor Talbot: The first useful thing to say is that it is far worse than anything that we have had to deal with before, in terms of the cumulative size of the deficit and, at the moment, the annual deficit, which is not to say that it will not get better in the future, but the size of the problem is huge. However, we are also in a position where we have had a fairly prolonged period of extra investment into frontline services particularly, and that raises issues about how far there is scope for things like efficiency savings in those areas. So the challenge is quite large, but we are starting from a fairly high base. I think the political administrative challenge is the one that I talked about at the beginning, which is how do we have some sort of system for taking strategic decisions about this, rather than the way in which we have tended to react in the past, and not always very successfully. I was doing my homework on the train, and rereading Leo Pliatzky's book about the Treasury under Mrs Thatcher, and it is quite salutary that the Thatcher administration came in in 1979 committed to freezing public expenditure, or in fact reducing it in real terms, and failed completely in the first five years. There may be a lesson there somewhere for people at the moment.

Mr Halpern: I hesitate to ever differ from Colin, but it seems to me that you could argue that the 1978 numbers were quite similar, although you might remind yourself also you ended up with a million public service workers on strike. Otherwise you have to go back to the Geddes Axe of the 1920s, which is the last time there was a sustained real term cut, and over that kind of period, from roughly 1920–21 through to 1928, there was roughly a 25% cut in central government expenditure. Arguably that was worse, but of course that was also post-war, and you had a lot of military spending which you were ready to wind down anyway.

Q5 Chairman: I was quite interested, reading the papers, to discover about the Blair Government's Fundamental Savings Review, was it called, in the last period?

Mr Halpern: It was, yes.

Q6 Chairman: Which you know about. It was going to be published, and then was not published, but it was sort of big thinking about savings, was it not? Everyone who was in the system keeps referring to it as a big moment; those of us who were not inside the system would like to know about it.

Mr Halpern: Some of it is now in the public domain. Forgive me if I do not get into the very specifics, but essentially it was an exercise in the context of a spending review, where the Prime Minister felt it was right and proper, if he was going to ask for additional spending, he should seek to identify areas where he felt there was less of a priority. So it was an exercise essentially to identify those areas where he would be prepared to see reductions in expenditure, and he roughly identified about £15 billion of spend. Of course, you might know, that is not that large a number compared to what we are now looking at, but in the sense of whether it was a sensible thing you might do in a spending review process in general, yes, absolutely. We are going to see that writ much larger when we say: what is it that we really want to protect and, therefore, what is it, in a more strategic way, that we are prepared to then sacrifice?

Q7 Chairman: What were the big ticket items?

Mr Halpern: Obviously some of them relate to aspects of benefits and so on, but forgive me if I do not go into the full detail. Julian McCrae, who is sitting quietly over there, was one of the figures, working for us, who did lead it.

Q8 Chairman: That is the frustration, as you know, of knowing people who know what the big ticket items were, but who will not quite tell you.

Mr Halpern: Basically, you can imagine it is an exercise where you are trying to work out which are areas of spend where you think their efficacy is less than you would hope. I can give you a personal view rather than one referring back to the FSR, if I might. You could argue that certain areas of certainly expenditure—EMAs, there was some analysis done where there was an argument there were quite large dead weight costs, some aspects of benefits where you get oscillations—

Mr Walker: We have jargon in there. Can you just speak slowly, in English, so us mere mortals can understand it?

Q9 Chairman: Charles is not a mere mortal!

Mr Halpern: Educational maintenance allowances were an area where the Treasury insisted on rather a good allowance of what worked and what did not. In that, you could work out there were quite dead weight costs, in the sense that there was money spent that you could say did not actually have a beneficial effect. Even though there were some benefits overall, when you worked out the total sum, which was quite substantial, half a billion-odd, you might say actually it was not the most effective form of spend. Another area which, of course, many MPs like is capital expenditure, for example on schools, where you might say in fact the empirical evidence for those educational improvements that follow from it were relatively limited. So there are issues like this, apart from my own examples, rather than from FSR, which there are plenty of.

Q10 Chairman: Thank you very much. One last question, and then colleagues will come in. I think you, David, mentioned Sweden and Canada. These are being given as the alternative scenarios, are they not? As it were, Canada, big targeted strategic cuts, certain bits of government taking the big hits; Sweden, everybody takes a hit across the board. Probably this is too crude, but there are two different approaches to doing it, and reading the materials that you have all been writing, my sense is that some of you are rather more Swedish and some of you are rather more Canadian. Do you want to just say something about that? Tony, I think you are a bit of a Swedish man.

Mr Travers: There is clearly at one end of the spectrum the possibility of carefully thought through, justified, targeted changes here and there, some services taking bigger reductions than others, changes to the way benefits are paid, and all of that carefully worked out line by line, department by department. Alternatively, there is the across the board method, and I can see that although the across the board method is intellectually less justifiable and less cogent in many ways, (a) it is probably easier for the politicians who undertake it, and (b) it has a kind of perverse sense of fairness about it, in the sense that everybody is being targeted with a 5% cut. Then it is fair, is it not, because everybody shares the pain and, frankly, from the Chief Secretary of the Treasury's point of view, fewer people would be coming to say, "Well, we really are an exception", because if it is an across the board cuts regime, then it would simply be easier to manage in that way too. So I think it was more the political reality, and that to some extent is born of observing the way allocation mechanisms work the other way round. Allocate money to local authorities and health authorities in a relatively flat rate way, the Government gets less of a reaction against it than if they skew the distribution so some get a lot and some get very little extra, because those

who get less complain. If you give everybody the same, you get broadly no reaction. So there is a kind of fairness embedded in the idea of across the board.

Q11 Chairman: So you are a sensible Swede. Colin, what are you?

Professor Talbot: Somewhere in between. There are those two alternatives. I think there is a third. The first one, I think Tony is absolutely right that the one governments generally go for, and our Government has in the past, is the across the board top slicing, share the pain equally. There are all sorts of reasons why that is easy, quick, causes less problems in terms of complaints, and so on and so forth. Alongside that as well there will be intense pressure on operational efficiency issues. That is at one end. I do not see these things necessarily as mutually exclusive. At the other end of the spectrum is the strategic allocative decisions about saying, "We are going to stop doing some things in a big way", and make some real savings doing that. I would say there is a third element to this, though, which I think needs to be looked at, or it ought to be looked at but I doubt will be, which is that where the big savings could really be made, in efficiency terms rather than allocative efficiency terms, I suspect, although probably a mixture of both, is in the sort of initiative which David's boss, Sir Michael Richard, has pioneered with this Total Place stuff, and looking at how public resources are actually used to achieve public purposes in particular areas. The problem with that is that it immediately runs into the extremely haphazard way in which public services are structured in the UK, and the historical accidents of the way some things are organised nationally and other things are organised locally, and some are part of local government when they are local and some are not part of local government when they are local, and that creates enormous problems. While Total Place I think may make some progress with the pilots it is doing, which are essentially driven by DCLG and the Treasury, if that was to make any real progress at local level, we would have to have new local government structures to actually make that work, and a new way of controlling all public services that are operating in a particular geographical area.

Q12 Chairman: David, you are definitely a Canadian, are you not?

Mr Halpern: I think we can be more Canadian than the Swedes, in the sense of our system of governance. It was interesting, as you know, we brought over the Canadians, both the politicians and also the senior civil servant who led the process in the early 1990s, and it was a very impressive story. Just for those who do not know the detail, obviously it did lead to quite differentiated cuts, surgical; in some areas, transport, cuts were up to 68% in transport, if I recall, other areas actually saw some increase in spend, like pensions. In that sense, it was quite differentiated, although it was very collegiate as a process. That is definitely one of the lessons you get. Nothing was signed off until everything was signed off, so the whole Cabinet had to agree to the total

package, and that seems to be part of the story. On the other hand, when we brought Göran Persson over a little while later, he was talking about a very flat approach, and we thought actually that does sound very sensible, because politically it is so powerful. But even the Canadians, if you listened to Marcel Masse speak, he was very much emphasising that partly why it worked, and indeed they were re-elected, was because of the spreading of the pain and all interest groups were kind of screaming. In that sense, the difference is not quite as dramatic as it seems, but a key thing, which Colin is alluding to, is: at what level do you go for the flat cut versus the differentiation? Our current system essentially of administration means you more or less at Treasury level settle with a department as a whole, and your ability to get into programme by programme, as you guys will know well, line by line analysis, is quite limited in the UK context. That sort of skews a bit where we are at and makes it more difficult. The Canadians partly settled that by having peer review of departmental spend, again driven in a collegiate way, but the point about Total Place, I think this illustrates it rather well, is what you are trying to do, you may go for an overall spread the pain, but at a level which cuts across the silos, so you can do something more intelligent than simply: let us cut a little bit off health and a little bit off education, and so on. A related point is that a simple devolutionary approach to it is not necessarily going to get you where you want to be. A very concrete example of something like the non-emergency telephone number, which everybody thinks is a great idea, we found it incredibly difficult to deliver such a thing even in the good times in the UK, let alone in the bad times. That is the trick; you can go for sharing the pain, but you do not want it just then to run down into these unreformed silos. If you do that, we know pretty predictably what we will get, and it will not be pretty.

Q13 Chairman: Andrew, I suspect you are an über Canadian.

Mr Haldenby: Yes, absolutely, because these services are different. In some cases, as we have said earlier, it is a question of whether government should be in this business at all. Let us take something like higher education, for example; we now have partial tuition fees, there is a higher education review going on, and I think we would all expect that that will see the tuition fee cap to rise. That would be an area of policy where we could move to government withdrawing from funding, and that becoming a private sector financed activity. That is one way of looking at it. But then, I think, looking at the other services, it is a question of productivity: where has the lowest productivity been, where has there been greatest increase in budget, greatest increase in headcount for least increase in outcomes? Well, probably top of the list would be the health service, so one would expect that the health service would undergo a greater period of change, and reduction in headcount and budget, than the other services. I think those sort of fundamental questions of the role

of government and then productivity will lead to a differentiating approach across each of the departments.

Chairman: That should get the Committee going.

Q14 Mr Prentice: I read in my papers somewhere that in Canada, the ratio of cuts to tax increases was seven to one, and in Sweden the ratio was two to one. In Britain, given where we are now, do you think there is scope for major tax increases rather than these savage cuts in the public sector that we have been reading about?

Mr Halpern: You will know the current Treasury figures suggest a ratio of 4:1 in the next Parliamentary period, but to answer your question, if you were going to go back to 2007, our analysis suggests that roughly you would do two thirds of it on the basis of reducing expenditure and a third of it you do by tax increases, noting you had a fall in revenue. That in broad terms is the answer. There is an interesting political twist to the story; when you look at the history of successful consolidations, governments on the left tend to do it more, perhaps surprisingly, you might think, by cutting expenditure, whereas on the right they have to do it through tax increases slightly more, and that may partly be about market credibility.

Q15 Mr Prentice: Talking about what is politically deliverable, the front page of the Daily Telegraph quotes Lord Myners today and tells us that 5,000 bankers earn £1 million, 5,000 earn £1 million. Large parts of the banks are now in the public sector, of course, we own 43% of Lloyds. Should these bankers in the public sector get their £1 million, or should those salaries be capped?

Mr Haldenby: No, I do not think they should be capped, because I think there should be a link between remuneration and performance.

Q16 Mr Prentice: You see that link, do you, between remuneration and performance?

Mr Haldenby: What is happening is the banks are having an incredibly good year, partly to do with regulatory change. That is the case. I do not think that the banking sector has settled down, I do not think it has reached a sustainable position, and that is the task that the Government has to achieve. Addressing bonuses and remuneration is a sort of symptom rather than a cause.

Q17 Mr Prentice: Do you see any role for tax increases, or do you think, in this economic maelstrom that we are in, the burden should fall on the shoulders of the public sector and the people who work in the public sector, apart from the bankers?

Mr Haldenby: Firstly, tax increases would fall on people who work in public services as much as anybody else. I would very, very, very strongly argue for the focus to be on spending. Firstly because what has happened to the UK public sector in the last decade is a dramatic increase in the size of budget and in the size of spending, so I think clearly that has to then be where the question is asked; but the second thing is the message to public sector

managers. Is the idea that we are going to raise taxes to support unchanged public services, or are we going to reform those public services? Just to tell one story about that, I happened to speak at the NHS Confederation annual conference in June, and it was the day, if you remember, that Andrew Lansley went on the Today programme to say that his budget was going to be protected, the NHS budget would always increase under a Conservative government, so all of his colleagues' budgets would have to be cut by large numbers. One of the chief executives of a PCT in one of the big cities said that she was furious about that, because she had been saying to her managers that the world has changed, and that budgets were going to need to be cut and they were going to need to do the difficult things, and they were going to need to change services and face up to the challenge of doing that, all the things they might have been postponing, now was the time to do it, and she felt Andrew Lansley had taken her legs out from under her by giving the impression that the money would always be there. I do think that there are excellent, excellent public sector managers who are waiting for a lead, and that lead includes saying there is no compromise on spending.

Q18 Mr Prentice: I will bring the others in in a moment, but you are recommending that we reduce senior doctors' pay by 10%, just like that, and a reduction of other senior managers' pay? Do you think that is deliverable, in the real world rather than on planet Mars? Do you think it is possible?

Mr Haldenby: The real world is one where authorities from the IMF to Mervyn King, the Bank of England, are saying that unless the UK has a plan to get out of this situation, then it will lose—

Q19 Mr Prentice: That is fair enough, you are not talking about a freeze, you are talking about a cut of 10%. That is fine, we understand that.

Mr Travers: The point I was going to raise is of course there is a case that can be made for higher taxes, the problem that we face here is that public expenditure as a proportion of GDP this year is going to be 49 or 50%, and taxes as a proportion of GDP will be about 33%. As the economy starts to grow again, the 49% will drop and the 33% will go back towards its 35–38%. As far as governments in recent times, if you look at the last Treasury Red Book, 38% seems to be a kind of ceiling. It would be possible to get that figure above 38%, that is tax as a proportion of GDP, but it would require leading politicians in the major parties to argue for higher taxes as a morally good thing, and it would have not to pretend that it can only be done, frankly, by a few bankers being taxed. It would require general taxes visibly to go up for people on all levels of income. Then it would be possible. But to pretend it can be done—I know you are not—by taxing bankers, it is just not going to be enough.

Q20 Mr Prentice: I know it is more than bankers.

Mr Travers: There is a perfectly good moral case to be made for raising taxes, but oddly, national politicians have not been making it very much, and

many of our taxes are very difficult to perceive, they are hidden. That is because taxation is unpopular. Politicians are much happier to talk about higher spending than they are to talk about higher taxes, as you know.

Professor Talbot: A couple of points. First of all, your Telegraph headline about the bankers. There is a general problem here, I think, which is pretty common across the Western world, which reminds me of a book published in the 1940s called *The Managerial Revolution*, which forecast the world being taken over by the managers; well, I think he was right, basically. The problem that we have, if you look at the ratio of earnings of senior managers to staff, across the private sector, in their businesses over the last 20 years, the ratios have absolutely skyrocketed. That is, I think, a major policy issue. Taxation is one way of addressing it, but there are other ways of addressing it as well, particularly about the governance of private institutions. But part of that has been a fall-out in the public sector, which is seen as a consequence, as a knock-on, I think, mainly, of some public sector salaries rising quite considerably and out of line with what is happening in the rest of the public sector, and certainly out of line with what the responsibilities of those managers are. That is one issue. There is a second issue about the health service, which is the key problem with the health service is clearly that we spent a lot of extra money on it, according to the ONS figures, with a fall in productivity as a result. My personal view is the main reason for that fall in productivity is twofold. One is the constant what has been called reorganisation of the health service. When I talk to groups of health service senior managers, their main concern is which job are they applying for next in the re-organised Trust, merged PCT or whatever it is that is going on. The other is the contracts for GPs and consultants, which were disastrous in their consequences. I have been in two GP practices in the last couple of years, and virtually all of my doctors are now part-time because they are earning the same amount of money as they did when they were full-time, and they do not have to do out of hours call-out either. That was the second point. The third point I wanted to make was just about this general overall picture. I would like the Committee to bear in mind the magic number 43—not, as Douglas Adams said, 42, but it is 43; the average proportion of GDP spent on the public sector over the last four or five decades has been about 43%. Before the crisis hit, we were on, guess what, about 43% of GDP. It was not actually extraordinarily high by historical standards, it has been much higher. The highest it has been in the last 40 years was under Margaret Thatcher, and the lowest was under Gordon Brown as Chancellor.

Q21 Mr Walker: When under Margaret Thatcher? 1979?

Professor Talbot: No, not 1979; the middle of the recession in the early 1980s, when it went up to nearly 50% GDP.

Q22 Mr Walker: In the first Parliament.

Professor Talbot: In the first Parliament, yes.

Q23 Mr Walker: Clearing up the mess of the last Parliament.

Professor Talbot: It is not playing with statistics. My point is this: for the last couple of general elections, we have basically had more or less political consensus that that is about the right proportion of national wealth to be spending on public services, and both the main parties have been working at keeping it at about that sort of level. We have now gone into the situation, because of the crisis, where, as Tony said, it has skyrocketed to 49–50% of GDP. Some of that will come back down as a result of economic growth. The key political question that both parties ought to be addressing is where do they see it being in five years' time or 10 years' time? Do they see it back down to that historical average of about 43% of GDP, and then we work out how we divvy up that money amongst the different public services, or do they see it being radically different, either higher or lower? This is one of the strangest general elections, I think, that we are heading towards at the moment, where we as electors have no idea what the main parties are saying about that, because it is totally unclear what they are saying. You could read some of the Conservative statements to suggest they want to move towards American levels of public spending, about a third of GDP, and some of the things that New Labour has been saying tend to suggest that we might hold public spending at much higher levels than 43% for some time to come. I do not know, and I doubt most of the population do when they go into the polling booths in six months' time.

Q24 Chairman: I think Roy Jenkins once suggested 40% as a target and got into trouble, but everyone is terrified of talking about numbers in terms of the size of the stake.

Mr Halpern: I was simply going to try and answer your question directly, in the sense that in the history of consolidations, and a lot of them have been done in the last 40 years and across countries, if they are strongly tax led, they fail at a much higher rate, and it is precisely for the reason that I think Andrew is alluding to, which is that it lets you off the hook doing lots of other things and you do not sort out your basic problems. That said, very powerfully said by Göran Persson, the Swedish PM who took them through this cycle, part of the story of sharing the pain, given that most welfare benefits and much of public expenditure disproportionately benefits the less advantaged in society, the quid pro quo of sharing the pain generally means tax increases for the most affluent and able, and it is difficult to see politically, in my view, how you would be able to do the kind of things you would need to do in public services without also sharing the pain in terms of the most affluent.

Q25 Mr Walker: Would you then therefore advocate that the 50% tax band due to come in is probably not high enough on the highest earners?

Mr Halpern: Forgive me if I avoid the very specifics, but the general point would certainly remain, you would have to say: in what form would that sharing the pain be? What is the equivalent of a squeeze on the public sector?

Q26 Chairman: Andrew, I think you are still back on the previous conversation.

Mr Haldenby: If we are going to penalise higher income people, then another way of doing it is to question the benefits that they receive. You do not have to introduce a whacking great tax rate which would be hard to remove, but you could take away subsidised student loans, you could take away child benefit for better off people; that may achieve the purpose of being tough on richer people, but it would also help to lower the public spending burden overall.

Q27 Mr Prentice: This is positively my last question for the moment: would you be in favour of the Opposition's policy of freezing salaries in the public sector for people earning more than £18,000?

Mr Haldenby: No, because, again, that seems to me to be a sort of short-term idea, which is a bit like stopping bonuses to bankers. The point is that remuneration should follow performance. If we are going to talk about the public sector workforce, what seems to me to be essential is to address the headcount, the numbers, as well as the remuneration, and where does the public sector workforce have to go in the end? It certainly has to become more productive, which is, I think, shared across politics, we want a higher, more productive public service. That vision then is really of a smaller workforce on higher wages, that is the kind of higher productivity workforce that you are going to get. I am much more critical of the Opposition's pledge to protect health spending forever, because it seems to me that there must be—

Mr Prentice: Yes, you made that point.

Q28 Kelvin Hopkins: If I can ask the obvious macro question first of all: cutting public expenditure at this particular time would surely just drive us deeper into recession, and have the opposite effect of what we want?

Mr Haldenby: There is another view to that, which is that there is a greater risk to not doing it. The risk to not addressing the fiscal deficit is that the markets will take a much lower view of the economy, they will not have confidence in the willingness of government to maintain a sustainable economy, Britain loses its top credit rating, we become seen as a second rank economy, which has damaging consequences for investment; there are also particular problems about having to pay higher interest payments on a skyrocketing national debt. So suddenly, by postponing cuts, Britain's economy is really a lot weaker, a lot weaker, with much lower investment, much lower employment. So there are two options here, and I very strongly think, and again as David has said, the evidence from many of these packages

with other countries is that getting a grip of public finances actually restores confidence, and enables growth after that.

Q29 Kelvin Hopkins: We have been asked not to get into the economic debate, I would love to do that, but I will just say that if you are going to invest, then in an economy which is indulging in blood-letting and reducing demand, you are not going to invest in that economy; one with rising demand, you might actually put some money into it. But we have been warned off that discussion.

Professor Talbot: Just very briefly, whilst I accept all those arguments about markets possibly taking fright, two things I think need to be borne in mind. One is that they have not, because I think, broadly speaking, the markets have recognised that what has happened has been so extraordinary, in the total collapse of income from taxation from the financial sector as a result of the nature of the crisis, that that has had a profound effect on the public finances. The second is that they are waiting to see whichever government it is has some clear strategy for the medium to long term to reducing the accumulated debt that we now have. Frankly, as long as the Government has that, what it does short-term, in the next year or two, I do not think matters that much to the markets. I think the markets will be perfectly happy to go along with where we are at the moment. If they were not, frankly, I would have expected them to have reacted much more badly by now to what is plain to everybody about the cumulative size of the national debt, as well as the annual deficit, and they have not. I think that is because they recognise that whichever government it is, there will be a medium-term plan; they may be different in terms of how quickly they do it, but I suspect actually they are going to be an awful lot closer than the political rhetoric at the moment would suggest.

Q30 Kelvin Hopkins: It is suggested that the Government is having no difficulties in selling gilts and raising money at the moment, so clearly there is not a fear in the markets that we are a busted flush for the longer term.

Mr Travers: That is true. I think the only difficulty with that analysis is that markets are fickle and they do not signal in advance that they are about to panic or change their minds. So it will be all right so long as it is all right. I am not an expert on the markets. As my colleagues have said, in a sense nobody is an expert in this, because it is impossible to judge whether withdrawing stimulus, and roughly £14 billion worth of lower borrowing would be equivalent to 1% of GDP is the ready reckoner as I understand it, so there clearly is an effect of reducing borrowing and spending sharply. On the other hand, there is the downside risk that the markets might decide—and you can see political instability in the UK, for example, a hung Parliament, would make this a much more problematic issue than a powerful government of one party or another. So these things are very, very difficult to judge, and we have seen again and again in the last 18 months that external

events can change things suddenly. I think nobody knows, is the real answer. We are not economic experts in all of this, but frankly nobody is any more.

Mr Halpern: There are questions about what the markets will tolerate, and I think that is fairly well rehearsed, although one caveat, of course, is that a lot of the international buyers are not so present, and we are buying a lot of our own bonds, you could argue. So you might say it is not fully tested in the current situation. But still I think the basic story holds true. Your point is not only about the markets, but a real economy. The markets will tolerate various kinds of economy, some of which we might not want to have in terms of the level of decimation. That suggests, in the short-term, a pretty strong argument to carry on propping up the economy. A couple of caveats, though. One is that in some areas of government spend, public servants have been surprised at the extent to which we are not cutting, we are continuing to inflate, projected expenditure increases are continuing to run through. A lot of it is about the timing, of course. If we try and act, realistically, given the political cycle, by the time these things feed through, you are going to be at least a year or so off anyway, so hopefully you are in a stronger economy. In terms of the broader story, it does look like you can do it, you can get these expenditures down, and you can get good prospects, and indeed arguably marginally better prospects for economic growth in the years to come.

Q31 Kelvin Hopkins: I will come back to that. The TUC is suggesting that the kind of cuts that are being suggested would raise unemployment by 40% in towns like Leicester, Middlesbrough and no doubt Luton, my own town, and this would actually reduce tax revenues and increase public expenditure on benefits. That has a negative effect, and makes the deficit worse. Surely the logic is to try to drive employment upwards and not increase unemployment. That would reduce the deficit and actually make the markets more confident.

Mr Halpern: I believe Heseltine was once asked about it in relation to renewal, urban regeneration and so on, and very similar arguments were played about: we should boost employment, and so on, and get more people going. He said: why do we not give people spoons instead of spades? The point is, the implication of a lot of this is you are going to have to do some restructuring in relation to aspects of public services, and there are some deep efficiency gains to be had, where you could do less for more. That does imply some employment shift across the economy, including the public sector. But you are absolutely right, there is clearly a very tricky issue of timing about when you do it, and now does not seem to be the right time to do it. That said, again, history tends to show the most successful fiscal consolidations that occur are substantially triggered in the year after an election, and they normally take about three years to substantially work their way through.

Q32 Kelvin Hopkins: I have a dozen more questions which I would like to ask, but just one more perhaps: is there not a moral question involved here too, that

we are asking working class people who have paid PAYE to take a hit for the crass mistakes and greed of bankers, for whom we are being told we must not raise their taxes?

Mr Halpern: I have touched on that point already, I think you do have to spread the pain, but what drags most countries into it—actually, we have moved into perhaps the reality of it faster than most countries have done in the past, to look at the consequences if you do not act. At the moment, our debt payments are £28 billion. Obviously they are going to rise very substantially, and if interest rates start to move at all, then even more substantially. What normally draws countries into having to resolve the issue is they are faced with exactly that kind of choice of the difficulty. On the other hand, they say: what happens if we do not? Then we will have to start doing really severe cuts which will be that much worse, we will be crucified on the back of this.

Mr Haldenby: Just a couple of things. One is it is not just these this kind of discretionary fiscal policy changes that determine demand in the economy; a much more important factor is monetary policy. While we have interest rates right on the floor, that will do more than anything to keep the economy going, but also non-discretionary fiscal policy, so benefits, the so-called automatic stabilisers. That is why public spending has suddenly gone up to 50%, there is this huge additional weight of spending. That will go on. So just to say, I think the implication that you must postpone anything of this kind in order to prevent economic activity stopping, full stop, is not true.

Mr Travers: This precise point is in response to Mr Hopkins' question and observation. I think I am right that there is a map in the Financial Times this morning of public sector employment by local authority area, which is very interesting, but it does point to the reality that public expenditure cuts, when they come, if they are public spending cuts rather than tax increases, will have a differential effect, because the public sector is different. The public sector is effectively an industry, and in some local authorities it is much more heavily present than others. Oddly, here in the City of Westminster the public sector, despite the existence of the Civil Service, is a relatively small part of the economy, but in many north eastern, Scottish and Welsh constituencies it can be up towards 50% of employment. So the impact of cuts in public employment, when and if they happen, will have a very different effect from place to place, which is an issue that the Centre for Cities has looked at in a little detail and produced figures for where it is most likely to be worst.

Q33 David Heyes: My question follows nicely from that. There is another aspect from that, is there not, which is the possible impact on morale, the ability of public sector to recruit and retain quality staff, experienced staff, and in that way potentially downgrading the quality of the public service. For any of you really, what is your sense of the likely

impact on staff morale, on issues like recruitment and retention, for the kind of major cuts that we have been speculating around today?

Mr Haldenby: We are publishing a report on Monday on public sector workforce and its contribution to the reduction in the deficit, and the evidence on morale and sickness absence, for example, job satisfaction, views of quality of management, is that actually the public sector is at a lower level; people in the public sector tend to take longer sickness absence, have lower job satisfaction, have lower morale, have a lower view of their own organisations. It comes back to what I was trying to say earlier about if we can reduce the size of the public sector and make it more productive, and I think reform it so that people working within it are more empowered to achieve the changes they want to make, I think that would improve the working experience of working in the public sector.

Mr Halpern: I think it is an absolutely fascinating question. I was certainly very interested to know what happened in previous times. Of course, our own history of Britain is not entirely a happy one, given the "winter of discontent", but in Canada especially, one of the people we brought over was Jocelyne Bourgon, who was effectively the equivalent of Cabinet Secretary. We asked, did it not decimate morale, what happened, given that in the Canadian case central government was planning cuts of roughly 20%, and her argument was: look, what happened, for several years, in fact, you can argue for almost a decade, they were trying to squeeze things down through efficiency gains, salami slicing, and actually what that did was that was totally destructive of morale. She argued that what happened is that people were so relieved that decisive action was finally taken, that in fact staff morale moved up substantially through the late 1990s. Those are the ones who are left, you can argue. The deeper question is: what happens to everybody? It goes, of course, to your point about what is the human cost of this? We are not in a society and world where there is not lots of work to do, there are many valuable things to do. I will just take you back to a very concrete example of the non-emergency number; when New York moved from it, it had more than 4,000 different numbers that the public would call, and it moved to a single number and integrated call centres. Clearly there are efficiency gains, that means less staff in call centres or whatever, but it also releases people to do more productive things, you hope, either in the public sector or in the wider economy, and this is the deep trick that we need to achieve.

Professor Talbot: Several things. One is, along with slashing budgets on an across-the-board basis, one of the typical reactions in these sorts of situations is to look at staffing numbers and want to cut the numbers, and that potentially is extremely damaging, because you cut the wrong people in the wrong places, and you have voluntary redundancy schemes, which means the best people leave because they are the ones that can go and get jobs elsewhere, and so on and so forth. It is quite interesting that in the late 1990s/early 2000s, most OECD governments

that had had controls on numbers across public sector staffing abandoned them on the grounds that they were extremely blunt and ineffective instruments. That is the first point. Second, Andrew's point about these smaller but better paid public services, I am afraid I just do not see that. There are large chunks of the work that is done in public services which is taken out of the market quite deliberately, which are relatively low-skilled jobs; emptying bedpans, being teaching assistants, plodding round streets protecting people are jobs which are never going to be highly technological. You are not going to be able to make huge savings through lots of capital investments, or by skilling people up. I know there is a general tendency at the moment for everybody to want a degree to do anything. All the professions are going for it, we have just seen the nurses, and now the social workers want to, and so on. Sure, I can understand why they want to do that, but the truth of the matter is there is a lot of stuff that gets done in the public sector, by very large numbers of public sector staff, which is never going to be extremely well paid, because of the nature of the work involved. I just think we have to recognise that. That is the reality of it. It is one of the things that also makes it very hard to drive very large productivity savings in the public sector. By and large, if you look at the economy as a whole, those areas where you get the biggest productivity gains are going to be those that are most capital-intensive. The public sector is almost entirely in the service sector and therefore is of low capital intensity, and therefore it is always going to be more difficult to drive productivity changes at even the average rate of the economy. It is something I have been arguing for years, that some of the so-called efficiency targets that have been set are just completely unrealistic for the nature of the organisations that we are dealing with.

Mr Travers: Interestingly, I think there is no doubt that we are currently in a sort of phoney war territory in all of this, because public expenditure this year will increase in real terms, and the Government's plans for next year are that it will increase in real terms. The local government finance settlement made last week shows a number of counties getting 4-7% grant increases in cash next year. So we are talking here about a world in which the Government and the main Opposition party find it extremely difficult to spell out what is going to happen, and this Committee is ahead of the game in that sense, but where public sector managers are behaving as if all the announcements of the cuts have been made. If you talk privately to chief executives in local authorities and health authorities, they are preparing with gusto and quite relaxedly, actually, to do all the things we are discussing. So the Institute for Fiscal Studies and the chief executive of the Audit Commission and others have said it is all going to be terrible, and the public sector managers and their finance officers have picked up that story. Politicians are sort of left out of all of this, because they do not comment on it. So what I think you will find happens is that senior officers are currently leading this process in advance of anything actually

happening. I think that points to something my colleagues have said already; if it is to be done at all and it is to be done well, it will require politicians to lead it, to say what is going to happen and then, as it were, to provide leadership to the people they employ, and that stage is missing at present.

Q34 David Heyes: That is certainly true of the people I speak to in my local area. The chief execs of Primary Care Trusts and hospital boards, and the chief execs in local government are busily planning away and just taking it for granted it is going to happen. They are fazed when challenged, or I try to put a counter point of view. Just one more point on this. Part of the offset against the sort of low motivation, low morale in the public sector is decent standard public sector pensions. That is another area that is coming under attack and is potentially being lined up for reduction in the value. I just wonder what impact that is likely to have, how appropriate it is that we do that and, linking it back to my previous question, what impact that might have on morale and the quality of service.

Mr Haldenby: You described it as an offset.

Q35 David Heyes: I speak as a former public sector worker. Maybe I still am a public sector worker, I do not know. With a good pension. I remember one of my colleagues saying: this job can be dire sometimes, but at least we have got a good pension to look forward to. That is very common, right across the public sector.

Mr Haldenby: Public sector pensions is a strange subject. Again, a bit like we were saying about managers, everybody assumes that something has to be done about them, but no one quite knows what. There are these enormous headline numbers about the total liability, which is many hundreds of billions of pounds over those years, but the real question is what is the annual cost of servicing them, and my understanding is that it is several billion pounds, somewhere between £5 billion and £10 billion a year. So the question is, faced with a structural deficit of whatever it is, £120 billion, does one have to address a cost of that size, and I think probably one does, yes.

Mr Travers: As somebody who has a university pension, as I suspect Colin does, I ought to declare that interest first, it seems to me that public sector pensions are going to get caught up in a wider debate, of which bankers and all of that are also a part, of fairness as between different groups in society, people who are in work, people who are out of work, rich, poor, and so on, which is a bigger issue, a cultural issue, which is almost certainly changing around us as we speak, in ways we will only understand when we look back on it. So big have been the changes to our economy, the financial sector and politics in the last 18 months that things will happen of that kind. So I think that public sector pensions will feature in that debate about fairness over time, fairness between sectors and so on. There would be ways of protecting the concept of pensions of this kind, but they are going to require give and take, and there will be give and take, I suspect, in the

areas of how much employees contribute, and also when the pensions start to be taken. I mean, those are the ways where compromise could be achieved without dropping the concept of these kind of pensions, which everybody agrees it would be better if the private sector had more of this kind of pension, but the issues of fairness are going to be sorted out partly because of politicians reacting to societal pressures that have to do with understanding the fairness between different groups.

Q36 David Heyes: But the question for this Committee is: to what extent does that impact on the quality of public administration?

Mr Travers: Clearly, public sector pensions and their relative generosity will make it possible for the public sector to employ higher quality staff and/or pay less, and Colin has referred to that issue, than would otherwise have been the case, and I think they need to be seen in that way, that they are part of the overall package of why people work in the public or private sector.

Professor Talbot: Just a general point. I absolutely agree with Tony, I think the key issue of this is going to be perceptions of fairness, and the psychological contract between public service workers and their employees, ie the rest of the public, has been in the past of one form, which included slightly lower wages than you get in the private sector and a better pension, and I have worked in several parts of the public sector and that was always the case in the different bits of it, even for university professors. If we are changing that contract, then we have to think about what—I think you are quite right about what the morale effects will be in the public services, and I think alongside that you have to fit that into a much broader picture about how society addresses what has clearly been a major crisis, which has caused us major long-term economic and financial problems, that have to be sorted out over probably a 10, 15, possibly 20-year period to recover from completely, what we have been through in the last couple of years, it is of that order of magnitude, and generally how we deal with that, in terms of policy options, I think is going to be absolutely fundamental, and I think fairness is going to be fundamental to that. We are concentrating at the moment on discussions about shrinking the public sector, which I think probably in the short-term is going to have to happen, but if you look at this in a more long-term perspective, I think there are some quite interesting trends, which is, roughly speaking, from the end of the Second World War up until the mid 1970s there was a general trend towards more collectivist solutions to things, and this was across the Western world, not just in Britain. We then had the oil crisis, and so on, we had a short interregnum, and then we moved into a phase which has lasted about 30 years where, by and large, individualist solutions to things, and “markets work, and markets are going to triumph and solve all our problems for us”, have been the dominant view. The question is what happens after the crisis we have now had? Are we going to move back to just saying, well, markets will solve everything for us, will they not? I personally

doubt that that is what is going to happen. Or are we going to move back towards some more collectivist view of saying, actually, even if we have a slightly smaller state, we do want to make sure that people are treated fairly. The other point I would make on this is that the research evidence now on levels of equality/inequality in advanced countries, causing major social, health and other problems, the epidemiological data on that is absolutely clear, that those countries that have the largest levels of inequality have the largest levels of social problems, of health problems, of educational problems, not just affecting those people who are poor, but affecting those people that are well off as well. You know, the evidence on that is quite clear. I suspect all of that is going to feed into a discussion about how do we deal with the consequences of this crisis in a way which is seen as being fair to everybody, including public sector workers?

Q37 Paul Rowen: Following on from what you have just said, Colin, is it a case of asking public services to do more with less, or is it an easyJet model, a basic with extra entitlements?

Professor Talbot: First of all, is it going to be a question of asking public services to do more with less? Yes, it always is. Even in times of plenty, we ought to be asking public services to do more with less, in the sense that all of human progress has been about doing more with less; that is what we do, we make stuff easier to do, and produce stuff more effectively. To that extent, public services always have to be seeking improvements in efficiencies. Secondly, it is clearly the case that large scale organisations, in both the public and the private sector, it is not just a public sector problem, very large scale organisations always have a tendency towards becoming more and more sclerotic, cumbersome, bureaucratic, and periodically have to have bouts of trying to sort themselves out. You can see exactly the same thing happening in the private sector with large organisations, they go through these periodic attempts to slim themselves down and make themselves more efficient. So yes, that is going to be an important element of what is going to happen. I do not think, however, we can exaggerate what is possible on the efficiency side. As I was saying at the beginning, I think strategic decisions will have to be made if we are going to make cutbacks in the amount of money we are spending, devoting to the public domain, of the order that people are talking about at the moment.

Q38 Paul Rowen: So do we go for the easyJet model? If you go into hospital, yes, you will get your medical treatment, but you provide your own food, or whatever.

Professor Talbot: I would be extremely cautious about that, for several reasons. One is, coming back to the fairness issue, I think there are going to be some important issues of fairness because, of course, if you do not provide things like food for people in hospitals, some people can afford to use the Marks & Spencer’s food dispensary that is going to be going into every hospital, apparently, and some

people cannot afford to do that, and they will be having to nip out to McDonalds to get their lunch. So there are going to be fairness issues involved, and that relates also to issues about taxation, because the point about public services largely is their universality, in the fact that everybody gets them equally, on a reasonable basis, and people pay their taxes on that basis. I think the more you move to a situation where it is not clear you are getting the benefit from paying taxes, people will become more reluctant to want to pay taxes for public services, so I think that is a major problem.

Mr Travers: If we just aim off for the term “easyJet model”, which I can see has become a kind of matter of ritual battle between different ideological positions, just aim off for the words, the idea that, as I understand, lies behind this idea is: would it be possible in some parts of the public sector to offer higher standards of service in a way that at best would cross-subsidise the general service, to liberate more money for the service? I think if you look at it like that, firstly, it is not as if it does not happen already, it happens in the NHS already, in dentistry. In dentistry, oddly enough, we have all of us accepted co-payments, because they are there, or prescription charges. Second, the Government itself has introduced this at the Passport Office, where you can either get a standard service, slowish, or passport overnight for £100-odd, I assume that cross-subsidises the general service, and of course with first class rail travel. So it is not as if this idea does not exist in the real world that the present Government currently operates. It does. It would crucially depend on whether this was a way of producing more money to protect the core service, and it would be a very different thing if it were to allow some people to get a proper service and other people to be left with a bad one. I think we need to be a bit more nuanced in how we interpret the easyJet model if that is what it is meant—

Q39 Paul Rowen: But easyJet and these low cost airlines are very popular. BA is struggling.

Mr Travers: Indeed. I did not want to go into that.

Q40 Paul Rowen: Is that going to allow public services to deliver?

Mr Travers: I did not want to get tangled up in civil aviation. You are absolutely right, although the budget airlines induce quite a lot of critical comment, they are also very popular, which is itself a confusion, even within civil aviation. They are doing well, and the high quality, traditional airlines less well. But the point I am making is that as far as the public sector and the structure of the public sector is concerned, I think that the question that we are really asking here is: are there ways of getting people to pay more for services that would cross-subsidise the core of the public service, at a time when money is going to be short? I think that is the key issue. As I say, I think it would be very unlikely for the NHS not to consider issues such as co-payments, they have already been debated, and remember, local authorities are under pressure from the Audit Commission to increase their charging anyway. So

the public sector already has all these elements in it. I think the issue, looking ahead, is can they be used constructively to raise more money for the core of public provision, at a time when taxpayers’ money will be short?

Mr Halpern: Will we see more of it? I am sure we will. Remember, easyJet also has other kinds of big changes it introduced, which is why it beats BA. Now you do not have to check in in the same way, you can do it online, and there are lots of other gains that come through such a system. Contrast that, for example, in relation to our benefits system, where we have hardly gone online at all. So there are plenty of examples even within it where you can try and squeeze out quite substantial advantages. I think the more profoundly interesting one, in terms of a public admin point of view, which I am sure your constituents must illustrate to you on a weekly basis, is you will routinely come across services duplicating and falling over each other. Indeed, an area I spent a long time working on in government was social exclusion, where you saw it in extreme forms. You could have 10, 12, 15 agencies involved in a family, spending a lot of money, with very little effect.

Q41 Paul Rowen: Is not the problem there that the centre of government, whether it is here, is reluctant to hand over control to localities to enable them to make the sorts of savings and changes which could be made?

Mr Halpern: Absolutely. That is why I think you are absolutely right to focus on it. There is a substantial public admin issue at the heart of this, and one of the reasons why we got very interested in Sir Michael being involved in Total Place is because he very passionately believes that on the basis of that evidence we can do a lot more for less.

Q42 Paul Rowen: It always strikes me that the NHS is the biggest communist state that we have. It is the most centralised, most controlled, multi-layered—you know, you cannot do anything in Rochdale without some civil servant here actually signing it off. Somebody earlier on talked about the multi-re-organisations that these things have. How do you actually go about things, without having to go through yet another whole series of re-organisations where they all re-invent themselves and get paid more along the way?

Mr Halpern: We do start to see that. There are a couple of PCTs which have now merged with local authorities, and we see it particularly at discussions, indeed in Total Place 2, around adult care and social care, where the budgets are very little overlapping today, and yet there are very substantial gains to be had, both for patients. Chronic conditions, very similar characteristics. The half-full version is there are lots of grounds to think there are things that we could do, but it does certainly involve a letting go in a relatively silo-based system from the centre, but also not a simple devolutionary settlement. The likelihood is that what we will see is some areas will get the hang of this. As Tony and others have illustrated, some public service managers have already been quite imaginative about this and they

will leap forward, and others will not; others will be the worst kind of the Ryanair example you are thinking of, with general degradation, even without imagination.

Mr Haldenby: On the easyJet idea, I think it is very, very unlikely that there will be an enormous debate about how that principle could be applied across the public sector, to the level of things like hospital food, which clearly would not be right. What is more likely to happen is a continuation of the things that are already happening. For example, in higher education, as I was mentioning earlier, there are already tuition fees, and we will probably see those increase; in pensions, there will be a compulsory private pension under the Adair Turner proposals, in 2012, I think. We will have that, and that might—

Q43 Paul Rowen: Personal accounts.

Mr Haldenby: Right. In the NHS, as of last year, it is now legal to have co-payments, particularly thinking about certain kinds of cancer drugs, and that might be extended. So there will be a general increase of that kind.

Q44 Paul Rowen: In terms of the size of the public sector, if we are going to shift this £120 billion deficit, what proportion of cuts do you see us having to make? I know some of you said we should not be doing that, but at the end of the day, you have to have a figure to aim for and you have to know when you have done it.

Mr Travers: For broad orders of magnitude, if we are starting with a £175 billion debt, that will shrink, because we are all assuming the economy will start to grow and continue to grow in all of these discussions, which itself is a brave thing, but we have to assume that; it starts to grow in 2011 and then grows at trend every year thereafter. That would start to shrink it in both directions, it would bring down public expenditure and it would increase tax yields, so the borrowing figure would shrink. There is disagreement, and I am not sure we are exactly the right people to have here to say how much of this is structural, but clearly, say, half of it is structural.

Mr Halpern: Our estimate is 90 billion.

Mr Travers: Right, 85–90 billion is structural. We are talking about, if it was two thirds/one third, 30 billion on tax and 60 billion off spending. It is those orders of magnitude, I would guess.

Mr Halpern: It is a political choice. Of course there are big political choices in here, but if you are saying get back to roughly 2007, which we were happy about, Tony's figures are exactly right, that is what we are talking about.

Q45 Paul Rowen: How does that equate in terms of public sector jobs, the size of the Civil Service, or is it more outsourcing and that is delivering things cheaper?

Mr Travers: Again, these are heroic, back of the envelope kind of numbers, but 60 billion is very broadly equivalent to, I will put it that way, 10% of public spending. If public spending were to be reduced by 60 billion, that is 10% of today's public sector. There have been some analyses done that

suggest that, in a sense, there would be a sort of mountain of public spending, and public sector employment would rise up to a zenith today, and then fall back to roughly where it was in 1998–99, if this happened, but I think Colin made this point indirectly and David has made it, that we are talking here about getting public expenditure back to levels that were probably realistically in the early 2000s. That is what is going to happen. So it is not all the way back to some earlier age, but it is bringing it down to that level. That is what we are talking about.

Professor Talbot: The size of the public sector workforce compared to the rest of the labour force has actually been remarkably stable over the last 20 years or so. It went down slightly under the last Conservative government, down to about 19% of the workforce, and it has gone up under the Labour government to about 22% at the moment, which is actually a very small variation, given the amounts of changes in spending patterns that we have seen over that period. But the rough, very, very rough ratio is that public sector employment tends to be about half of whatever public sector spending is as a proportion of GDP, so it varies a bit. The question will be, the 60 billion that would come out of saving on public spending, how much of that is saving on the half of public spending which goes on services, which employs people, and how much of it will come out of the half—

Q46 Paul Rowen: How much of it would be on the easyJet model? If you say we provide a base level of service, of that 60 billion are you going to say 20 billion will be through greater income streams or whatever?

Mr Travers: I think that is too many hypotheticals for us.

Professor Talbot: I would say I think it is extremely unlikely that you could generate income from the sort of easyJet, “easyCouncil” model, that would in any way make a huge dent on that. There is a big difference between saying we have some areas at the moment in public services which have elements of co-payment in them, to saying that we move the whole of public services and the core of public spending on public services to co-payment models. You are talking about a quantum leap in terms of change of the way things would have to operate, and that would raise all sorts of political problems. The point I was trying to make, and I will put it in the airline terms, how long would people tolerate paying BA prices for easyJet services, in terms of paying BA levels of taxation for easyJet levels of services? Not very long, I suspect.

Q47 Mr Prentice: Are people ready for a fairly big extension of means testing? Because Andrew has said universal child benefit should go, universal winter fuel allowances should go, free TV licences are just a gimmick, and so on; there is a long list. Do you think in the present climate, given what you have said about fairness, that the people out there would be ready to accept a big extension in means testing?

Professor Talbot: I have no idea. We do not know. I do not think anybody knows at the moment.

Q48 Mr Prentice: No, but you think about these things all the time, you must have a view.

Professor Talbot: My personal view would be that I suspect there are some areas where people would be tolerant of those sorts of changes, if they saw it as part of an overall package which was leading towards a fairer society and they were being asked to make their contribution towards it. But, frankly, middle class families losing things like support for childcare may well tolerate that if at the same time the bankers that you are talking about were taking a hit, rather than at the moment we are in a ludicrous situation where, frankly, they are getting paid for failure, and us having had to bail them all out through the taxation system. I suspect, if you start saying to middle class parents, "Would you mind giving up your childcare allowance to help us make sure that the people in RBS who we publicly own get their bonuses?" which is in effect what is happening, they might be just a little bit miffed.

Q49 Kelvin Hopkins: The real route to redistribution is through the taxation system, not means testing.

Mr Travers: I think this is trading off different evils, because what we are coming round to is that unless politicians are prepared to say "We want higher taxes for all", and have a bigger stake permanently, then we are broadly agreed that public spending will to some degree have to fall. There are various ways of doing that, and all we are doing is fleshing out the various possibilities, and these are to some degree alternatives. Means testing benefits would substantially reduce public expenditure relatively quickly, but it has a number of risks, not the least of which it might lead some more well-off people, as it were, to feel they were getting nothing back out of the welfare state. That is a risk the previous Prime Minister was always exercised by, but there are others besides we have not talked about. Massive asset sales, that is another way of doing this; one-off, it is true. So means testing, efficiency savings, asset sales, putting up taxes, they are all to some degree charging, they all compete for doing the same thing. Now I think, in a sense, what you would expect most politicians to do would be to mix and match from among all of these, because the more you mix and match them, the less you have to do any one to the exclusion of all the others.

Q50 Julie Morgan: Surely one of the disadvantages of the means tested benefits is the low take-up. If you are talking about fairness and reaching people, a lot of the means tested benefits have very low take-up, whereas the universal benefits do absolutely reach everybody.

Mr Haldenby: Since we looked at it, some of the means tested benefits have very high take-up, 95%, so it is partly about the design of that. As Tony says, it is the lesser of two evils. Means testing has all of the obvious disadvantages, but take something like child benefit, the total cost of that benefit is over £10 billion a year, so there is obviously the idea there that

some people receiving the benefit do not need the £20 a week for the first child, and that is why we raise it as an idea.

Q51 Julie Morgan: It is balancing, is it not?

Mr Halpern: I was going to make the straightforward point which of course is the big area of public spending, at least a third or so, which in principle you could cover without having impacts on jobs, which causes benefits, which includes pensions and all kinds of things, not a particularly pleasant area to start picking at, but you might decide—because there is obviously a lot of money in that.

Q52 Paul Rowen: If you take most of the benefits, they are already below poverty levels.

Mr Halpern: Absolutely. Contrast with Sweden, which did a lot of cutting. If you look at the history of these things, you may say Canada had a lot of inbuilt subsidies, they were easier low hanging fruit, Sweden had a more generous benefits system. What is the equivalent for us? Most people would probably say it is public services, that is the area which we have expanded most rapidly. The question is: can we do that? What would that mean in job terms? If you move to a model, for example, long-term care, where you use more telemedicine, et cetera, what does it actually mean? It does mean some people doing less things than they are doing now, but it also might mean new things; people might be working in new higher tech forms of medicine or chips. There are possibilities, but there is a lot of pain along the way too. We are putting out a report on this, pulling together what we have been doing together on this for the last six months or so, after the PBR, and I think the key thing, and it is very much a public admin one, is what are the sorts of changes that we can make to the way our government operates that mean that we do a better consolidation, rather than one that meets the headline figures but actually has lots of pain along the way? That is what we are in the business of. It turns out a lot of that hinges on the detailed ways in which our government operates from top to bottom. We have this window of opportunity where we can try and get some of those changes in place. They are the ones that we really need to zoom in on. Can I just offer a few thoughts where I think we will move towards? Obviously it starts at the top, it is a certain collegiate-style approach, where you have to reach a collective settlement about your relative priorities. You have to do that, and you have to reach a collective settlement at Cabinet level, and all the tough things it involves, and not allow it to be done on a Treasury, by department, sort of silo base. That would be a disaster. There are ways you could reinforce that. We are quite keen on, as indeed the Cabinet Secretary is, I know, on cross-cutting budgets, where you have a powerful minister who holds a large budget for an issue such as some youth issues, for example, but who does not actually sit in the department. Then they drive, as it were, a different perspective on spending. Of course, you then have to do that at local level, which is a point being made repeatedly. We are relatively upbeat

about the evidence coming from Total Place about the lessons. We have some things in place already, like the common area assessment, it starts to move you towards looking at it as a whole, as opposed to testing each service individually. But a lot of it will involve Treasury and others letting go, and we are going to have to let some local authorities and areas, and PCTs and so on, do their own thing, and yet they have to do it in a way which is kind of connected, imaginative. Could it mean devolution beyond that? We think there is a lot of promise in individually held budgets. The number of budgets we have said we are going to do, more individually held budgets for problem youth and so on, actually our progress on it is quite limited. Social care, we have 3,500 people on individual budgets, but we think there are 1.3 million who could hold them. That is what we have to do. If we could get into a world like that, and create the kind of platforms for that sort of public service, then we can be reasonably confident that in five years' time actually the pain will have been somewhat less, there will still be pain, but we will really have more efficient, effective public services that we can be proud of.

Q53 Julie Morgan: I had a meeting earlier in the week with a small voluntary body who had worked with young offenders. They were funded by the local authority. What this voluntary body did was work with young offenders who were in institutions and then followed them into the community, and did some very simple things, like ensuring they had bank accounts, supported them with accommodation. This was evaluated, and there was a huge drop in the re-offending rate, a huge saving to the public purse by some very simple measures. They had lobbied everybody to try to get this spread throughout the whole of the UK, and it seemed to be almost virtually impossible to make that move. I wondered whether simple evidence-based things that have long-term effects, how that sort of decision, those sort of movements forward could be built into the sort of process that is going to happen? Because my fear is that we will look at ways to cut here, there, and we will not look at the policies that will actually bring spending down long-term but are actually very positive for people in the community generally.

Professor Talbot: I think part of that is about the way in which we take decisions about allocation of money to particular areas. One of the things that is unusual about the British set-up is that we have a Parliament that plays absolutely no role whatsoever in deciding how we spend money. In every other Western country, and in Scotland and Wales and Northern Ireland, the assembly body, in Parliament or Congress, has a real role in public expenditure decisions, and actually scrutinises decisions before they are made, and has a chance to feed into them and present exactly the sort of evidence that you are talking about in that process. In Scotland, for example, the Parliament publishes draft budgets and then the various departmental committees hold hearings at which interest groups and people with that sort of evidence can come along and challenge spending priorities and decisions by saying, "Should we be putting money into this area? It

does not work", or "Should we not be putting money into this area? It does work." None of that conversation in Britain takes place outside the discussions within Whitehall, at the moment between the Treasury and the individual spending ministries, and the occasional cross-cutting review. It seems to me that only when you open that system up to that sort of democratic scrutiny, and Parliament becomes involved in it—we have had the perfect opportunity for the last 12 years with the spending review processes, they were every two or three years, depending on what flavour it was this time round, and it gave ample opportunity for them to have published draft spending plans, inviting select committees in Parliament to hold hearings around them, take evidence, judge which things seemed to work and which did not, and instead it is all done at the moment by civil servants and ministers behind closed doors. I think that is a major public administration change that we would need to make to the way the system operates. It would not take away the right of the executive to take the eventual decisions, but it would be subject to all sorts of checks and balances through doing that, and scrutiny, before they made the decisions about where they were putting the money, and precisely give people involved in the sorts of initiatives that you are talking about the opportunity to get involved. At the moment, the attitude in most of the public sector, I was talking to some colleagues who are involved in a major collaborative project about protecting parts of the national parks and moorlands from wildfires, it is a great collaboration between all sorts of different bodies, and their one great fear was that Whitehall found out about it.

Mr Haldenby: I think you have asked the big question really, which is of all of the things, we all know, in the public sector, so many wonderful things are happening, and people are achieving more for less, and remarkable things are being done, why are they not just naturally disseminated and get repeated? I think it is because, and we're back to these words of accountability, who actually is accountable for achieving that saving? Who benefits for achieving that saving? I suspect that the person who has achieved that saving that you have just described does not really see it, it is just sort of lost in the general scheme of things. This Committee has done so much work on improving the accountability of government and public services. I think something like criminal justice can be made more locally accountable, with money raised locally for those services and then spent on those services, so that local people can see the benefit. Some other services are more accountable to the individual, like the health service, so that if money is saved in the health service, that can come back to the patient. There are different ways of doing it, but I think it does take you back to the fundamental thing that unless we are quite tough about making public services more accountable, those kind of examples of best practice will not be taken up.

Mr Halpern: I think it is a very powerful example, it is one that comes up all the time. If you think about it, you are an offender, you are out of prison, your drug dealer will get to you in a few hours, but it will take weeks for someone to sort out your housing and lots

of other issues. What is going on? It is a split budget. It is a classic split budget issue. Those who have the ability, in principle, to be there and greet someone as they leave, they are not handling the criminal justice budget, and vice versa. You can imagine a world where those things are held. I remember when John Reid said we should transfer criminal justice costs back to countries where the offenders are coming from. Of course, we probably would have a net loss, given we produce a lot of them. But you could do that in terms of local authorities. In the same way, in previous generations, local authorities took responsibility for people going off to university; actually, you could take responsibility for criminal justice expenditure. So you would hold the whole budget, and then you would see it in a rounded way, and surely you would do very different things to what our current practice would be.

Professor Talbot: Can I just add to that? That is one of the points I was trying to make earlier. Out of historical accident, within England and Wales the prisons are organised on an English and Welsh basis as a national agency, whereas everybody that I have talked to in the criminal justice system says it would be much more sensible for the vast majority of people who have to go to prison to have locally managed and administered prison services, which were tied into local services, which kept people close to home and so on, and yet we have an entire system structured at the moment around the historical accident that it is run by the Home Office, and has been since the 1960s. It is completely mad. As a result, we get proposals for things like giant prisons instead of, where the real problem is, it is the short-term prison sentence offender for whom the key issue when they come out of prison is: do they still have a relationship with somebody, do they have somewhere to live, do they have a job, do they have support; all of those issues, which are destroyed by the fact that at the moment they are shunted around—somebody from South Wales doing three months can end up in the north-east, because that is where the prison place is.

Mr Halpern: 70% of our expenditure is central government driven in the UK, higher than any other country in the OECD and New Zealand, I think I am right in saying. It comes back to the fundamental. We can do fiscal consolidations really well, we can get Treasury and shut down those numbers, and actually we will generally do it in a very bad way when it is expressed at local level. That is the fundamentals of that situation.

Q54 Chairman: Could we perhaps end on a positive note, which is that often adversity is the real spur to innovation, is it not? There is a way of telling this which, as Tony rightly says, we shall not know until some years down the track when we look back at what we did, but it is at least conceivable that this is going to be a moment of major innovation in actually how we do government in this country, not because anybody chose to do it in that way, but because we were forced to think rather radically about it. We are going to have a paper, are we not, shortly, on the

“smarter state”, which is going to carry some of this? Someone suggested the problem is we may finish up with a stupider state if we do not get it right. But the chance of getting it right is there, is it not, if we actually do a project in the right way? We should reconvene in several years’ time and see how we got on.

Professor Talbot: May I have one last comment? The one thing that we have not addressed is the machinery of government issues, which David sort of alluded to, about how government takes these decisions in relation to things like collective Cabinet responsibility, but I think that also spills over into the institutional realm. Again, we are an outlier, in Britain, in having the finance ministry running the show, basically. There are very few other countries where the equivalent of the Treasury is as powerful as it is within the British system, particularly in relation to domestic policies. At the moment, I think that is even more true, because the First Lord of the Treasury happens to be the person who was the Chancellor for 10 years as well. I think one of the institutional issues that has to be addressed, which has come up perennially over the last 30 or 40 years, has been how do you actually have a strategic centre to government which can make strategic decisions that isn’t the Treasury; includes the Treasury but is not the Treasury? We have had the Department for Economic Affairs and the CPRS and all sorts of other things as attempts to do that, and it has never succeeded at the moment. Unless we find some way of solving that problem, I think a lot of the things we have been talking about today just will not happen.

Chairman: Now that you have provoked me with more things, Tony’s point about the politicians being the sort of silent voices here, all the managers ready to go on all this stuff, it did really remind me that certainly in Sweden, but possibly in Canada too, they were very different political cultures, in a different world, and particularly if you are trying to get a programme which convinces people that it is fair, and gets national assent to it, you try to do things in a rather more collegiate way. I mean, you would have a national recovery programme, you would say that for five years, or whatever it is going to be, we have all got to—but the problem is, we do not do politics like that here, and that is a big impediment, is it not, to doing the kind of things we are talking about?

Mr Prentice: That is another story.

Q55 Chairman: May I just say, we have had a really, really excellent panel, it really has been very, very interesting, a brilliant panel. We are very grateful to all of you for coming along and sharing all of this with us.

Mr Halpern: I just want to say one tiny little thing? It was just simply that you may not be able to fix the Treasury, but you can try and make Parliamentary committees scrutinise other than within departmental silos, and that is something which actually is—

Chairman: That is an even bigger issue, but thank you for it. Thank you very much.

Thursday 21 January 2010

Members present

Dr Tony Wright, in the Chair

David Heyes
Kelvin Hopkins
Mr Ian Liddell-Grainger

Julie Morgan
Mr Gordon Prentice
Mr Charles Walker

Witnesses: **Mr Steve Bundred**, Chief Executive, Audit Commission, and **Mr Amyas Morse**, Comptroller and Auditor General and **Mr Michael Whitehouse**, Chief Operating Officer, National Audit Office, gave evidence.

Q56 Chairman: Could I welcome our two witnesses this morning. As you know, we are having a canter through some of the issues surrounding the implications for public administration in the fiscal squeeze and we thought you were two people, amongst others, that we should talk to, and so we are delighted to welcome Amyas Morse, the recently arrived Comptroller and Auditor General, and Steve Bundred, the soon-to-depart Chief Executive of the Audit Commission. Between you we think we have got the right sort of people here. We have been looking at some of the things you have been saying, but would you like to say something by way of a short introduction?

Mr Bundred: I can be extremely short because had I submitted a written memorandum to this Committee, it would have covered much the same ground as the memorandum you received from Tony Travers; so I can save you all a lot of extra reading time simply by saying that I have read Professor Travers' memorandum and I agree with it completely.

Mr Morse: I am going to be slightly less brief than that; I cannot compete with you there. Steve and I did discuss beforehand, and what you are going to hear from us, I think, mostly, will be different aspects of a view that is quite coherent. I will allow myself a couple of comments, one of them because I have a private sector background, now receding behind me but, nonetheless, there. If I may, it is perhaps worthwhile to reflect a little bit for a moment on the difference between my private sector and public sector experiences, if you will find that useful. Typically, if you said to me "difference in competence", there is a significant focus in the private sector on cost management for pretty simple reasons, the simple reason being that it is much easier to improve the performance and profitability of a business quickly by taking costs out than it is by putting things onto the sales line. If you imagine, for a second, every time you make a sale, if you take £1 off the cost line it goes to the bottom line; if you put £1 onto the sales line, you are going to get a certain percentage of that as profit and then you have got to re-sell it next year. Therefore, if you are permanently restructuring your costs to take things down, it is a much more rapid and permanent improvement, and that is why, if you cut through much of the theoretical talk, an awful lot of the substance of management publications in the private sector are actually about cost reduction or re-profiling of

organisations and, most typically, they have a lot of common factors. They involve using information to enable you to take layers of structure out of the organisation and, as a substitute for layers of management in particular, using information to allow more standardised ways of working and simpler decision flows without as much human interaction as normal and, therefore, a flatter organisation structure. It is not mysterious; it has been evolving for many years in the private sector. It is not miraculous, but it is an approach, and I think it is fair to say that the strong motivator there of a constant requirement for profit improvement is not as much present in the public sector, but I am hopeful that, despite the unwelcome aspects of the current financial crisis, actually it does provide somewhat of an approximation for that pressure to try to build confidence in some of those, what I call, management discipline areas. Therefore, I am hopeful to see that being pushed forward and I think it is a key ingredient to effective cost reduction of a sustainable, long-term kind.

Q57 Chairman: That is all very interesting, and I will bring Steve in here, but is it not just much more difficult to achieve the cost reductions in the public sector than it is in the private sector? Is that not one of the issues that we are going to confront?

Mr Morse: Inherently there is nothing magically more difficult. The difficulties come, I believe—and Steve can jump in—from lack of clear prioritisation, lack of having a clear programme and clear objectives and you get the impression that, if you resist long enough, you may manage to be successful in protecting your particular budget or programme. In other words, if it appears that the reality is that if you hold out for long enough, they will go away and that this not part of a structural change in approach which is really going to be driven through, then you will get a build-up of resistance and people playing it long on you and, therefore, it is much more difficult. If you also do not have a clear and coherent organisation and a clear leadership of what is to be done, then, yes, it is more difficult, but it is difficult for those reasons, not because of something inherent in the air in the public sector.

Q58 Chairman: Let us regroup and start at the beginning, if we can. You mentioned the Tony Travers memorandum to us, which I think, essentially, said the public sector does not know

what is going to hit them and they are woefully ill-prepared for it. Could we get a grip on this. What is about to hit them and how does what is about to hit them now compare with moments of being hit in the past?

Mr Bundred: Let me deal with the latter part of that question first. Although it is undoubtedly the case that we are going to experience spending cuts of a kind that have not been seen probably in the lifetime of any of those currently working in the public sector, it is also the case that they are going to come after a period of 10 years of sustained growth, and the public sector is starting from a much higher base than it experienced when there were spending cuts in the mid-1970s and in the early 1990s. Even if there were to be £50 billion of reductions in public expenditure, we would still be spending more in real terms than we were at the time of the last General Election.

Q59 Chairman: Tony Travers, who is going to figure largely in this session, obviously, said that the £50 billion actually should be £90 billion.

Mr Bundred: The £90 billion figure, I think, was probably the estimate of the structural deficit at the time of the last Budget. I think in the Pre-Budget Report that figure is more like £73 billion, and, of course that will be found by some combination, yet to be determined, of tax increases and spending cuts; it will not all be spending cuts.

Q60 Chairman: But we are agreed that this is of an order that in modern times the public sector has never experienced.

Mr Bundred: Yes.

Mr Morse: And, therefore, requires a different approach. I am trying to make the point, Chairman, that it is not a question of simply saying this needs cuts. It needs restructuring of approach. If you are going to achieve sustainable cost reductions of this kind, it has to be part of a change process, not simply saying, “We are going to take the lawnmower over everything”, “We are going to take the lawnmower over the cost base, as we normally do, but this time we will set the ratchet differently”. That does not work. It needs a more planned and intelligent approach.

Q61 Chairman: This is what we want to explore with you. Steve, I have been reading some of your stuff. I have not got the dates, but at one point you say that this is Armageddon, and then, later on, you say this is all perfectly manageable.

Mr Bundred: No, the word “Armageddon” I used not of the spending cuts. I said that the Armageddon scenario for the Government was that there would be insufficient lenders to match its borrowing requirement and that is why its spending cuts were inevitable. I never used the word “Armageddon” in relation to cuts themselves.

Q62 Chairman: Let us explore this question of what you are talking about now, Mr Morse, which is the scope of the public sector to achieve reductions of the scale that we are talking about without doing

fundamental harm to the core services themselves. I suppose my question is: is that doable or is it an illusion that it can happen in that way?

Mr Morse: First of all, if I rest on what Steve just said, that we have had significant growth and so there is capacity to reduce, and you have to think, “What do you mean by ‘irretrievable harm?’” What I would say is that I do believe it is doable and it is doable by understanding that what we are talking about is achieving results. Can we maintain the same level of resource throughout system? No, obviously we cannot. Do I buy that a reduction in the amount of resource in the system equals, necessarily, a degradation of results? No, I do not buy that. I believe that a more flexible approach, both to administration within the system, to the amount of resource that government spends talking to itself, making decisions and administering itself and also to the medium of service delivery—a different and more flexed approach to service delivery and one with resources used more economically while still delivering services and meeting needs but meeting them, perhaps, in an evolving and different way—is entirely achievable and you see that already happening. If I can take HMRC, where there is a major change to go from the amount of face-to-face interaction to say, as far as possible, if we can do things on electronic media, either by phone or online, it has got difficulties about it but it takes the cost down and, essentially, in many ways you are still delivering the service; so that is a change process rather than a degradation in service.

Q63 Chairman: I think the judgment that I am asking for is, given what we are saying about the scale of what has to be done, can this be achieved by doing existing things more efficiently or do we have to say we are going to do fewer things?

Mr Bundred: I agree with Amyas: it is doable but I do not pretend it is easy. If you look at the NHS as an example, last year the NHS commissioned a report from McKinsey’s on what would need to happen if they were required to take £20 billion out of the system. That report has not been published, I believe, but it has certainly been extensively leaked, and it did show that it is doable but it would require politicians to take some very difficult decisions around closing capacity in some places and certainly reducing staff.

Q64 Chairman: I have been reading your interesting remarks. You are saying it makes no sense at all to exempt major services like health and education from what has got to be done?

Mr Bundred: It seems to me to be absurd to imagine that the only services where no efficiencies can be found are those that have been most generously funded for the last 10 years, and I also think, because of the difficulty of making cuts elsewhere, there is a need to be seen to be fair in the allocation of cuts. Of course, politicians are entitled to have priorities, and one would expect those priorities to be manifest in the decisions they make about cuts as well as in the decisions they make about growth, but to simply

exempt the two most well funded services from the kind of pain that will be inflicted on everybody else seems to me to be a mistake.

Chairman: We want to talk to you about some of the efficiency savings that are being talked about.

Q65 Mr Walker: For the last 20 years governments have talked about efficiency savings and the drive to cut out waste. It forms the centre of most election manifestos—“We are going to address the social security budget as £5 billion is being taken by people who should not be taking it”, and so on and so forth—and actually little happens. How many of the efficiency savings over the last five or 10 years have been illusory and what are the chances, going ahead, that real, genuine efficiency savings will be made?

Mr Morse: We have recently done reports on efficiency savings in the Department for Transport and in the Home Office, and we looked at those savings on the basis of savings we had complete confidence in and savings that, for one reason or another, we were doubtful about, in the sense that we thought there was a serious question, so there were three categories of traffic light priority. In each case there was a significant proportion of savings, a variable proportion of savings, that we felt really confident in. There were quite a lot that were one-off savings, so not things which were permanent reductions at the cost-base, and there were some which we thought were really a bit speculative. In all cases there is genuine forward movement through efficiency, but I would make the point to you that I think there is a very serious limit to how much can be accomplished by that means; in other words simply by incremental tightening. I think that if you are not prepared to go to something more radical than that, you will only achieve a marginal improvement, worth having but not likely to meet the strategic needs we are talking about today.

Mr Bundred: The only thing I would add to that is that there are further efficiencies to be found in the public sector, undoubtedly, but not just in back office functions. I think it is important in the debate about efficiencies to recognise that there is greater productivity to be found from the frontline as well as from back offices.

Q66 Mr Walker: One of the things that has happened to the public sector, rightly or wrongly, over the last 10 or 15 years is that it has grown in the number of people it employs. People do not like to talk about headcount reduction, but we have seen a number of companies make significant headcount reductions. They reduce heads because that is probably one of the most effective ways of saving real money. What size of headcount reductions have you looked at in the public sector?

Mr Morse: I do not have a good answer to that, but I will give you an answer in principle, which is that if a large part of your cost-base is headcount, you are not going to reduce the costs without taking people out in the long run. If you do that as part of reorganising and re-costing or having a flat

organisation, it follows inevitably that you are not going to have the same number of people in it; otherwise the cost will not go down in that way. Some costs can be associated with more efficient service delivery, getting more for less money, but you have to look at what the cost drivers are, and a significant part of cost drivers in the public sector, not the only part but a significant part, are people. It is very unlikely that will be excluded from how you achieve ultimate, serious cost reductions.

Mr Bundred: I agree with a lot of that too. I would add that certainly in local government we have observed a number of councils that are already either implementing staffing reductions or planning to do them, but we have not attempted to aggregate that and put a figure on what is happening currently or an estimate of what might happen in the future.

Q67 Mr Walker: You mention that there is always resistance from senior civil servants to reducing the size of their empire, or there tends to be resistance. Could it get to such a crude level that permanent secretaries are told, “In six months to a year we are going to review your performance and if you really have not taken up the cudgels on this one, you are going to be shown the door. That is how serious we are”? Do you think those sorts of conversations have to happen? They happen in the private sector with divisional heads and divisional and country managing directors: “You either reduce your costs or you leave the business.” Are those conversations going to happen, do you think, whoever wins the next General Election, across Whitehall?

Mr Morse: I do not think I was saying that it is automatic that senior civil servants will resist cost reductions, if you do not mind me saying so, Mr Walker, but what I do think is there is a natural effect. If you do a very crude cost reduction programme and you begin, as a result, to degrade quality of administration and quality of service, what will happen over a period of time is that people will not like it and you will rapidly get a push-back developing. Steve mentioned a number. It does not matter; it is a very big number that we need to accomplish in getting back to roughly where we were before the financial crisis in terms of the overall public finances. To get that far we need a degree of consent and co-operation from the people in restructuring the public services. It is not enough to say, “We are just going to do it to you”, in a very rough and crude way. It needs to be something which is seen as a change process leading to a credible and in many ways improved approach if you are going to get consent and, therefore, a sustained effort over the longer term. I do not regard that as a bit of soft advice. If you do a structured cost reduction and you do not obtain the buy-in and support, not just by being tough, of the people that you are inviting to lead the change, it will not work very well for very long.

Q68 Mr Walker: What areas do you feel government should consider withdrawing from?

Mr Bundred: I do not think that is for me to say because that is essentially a political judgment. All I would say is that I think there should be no area which is exempt from consideration of the scope of spending reductions.

Q69 Chairman: Education, you tell us.

Mr Bundred: I am not suggesting that the Government should withdraw from education, but there is certainly scope for spending reductions in education.

Q70 Chairman: All these thousands of teaching assistants have been employed and you suggest that school numbers have gone down; staff have gone up.

Mr Bundred: Since 1997 there have been 32,000 new teachers, 70,000 extra support staff, 100,000 new teaching assistants and 80,000 fewer pupils.

Q71 Chairman: So you want a serious cull of people like this?

Mr Bundred: I think there needs to be some consideration as to whether or not the same outcomes could be achieved with less spending.

Q72 Chairman: I am sorry to press you on this, but I think we need to know exactly what you are saying, because you have got things to tell us. You say here, "Do not believe the shroud-wavers who tell you grannies will die and children starve if spending is cut." Then you go on to say that we need what you call a frank and intelligent debate about how and where they will fall—that is, the cuts.

Mr Bundred: Yes.

Q73 Chairman: What would a frank and intelligent debate involve then?

Mr Bundred: It might involve looking at the scope, for example, for greater efficiencies in education and in health rather than simply accepting that those two areas should be exempt from the pain that will be inflicted on everybody else.

Q74 Chairman: You say more than that, do you not?

Mr Bundred: The Audit Commission has published reports about value for money in schools, which certainly shows that there is scope for spending reductions in schools. Schools have increased their balances, schools are currently sitting on £2 billion of balances, which is money that they have been given that they have not spent at all.

Q75 Chairman: More generally, you tell us—and this is interesting coming from a major audit body—that there is no direct correlation between levels of spend and quality of service. That is a pretty alarming thing for politicians to be told, is it not?

Mr Bundred: It should not surprise you, because the best run public services are those where management pays attention to delivering value for money.

Q76 Chairman: Frank and intelligent debate would involve telling people honestly the scale of what is to be done?

Mr Bundred: Yes.

Q77 Chairman: Do you think politicians of any party at the moment are telling people the truth about the scale of what is to be done?

Mr Bundred: The scale of what is to be done is evident from the Pre-Budget Report. What politicians are not saying at the moment is what judgment they would make about the balance to be struck between tax increases and spending cuts and where those spending cuts should fall.

Q78 Chairman: So they should be explicit about the tax spend?

Mr Bundred: I would like to see a more open discussion and greater clarity about the intentions of politicians of all parties.

Q79 Chairman: We have been told by previous witnesses that, on the whole, people think that a balance of two-thirds spending cuts, one third tax increase is about right. Is that what you think?

Mr Bundred: I think that is a matter for political judgment.

Q80 Chairman: Yes, but in the spirit of frank and intelligent debate?

Mr Bundred: I think the experience of other countries has certainly been that there needs to be more on the spending side than on the tax side.

Q81 Chairman: Do you think politicians should now be far more explicit, not only about the scale, but about the nature of cuts that are coming?

Mr Bundred: I would certainly welcome that.

Q82 Kelvin Hopkins: If I could preface my questions by saying I do not accept the cuts agenda and I think there is an intelligent alternative to this report, which I will not trouble you with now but which does put out an alternative. We are in the middle of a recession. Cutting jobs and cutting spending in a recession is not counter-cyclical, it is actually going to reinforce the recession, and so maybe this cuts agenda needs to be questioned.

Mr Morse: Let me comment on that. If you are going to achieve something—and I am repeating myself a little bit, Chairman—which changes the way you are organised, actually in the very short-term you should not be looking for that to produce enormous saving because you are probably going to have to invest, and certainly do some planning, and probably some enabling investment to allow you to rebalance the way you are organised. If you are going to become more information-led, if you are going to do things in that way, you are going to have to do some planning and some development in order to get that to happen. There are two subjects: one of them is a medium-term structural reduction and rebalancing and the other is what can be done in the short-term? I think those two need to be worked against each other. Then you can have a debate about what is appropriate short-term and you can have a debate about medium-term restructuring.

Mr Bundred: I would also add that we are coming out of recession. Clearly, in the midst of a recession there is a case for government to borrow and spend but, on the Chancellor's estimates, we will have growth this year and very substantial growth next year.

Q83 Kelvin Hopkins: We have two and a half million unemployed, and that is not coming down very quickly. It is reducing slightly. Typically in the 1950s and 1960s there were half a million unemployed. Two million unemployed is a very significant number and a significant cost. You touched on this, separating out the cyclical component of the deficit and the structural component. Clearly, the structural component has to be addressed by tax increases, I would suggest, or efficiencies, or whatever. It is the structural part that we should be looking at, not the cyclical part, and we are currently confusing the two and frightening everybody that we have to make savage cuts. Is that not the case?

Mr Bundred: I am certainly not confusing the two. The figure I quoted earlier in this hearing was the Chancellor's estimate of the structural deficit.

Q84 Kelvin Hopkins: If you look at some of the efficiencies, some of the problem, is it not, is driven by policy. The difference between the private sector, which is profit and loss driven, and the public sector is that we have policies sometimes which are costly? It was a decision, not one I agreed with, for example, to give schools local management responsibility. It was over time, first financial and then general. That was costly. Is it not the case that if we actually re-established strong centralised local authorities where all that management was done by the local authority, we could make some savings? It might not be politically what people want, but it would make significant savings.

Mr Bundred: You can require schools to make savings without taking them back into local authority control. I do not think you need to make those sorts of changes in order to get greater efficiencies from the money that is spent on education.

Mr Morse: I agree with that. I think if you have good information and you use it intelligently, you are clear as to what it is you require, but just having a reorganisation is not necessary in order to achieve efficiencies. I am not saying it might not be a good thing; I am agnostic on that point. I am simply saying it is not an absolute necessity in order to achieve more cost control.

Q85 Kelvin Hopkins: But the skills required to manage costs are not going to be sufficient to manage, independently, thousands of schools. There are essentially head teachers who pick up a bit of accounting and school secretaries who pick up a few financial management skills, but it is not the same as the kind of skills you could employ at a unitary authority, for example.

Mr Bundred: Local authorities can certainly do more to provide support for schools in relation to financial management, but that is not at all the same thing as

taking responsibility for financial management away from schools and placing it back within the local authority.

Q86 Kelvin Hopkins: It has been put to us that, for example, bulk ordering of equipment for schools—computers for example—by a local authority would be much more efficient than getting local schools to make their own individual orders with companies. With a big order from a local authority, price can be driven down.

Mr Bundred: I would not disagree with that, and it happens now to some extent, and there is certainly scope for it to happen to a greater extent. My point is simply that there is nothing in the present arrangements for devolved financial management in schools which prevents that.

Mr Morse: Collaborative procurement can be applied across government, central government departments, to a significant degree; you can apply it across organisational structures: you do not need to be in an organisation to collaborate in procuring and getting benefits of scale.

Q87 Kelvin Hopkins: We have increased spending on education, but we are still only creeping up towards the European average spending per head on education, and we still have educational problems, we still have some of the largest classes in Europe. Using the base of 12–13 years ago as the reference point is really suggesting that we were right then and we are wrong now. In fact, the base now is still not perhaps where it should be. Quality might actually require more spending on education rather than less.

Mr Bundred: As I said earlier, governments are entitled to have priorities. This Government has prioritised education, and no doubt it will continue to do so for as long as it remains in office, but that does not exclude the possibility that there are efficiencies to be found in education. As the Audit Commission said in the report it published on value for money in schools last year, the incentives for greater value for money in schools are very weak.

Q88 Kelvin Hopkins: The point I made at the beginning, or that has been made earlier, is this balancing of taxation with spending. Other countries have higher tax rates, particularly on the better off, they have higher company taxation and they have more revenue coming in which they are able to spend on their public services. We almost ignore the possibility of higher taxes and, indeed, the parties have been competing to cut taxes. Our Chancellor, our Prime Minister cut the standard rate by three pence. Three pence is the equivalent to £12 billion a year, roughly. £12 billion is an awful lot of money, much more than some of the tiny savings that have been suggested in the Smarter Government report: £100 million here and £200 million there. One pence on the standard rate could make a very, very significant difference. I am not suggesting we should raise the standard rate, but that is the reality.

Mr Morse: Okay, but what can I add to that? That is a point of view and it is a policy decision. Do you want to have a higher tax regime or not? Obviously, if you decide to collect more tax, it reduces the amount of cost reduction you have to do.

Q89 Kelvin Hopkins: I am just hoping that as independent-minded public servants and not politicians you should remind government that there are other ways of approaching deficits than savage cuts.

Mr Bundred: As I said earlier in this Committee, the deficit will be eliminated by some combination of tax increases and spending cuts yet to be determined, and I would like to see greater clarity about what that combination will be.

Q90 Mr Prentice: On this business about tax, I am told that £27 billion of tax goes uncollected every year and £70 billion is lost through tax evasion. This comes at a time when the Government wants HMRC to close 200 offices by 2011 and get rid of 20,000 jobs. Does it make sense to put that kind of squeeze on Revenue and Customs when there is all that money out there which should be collected but, for one reason or other, is not being collected?

Mr Morse: This happens to be a subject that we have looked at closely in the NAO. I would say that there is spending that could happen in HMRC that would accelerate some aspect of tax collection, and it is very sensible and relatively painless to get on and do that. Because of the financial crisis, there is a big tax debt and there is a resolution of cases which would release more tax income, so this is a money-gathering device for government; we need to get it to work efficiently and not just treat it like any other department in that way.

Q91 Mr Prentice: Why have we not done that before?

Mr Morse: Forgive me for a second. That is true, but it does not follow that the way to do that is to keep the distributive revenue system. It may mean actually making some more central investment in debt-targeting systems and things of that sort, which the Revenue needs to do, in my view, in order to be in a position to collect money and pick some fairly low-hanging fruit.

Q92 Kelvin Hopkins: One of the points made in this report is that the most efficient way of bringing down the deficit is to maximise public investment in the short to medium term because that creates employment and employment means benefits reduce and tax revenues increase, and that is the quickest and most efficient way of reducing the deficit, not by making cuts in services which would simply increase unemployment and make the deficit worse.

Mr Morse: Forgive me, just going through that, it cannot be right to say that the way to reduce the deficit is to either keep employment high or necessarily to employ more people, because obviously you have got the cost of employment and then the tax is a percentage of that, and I am

assuming that benefits are a lower level as well. Just in maths terms, it cannot quite work out, I do not think, in that way.

Kelvin Hopkins: I will send you a copy of the report.

Q93 David Heyes: Mr Morse, you have painted a picture of a private sector that is much more cost-effective, with flatter organisational structures, where the drive for profit puts on the pressure. They are just generally quicker on their feet. That was the picture you painted. You contrasted that with a public sector where there was a lack of clear prioritisation, a lack of urgency, the avoidance of structural change, a lack of clear leadership, and so on. Are the distinctions between the private sector and the public sector as clear as that nowadays? Massive areas of public sector service delivery, which is what we have been talking about, are delivered by these super-efficient private firms. What is your comment on that?

Mr Morse: First of all, if I gave that impression, thank you for giving me a chance to clarify.

Q94 David Heyes: It was more than an impression: those were your words.

Mr Morse: Just to be clear with you, I do not regard everything (and I thought I did say this) in the private sector as a patent and I certainly do not mean to suggest that. What I simply said was, as it happens, in the area of cost management there has been a very heavy development in the private sector because it is an easy way to drive up profits—I did not think I went much further than that in it—and, therefore, there is something there that is useful to at least look at, not to bring over wholesale but to look at and understand, and that has been going on for a very long time. It is not to say that everything about the private sector is wonderful. I do not think that, but I do think that in these focused areas of what is the way in which you can reconfigure an organisation, roughly speaking, so as to get the results and deliver the services and have less cost, there are suggestive examples in the private sector.

Q95 David Heyes: But the private sector within the public sector is somehow stifled from doing that. That seems to be the inference to take from that.

Mr Morse: I should think the private sector within the public sector will do what it is contracted to do. If the contract says, “Be as efficient as you can possibly be,” they will do that. If they are contracted to deliver a particular service, then they will do that.

Q96 David Heyes: That would open up a whole new area that, I suspect, is not in the brief of this Committee. You were saying that one of the ways in which the public sector can achieve that crisper, more responsive private sector approach would be through better information systems. I would like you to help us to understand what you imagine that consists of. Help us to understand what you mean by “better information systems”. Is it just an accountant arguing for more accountants?

Mr Morse: No, it is not, it is an argument for fewer layers of management and fewer touches on every decision that gets made, to be very brief about it. In other words, any decision in any file that is going through the public sector, if you had a clicker for every single person that looks at it and gives input to it, you would be startled by the number. I had three years in the MoD, so I am not just making this up. I am now trying to get reports cleared through the public sector. An awful lot of people look at everything. If you actually said, “How many people absolutely need to be involved in each of these decisions?” you would find there was a startlingly smaller number than the number who actually are involved and who touch it. So there is room, in my view, from my own direct experience as well as from what I see in organisation structures, for much simpler and more direct decision pathways, and that means fewer layers involved in making decisions, and if you have good quality, consistent and coherent information, and not everybody inventing their own version of things, it is possible to make those decisions more quickly and many times they are better decisions.

Mr Bundred: It is also an argument for better data quality in the public sector. Much of the data on which decisions in the public sector are based is of very poor quality.

Q97 David Heyes: Can you give some examples of what leads you to say that?

Mr Bundred: The Audit Commission is responsible for providing an assurance framework around Payment by Results in the National Health Service. We found that the error rate of clinical coding decisions on which funding flows are based in the National Health Service varies from zero in the best NHS trusts to 50% in the worst.

Q98 David Heyes: I heard the words you said; I did not entirely understand them: “Improved information pathways”. We are lay people and that is the kind of jargon that is a bit lost on me. Can you put it more in layman’s terms for us?

Mr Morse: I am sorry about the jargon. Let us try and think about it like this. Supposing you said, in order to clear a decision of a particular kind (and I am going to go back to my previous MoD job), you need someone to decide that a piece of equipment was needed, someone to decide that the deal being proposed was commercially viable, someone to decide that it fitted into the budget and someone to decide that it could be delivered on time; in other words that the supply chain could be managed, so that would be four people. In order to make a good decision you needed four people who really had something to give, a different competence laid on top of that decision as it came through. Everyone else looking at it was probably giving a view. It was being socialised with a lot of people who were not necessarily required in order to make a good decision. If you ask yourself that question, when you see decisions in public life—how many people are actually adding real knowledge and substance to how the decision should be made and how many

people are actually accountable for the consequences of the decision and, then, how many people are involved—if you can cut the number of people involved and bring it close to the number who really add value, you get a much simpler activity. This is not a big IT argument; this is an argument for being disciplined, using information and saying, “Okay, this person said this, that person said that. It follows that we should conclude like this”, and you actually make it simpler.

Q99 David Heyes: That is surprising, coming from an auditor, because those sorts of systems often exist as a safeguard against malpractice involving numbers of people in making decisions. Having decisions go through different layers and being recorded for there to be an audit chain that can be identified is often, in my experience, more in the local government than the national government sphere, the kind of thing that auditors insist on.

Mr Morse: Just to be clear, if you have a decision where competent people have looked at it and you have clearly recorded the evidence on which they base their decision, it is all properly recorded, you will find that you can audit it very readily. Interestingly, in a lot of the audit work we did we found that information of that kind does not exist in the structures that are there now. You say, “Can you please produce evidence of this?”, and the answer is often, “No”, or it is, “We had to create the evidence ourselves by doing focus groups and things of that sort, or by sampling and doing our own exercises to create evidence.” What I am saying is it is not as if there is a high level of assurance in everything we look at now. In fact, with a simpler and more straightforward approach, you would have more confidence in the decisions being made.

Q100 David Heyes: Is this an argument really for saying that it is politics and politicians that add these layers that cause these delays in the decision-making process and the other criticisms that you have made about public sector delivery?

Mr Morse: It is that, but it is also the capacity of organisations to spend a huge amount of resource talking to themselves. Tell me you do not think that is true in the public sector. If you cut that out and say, “What is strictly necessary to go from here to here; everybody else stay out?” you get a remarkably direct process.

Q101 David Heyes: Steve, do you agree with that? Let us cut the politics and then we can all be more efficient and we can get on with making savings?

Mr Bundred: I would never suggest that managers in the public sector do not have the capacity to make things more difficult for themselves too. We started off in this hearing by saying whatever the number is it is a big number but, in our view, it is manageable although it will not be easy. I think the point that I would want to make is that in order to manage it public bodies do need to ensure—this is certainly true in local government—that they have got the capacity and the information systems to enable them to make difficult decisions and give effect to those

decisions in a timely way, and although in local government there are many local authorities who are already preparing in quite a sensible way for the possibility or the likelihood of having less money available to them in the future, there are certainly a number of other smaller local authorities, in particular, who ought to be asking themselves some questions at the moment about the capacity of their finance function.

Q102 Chairman: I was going to ask you what public sector bodies, knowing all that we know, should be doing at this moment and, also, whether audit bodies like you ought to be helping them or ensuring that they are doing it?

Mr Bundred: They certainly ought to be looking at the quality of the data upon which they are basing their decisions and the information systems that Amyas has talked about. They should be asking themselves some questions about the capacity of their finance function and they should be looking at ways in which savings can be achieved without impacting upon the quality of services that they give to the public. They should be talking about things like collaborative procurement. They should be looking at the use of their assets. They should be looking very rigorously at the incentives that they have to get their staff to deliver better value for money.

Q103 Chairman: Your view is that some organisations are doing this and some are not. The second part of the question is this: is it the auditor's role now, knowing what is coming, knowing what they should be doing, to evaluate whether they are doing it or not?

Mr Bundred: We do that. Our auditors make scored judgments about the use of resources within the bodies that we audit, and we publish that information. We express a view about whether public bodies, local authorities, and so on are using their resources well.

Q104 Chairman: Do you think there is an exercise to be done, given the fact that we are all saying that there should be serious planning going on now for these next few years, to make sure that you do not take daft decisions, you take good decisions, well thought out decisions, ones that get rid of the bloatedness and retains what is essential? Is it not possible to do an exercise actually to evaluate, at least at the planning stage, how effectively these bodies are putting in place plans to do this?

Mr Morse: I think we can do something. We are not managing these bodies, and it is quite important, as auditors, not to get sucked into managing or acting as quasi managers—that is not our job—but what we can very clearly do, and we are doing this in the NAO, is to put forward principles of what we would regard as how to do coherent change processes and cost reduction processes and say, “We are looking for some of these elements. It is not a recipe but if you have not thought about these things, that is not right.”

Q105 Chairman: You are telling your public sector bodies that at the moment, are you?

Mr Morse: Yes, and if our individual clients say to us, “I would like you to have a more detailed and engaged discussion,” we are willing to have that discussion, but, on the other hand, it is not our job to force our way into the board room to have it. What we are prepared to do is to say what are the criteria we are looking for. If we were in future evaluating what they have done, what we will look for is the hallmarks, the badges, of a coherent, well thought out and well executed programme, and I think it is only fair that we should be prepared to give some indication of what they are rather than waiting until after the event solely with the benefit of hindsight.

Q106 Chairman: Is the Audit Commission doing something similar for local government and the Health Service?

Mr Bundred: CIPFA and SOLACE have done that for local government, and the NHS itself is looking at ways in which efficiencies can be found from NHS spending. The other thing, of course, that auditors can do and that we do do is to identify service areas where we believe there is scope for better value for money, and we have published a series of reports doing that. I mentioned the report we published last year on value for money in schools, but there have been other reports about other service areas too.

Q107 Chairman: You can retrench badly or you can retrench intelligently. It is how we have any safeguards that one rather than the other is going to happen.

Mr Morse: What you need is not actually to characterise it primarily through retrenchment but to characterise it as a change from the way we did things before to a new way of doing things. If you have a plan like that, if you have actually thought that through and said, “We are not just going to talk about maintaining services. We can see how we can deliver these new services. We can see how we can administer and support all of that. We can see how that would all work in the new state. We have got that plan and, although it may change a bit, we have got it there and now we are going to, in a credible way, move through into implementing that,” then you have got something to work with, and then you are talking about measuring: did they actually do it? Is it sensible? But to start at least with that, you would say, “All right, these people are thinking clearly about the future and not just taking it from day to day.”

Q108 Mr Walker: When I was in the private sector we had a lot of dealings with government, and our eyes lit up when we got government contracts because it was so much easier to earn significant sums of money off central and local government than it was off the private sector. I am saying this because you mentioned procurement. I do think that central government and local government procurement really does need to sharpen up its act. I have got acquaintances at the moment still fulfilling

contracts with central and local government and government agencies and they simply cannot believe the amount of money they are being given to do fairly simple things. Is that a concern that you share?

Mr Morse: I would say that there is a big effort going on to raise commercial skills. It is a necessary part. If you are going to contract, particularly if you select a somewhat complex contract or a partnering contract where you have got to work closely with the private sector and you cannot field people who have comparable skills to the people they are supposed work along with, you are likely to have a bit of an unfortunate result. You have to make sure you have the right skills in place. However, there is a big effort going on to raise commercial skill levels and it is having an effect. Is it all perfect? I am not saying that, but I think it would be unfair to suggest that this effort is not going on, led by the Office of Government Commerce. There is an effort but it is still sometimes an uneven relationship in terms of skill levels; I cannot deny that.

Q109 Mr Walker: I know it is a well-worn example, but the GP contract was the most incredible thing for the public sector to enter into. You virtually doubled GPs' money while reducing their hours and weekend work. Are we going to see the end of those types of arrangements in the public sector and why on earth was that allowed to happen, in your view?

Mr Morse: That is not a particular one I have looked at, so I cannot comment.

Q110 Mr Walker: You must be aware of it.

Mr Morse: Of course I am aware of it, yes.

Q111 Mr Walker: Why would you not comment? You must have a view.

Mr Morse: On this particular matter, I do not have a better view than anyone else.

Q112 Mr Walker: What is your personal view? You must have a personal view as an informed commentator on these matters.

Mr Morse: I am not here as a person; I am here as the Comptroller and Auditor General.

Q113 Chairman: I have got a feeling that we have had an audit report on this, have we not? It must have come from the NAO, must it not?

Mr Whitehouse: Yes, we did a series of three reports on the contractual arrangements that were introduced in the NHS for consultants, GPs and ancillary staff. Our work supported the observations that Mr Walker made.

Q114 Chairman: So you can speak with authority then.

Mr Whitehouse: As he said, it was before Mr Morse's appointment.

Q115 Mr Prentice: Jack Straw created a bit of a storm a month or two ago when he said that police officers should be out catching criminals but they stayed in the police stations because the police stations were nice and warm. It got me thinking

about efficiencies in the Police Service. What are the most inefficient parts of the public service? Let us begin with the police. Are the police as efficient as they should be?

Mr Bundred: I think there is no part of the public service that could not be more efficient. The Police Service is not exempt from that.

Q116 Mr Prentice: It is a flat organisation, a lot of ranks were stripped out years ago, and I am just left wondering whether it is as efficient as it could be. I rephrase the question.

Mr Bundred: I am absolutely sure it could be more efficient, but I am certainly not in a position to comment on Jack Straw's statement. I have no evidence to support that.

Q117 Mr Prentice: What are the bits of the public sector, as you see it, that are least efficient?

Mr Bundred: Let me just say this about the Police Service, and it applies to the Fire Service too. I think the degree of scrutiny to which the uniformed services are subject is less rigorous than the degree of scrutiny to which, say, local authorities are subject, and that does apply to value for money considerations as well as to service quality considerations.

Q118 Mr Prentice: Why is that? Is it just a historic thing, or are we afraid of people in uniforms, or what?

Mr Bundred: I think it is partly cultural and it is partly to do with the natural trepidation of political involvement in relation to those uniformed services.

Q119 Chairman: Who should be doing the audit work in relation to them, and why is it not, therefore, as rigorous as it should be?

Mr Bundred: Because they are not accountable to directly elected bodies.

Q120 Chairman: No, but the Health Service is not either.

Mr Bundred: The Health Service is accountable to the Secretary of State for Health.

Q121 Chairman: So are these other services; so that cannot be the answer, can it?

Mr Morse: They are accountable to the Department of Justice, surely.

Mr Bundred: Police and fire services are accountable to partly indirectly elected police and fire authorities.

Q122 Chairman: Gordon is asking you, if you are saying this is the issue, why are we not getting an audit of these services?

Mr Morse: They are getting audited.

Mr Bundred: They are getting audited and they are also subject to inspection by HMIC.

Q123 Chairman: But you are saying it is less rigorous.

Mr Bundred: I am saying that the political scrutiny of them is less rigorous.

Mr Morse: You are not saying the audit is less rigorous.

Mr Bundred: I am not saying that the audit is less rigorous.

Q124 Mr Prentice: I think we have exhausted this one. David Halpern, when he came before us, said something counter-intuitive: that if you reduce staffing numbers it improves morale. You said the same thing, Mr Bundred, in Camden when you were chief executive all those years ago: that when you took an axe to the numbers of people working in that local authority, among those that remained, the morale improved.

Mr Bundred: Yes, that is correct.

Q125 Mr Prentice: It is a funny old world, is it not? If you get rid of people it improves morale amongst those who remain?

Mr Bundred: It should not be surprising because people join public services in order to deliver good quality services to the public, not to spend all their time coping with financial crises. When the financial crisis is dealt with, in the Camden case, when the finances of local government are put on a proper footing and the staff can spend their time focusing on the services they provide rather than on the budget, then of course that will be more satisfactory.

Q126 Mr Prentice: Did morale improve in the Audit Commission? I have a little note here in front of me that you agreed a package of housekeeping measures: you scrapped directors' bonuses; you cut £2 million from the pay bill; you shed 89 posts. Did morale improve in the Audit Commission after you did that?

Mr Bundred: Morale is very high in the Audit Commission, and it continues to improve.

Q127 Mr Prentice: Can I continue this line about morale? We learned yesterday that there is going to be a pay freeze in local government as from April next year, affecting one and a half million people. What do you think the consequences will be? Do you fear that people employed in local government are just going to take this on the chin or are they going to do something about it? Are they going to respond?

Mr Bundred: Do you mean by way of industrial action?

Q128 Mr Prentice: Yes, or whatever.

Mr Bundred: I am not in a position to judge.

Q129 Mr Prentice: You have advocated a pay freeze before, have you not?

Mr Bundred: I have not advocated it; I have predicted it. I have said that pay restraint was bound to be a part of the solution, and we are seeing pay restraint in the public sector, we are seeing it in the Audit Commission. We are freezing the pay of all our senior staff and the majority of our staff will get an increase of 0.7% at a time when inflation is running at 2.9%.

Q130 Mr Prentice: Would you like to see a pay freeze across the entire public sector?

Mr Bundred: The Chancellor has already indicated that there will be a cap on public sector pay for two years, and that seems to me to be entirely appropriate.

Q131 Mr Walker: Can I ask Mr Morse a question, just out of interest. I notice that you held a senior position at Price Waterhouse. I am not an economist and this is not a trick question. It is just something that Mr Bundred said that sparked an interest. What happens if you have a period of sustained pay freezes, for example in the public sector, matched to a period of high-ish—in historical terms—inflation? What sort of pressures would build up over two or three years? Some people talk about two or three-year pay freezes in the public sector. What sort of future unintended consequences does this build into the system?

Mr Morse: I think the main consequence that you have would be that if people are finding that their way of life is materially affected, in other words they cannot absorb it in their personal budgets, they are going to be under quite strong pressure to think about moving somewhere else, if they can, and they are also going to be waiting for the first opportunity to try and recoup what they see as what they have lost. I think you have to understand, if you just say, "Let us freeze it for a period of time," you have not got rid of the dynamic that might be underneath that; you are going to have to deal with that.

Q132 Mr Walker: So if you froze pay for two years and it increased very slowly for the next two or three years but during that period inflation was running at 3%, you could argue that over a four or a five-year period people could have taken up to a 10 or 15% real terms drop in their standard of living, potentially.

Mr Morse: That is reasonable. You are not talking necessarily about people who are starting with a particularly generous pay packet, so you just have to be aware of that. I am not against it; I am just saying that you need to understand that you may be creating pent-up pressure. This does not just all go away because you have decided on freezing pay.

Q133 Mr Walker: Absolutely, because then there is pressure to catch up, is there not?

Mr Morse: There can be.

Q134 Kelvin Hopkins: Government policies sometimes are expensive. They choose to adopt them because they are committed to them for ideological or philosophical reasons. Will you be advising government very seriously about some of their policies, like personalisation of public services, that might be very expensive—hiving things off to quangos rather than having direct services from local government? There is a whole range of policies which may actually be expensive and you are in pole position in giving advice to the Government, saying, "If you want to save money, do not do this."

Mr Morse: What we are going to be doing is giving the Government advice, and the NAO is preparing a report at the moment, on very accurate evaluation of the cost impact of policy decisions. I have to be frank and say that I think there is room for some more improvement in that area and it is likely that our report will come to that conclusion. We are saying more rigorous, clearer and more independent evaluation of policy impact. Whatever the decision the Government makes, and of course they are entitled to make them, it is a pity if they do not actually know what the cost is going to be of the decisions they are making.

Kelvin Hopkins: In our papers at one point it suggests that if services were moved back into local authorities and run directly by fairly tightly controlled local authorities with a good elected council, they would actually be run more efficiently, and probably more cheaply, than the way things have gone with hiving off to partnerships and the complexity and plethora of organisations that have been set up for philosophical reasons, I think, rather than financial reasons over the last 10 or 15 years.

Chairman: I do not think you will be offering the sort of advice that Kelvin would like you to advise, nor do I think it is your role to do that kind of thing either, but it is on the record.

Q135 Mr Prentice: You seemed to suggest earlier, Mr Morse, that changing organisations could produce leaner, more efficient organisations, but when I look back over the years we have had endless Whitehall re-organisations which have cost an arm and a leg and delivered nothing. We have had endless re-organisations of the NHS. I have lost count of the number of re-organisations of local government, the millions, perhaps billions that must have been squandered in that way. Have you calculated the cost of all those re-organisations and whether they have delivered a fraction of what was promised?

Mr Morse: Two things. I have not calculated the costs of all those re-organisations, but we have an up-coming report on the machinery of government changes and I think we would be quite interested in the cost of that, let alone anything else.

Q136 Chairman: How up-coming is it?

Mr Whitehouse: We aim to publish in March.

Q137 Chairman: March is good

Mr Morse: We are trying to get a lot of things done by March, for some reason. I am not arguing for an organisation structure change. That is like, "Let us pour the same contents into different buckets." That is not what I am trying to say. I am trying to talk about changing the way you work in the organisation. I am not suggesting that if we just arrange the organisation chart differently everything will be wonderful. No, it will not. You have to work differently, more simply, directly and using management information properly, not, "Let's just fiddle around with the structure." That is not at all what I am recommending.

Q138 Chairman: The Government gave us their *Smarter Government* report just before Christmas, where they are saying they are going to find a further £12 billion of savings on top of the existing efficiency savings programme. Mr Morse, just in the way that you audit the assumptions underlying the Budget, is there an intention for you to audit the assumptions underlying this programme?

Mr Whitehouse: We have a remit at the moment with the existing efficiency programme that was introduced by the Chancellor in previous years. We are having some discussion with the Treasury about it, but there is no firm commitment that we will audit that.

Q139 Chairman: You should have been on our front row, I think. I know we are all over the place but it is all very interesting. Can I ask this as we end, in the spirit of frank and intelligent debate. If we look five years or so down the line, is your judgment that we shall say that we have now got a leaner and fitter, a better motivated, more innovative public sector because of what has happened or that it will simply be worse?

Mr Bundred: My guess is that it probably will be the former rather than the latter. Certainly it is the case that financial management in the NHS has improved greatly over recent years. It is also the case that the quality of management and the quality of services in local government has continued to improve. As Amyas and I have both said, we believe that the cuts that are likely to come are manageable. They are difficult but they are manageable without seriously adverse implications for service quality, and what we also know is that the necessity to make cuts is often a source of innovation in service delivery. I am certainly not pessimistic in any way about the future.

Mr Morse: I will give a slightly different answer. If it is done in a short-term, unplanned way, then I am not optimistic and I do not think that the cost reductions required will be necessarily achieved. If it is done in an intelligent, planned way over a period of time, then, yes, it could lead us to something much more positive.

Q140 Chairman: If we asked the same question about the audit bodies, and if the proposal was over the next five years, in the interests of efficiency, to put your two audit bodies together, would that be a great gain for efficiency or would it be an example of some of the perils of making machinery of government changes?

Mr Morse: I think it is probably more of the latter than the former. I have been through two major mergers in my life. There are some positive things to be said for bringing the bodies together. There are obviously some constitutional and other difficulties about it, but there are some positive things to be said for it. What I would worry about is taking the eye of both of us off the ball for a period of time when there is more pressure on the public finances than at any other time and finding ourselves focused on sorting out all the internal reconciliation problems, and really you should not underestimate how long that takes.

Mr Bundred: When Tim Burr and I last appeared before the Committee you asked us a similar question. I think the answer we gave then is the same answer now. If you were starting with a blank piece of paper, you probably would not design two public audit agencies in England. However, as we have two, there is an onus on both of us to work very closely

together, which we do, so as to ensure that there is no problem that needs to be solved by bringing the two together.

Chairman: Thank you very much indeed for coming and thank you for answering in the way you have done and thank you for the work you do on the public's behalf as well.

Thursday 25 February 2010

Members present

Dr Tony Wright, in the Chair

Paul Flynn
Kelvin Hopkins
Mr Ian Liddell-Grainger

Julie Morgan
Mr Gordon Prentice
Mr Charles Walker

Witnesses: **Rt Hon Liam Byrne MP**, Chief Secretary to the Treasury, **Mr Ben Jupp**, Director, Public Services Strategy and Innovation, Cabinet Office and **Mr James Richardson**, Director, Public Spending, HM Treasury, gave evidence.

Q141 Chairman: This morning we are delighted to have before us Mr Liam Byrne, Chief Secretary to the Treasury; Mr Ben Jupp, Director of Public Services Strategy and Innovation at the Cabinet Office; and Mr James Richardson, Director of Public Spending at the Treasury. Mr Byrne, this will be the last time we do anything like this because we come to the end of things, so it is a particular pleasure to have you here as one of our last guests. Over the past few sessions we have been turning our mind to the implications for public administration of fiscal squeeze. We have taken some interesting evidence on it already and we turn to you last. Is there something you would like to say by way of introduction?

Mr Byrne: Thank you for the opportunity to come along. I want to make three points on what is a very important inquiry; it is one of the definitional questions in British politics for the next few years. First, our starting point is the outlook we have set for public spending. That is clearly set out in the Pre-Budget Report. We have to halve the deficit over the next four years. We do not believe that the business of consolidation should start this year; we think it important to lock in the recovery first which is a view supported by both the IMF and some 60 economists who wrote to the newspapers last week. Second, what we have done in the Pre-Budget Report is set out a plan for how something like £82 billion worth of deficit reduction is accomplished over the next four years. Broadly speaking, about £25 billion of that will come from growth—a return to business as usual in the economy—and therefore about £57 billion is required from discretionary action. We have tried to secure about one third of that £57 billion from tax—£19 billion of tax revenues—of which about half is paid for by the top 5% of earners and about £38 billion comes from spending control. The Pre-Budget Report sets out from where that is to come. Third, what we are trying to do in *Smarter Government* is to set out how the reform of public services needs to proceed alongside that drive for efficiency. Three very simple principles informed the Government: first, we wanted to strengthen the power of citizens with regard to public services, which is why we have tried to set out a series of rights and entitlements to public services backed by a form of redress; second, we wanted to devolve power from Westminster and Whitehall to frontline public servants who are bigger in number and better trained, equipped and

resourced than ever before; and, third, we wanted to take steps to strengthen the power of civic society to help deliver public services. That is why we will introduce a social investment wholesale bank, Mr Denham will bring forward an index of civic health and we will pilot social impact bonds. All of these things have been welcomed by the third sector. We go into the next three to four-year period with some difficult decisions to take but also a degree of confidence because of the investment we have made over the past 10 years. We believe there is a great deal of strength in our public services on which we can now draw.

Q142 Chairman: Thank you for that. It invites us to go everywhere but we shall try to keep our focus. As with other witnesses in previous evidence sessions I start by getting a sense of the enormity of the challenge. All of the other witnesses from the Audit Commission, outside experts and others have agreed that the fiscal squeeze which now confronts us is on a scale we have not seen before in modern times; it is certainly the biggest since the war. Is that exactly how you would describe it?

Mr Byrne: The Chancellor has said that this will be the toughest comprehensive spending review for about 20 years. That needs to be accomplished by October so the budgets are set in time. The Committee may find it helpful if I provide a few comparisons. If one looks at the squeeze in the late 1980s, between 1985–86 and 1988–89 public spending as a share of the economy dropped by about 8.6%. Between 2011–12 and 2014–15 public spending as a share of the economy will fall by about 5.9%. In broad terms the public spending crunch is absolutely the sharpest for about 20 years, but last night as I looked back to the early 1970s in preparing for this meeting it struck me that the years ahead are not as bad as the late 1980s, but it will certainly be the toughest settlement for 20 years.

Q143 Chairman: So, you do not accept what everybody else has told us, namely that this is the biggest fiscal problem we have had in the modern period, not just 20 years but 50 or 60 years?

Mr Byrne: The figures I looked up last night told me that the late 1980s was a slightly tougher period but that takes nothing away from the scale of the challenge. The one point of difference I make is that

uniquely in the postwar era we enter this fiscal consolidation after 10 years of consistent investment.

Q144 Chairman: We know there is a huge hole in the public finances; according to the Pre-Budget Report it is £73 billion. You have issued the paper *Smarter Government*. The other day I heard an IT expert say that we should beware of anything that had “smarter” in its title. Leaving that aside, the paper has a foreword by the Prime Minister in which he says: “In meeting this inescapable fiscal challenge we must ensure that we do not damage the public services on which so many depend.” I put to you the same charge I put to the opposition. That is just not a sustainable statement. You cannot take £73 billion out of the economy to fill a black hole and not do any damage to public services, can you?

Mr Byrne: I disagree with that proposition.

Q145 Chairman: But it cannot be done. If you disagree you are saying that the state is so bloated we can happily take billions and billions out of it and it will not damage public services, which means there is something wrong about how we have been doing it. It is just not logical to say that we can have the biggest fiscal squeeze of modern times and it will do no damage to public services. It is not being honest, is it?

Mr Byrne: I think there is a flaw in your logic. First, we have built up great strengths over the past 10 years. For example, we now know that people want to participate far more in the way their public services are delivered, so there is strength in civic society on which we can draw in years to come. Second, there is an enormous strength in our frontline public services. I give you one very simple example. Over the past 10 years public sector pay has increased. It was a matter of controversy in some circles but I believe it was the right thing to do. In real terms public sector pay has risen by about 25% in the past 10 years. That means teaching is now the number one choice of profession for graduates. I believe that investment over the past 10 years makes it easier for us to say to public servants today that over the next three or four years public spending and therefore pay will be tougher. That was why we said in the Pre-Budget Report that public sector pay would be capped at 1%. That yields a saving of something like £3.8 billion. I believe that is deliverable only because of the investment we have made over the past 10 years. If one remembers that pay is something like half of departmental expenditure one can deliver quite significant savings as the UK economy returns to growth. I do not believe that diminishes or damages one’s ability to deliver public services.

Q146 Chairman: One accepts that all kinds of things can be done to save money and that growth and so on will help, but the structural deficit is such that one knows action must be taken on a scale that has not been seen before in modern times. All I am saying to you is: it cannot be honest to say one can do that

without it having any effect on public services. It is just not possible, is it? One has to say there will be pain and difficulty.

Mr Byrne: There will be a degree of pain but I do not think it damages the ability to deliver good public services. Let us take another example. In the case of higher education we have said we want to save from BIS¹ something of the order of £900 million by 2012–13. That is a saving of £600 million in HE² that we would like to make. You can make that saving, for example, by asking employers to increase the number of courses that they co-fund and changing the mix between full-time and part-time students. I do not believe that is damaging to public services. It is a painful decision and it would be nice not to have to take it, but I believe that in 2012–13 HE will remain very strong.

Q147 Chairman: Let us be simple about this. There are lots of holes in the road at the moment aggravated by the winter weather. This is broken Britain. Just drive around and you will find it. On any sensible view of this we will have less money to fill the holes in the road. If so, the quality of our public provision, let alone our cars, will be damaged. It is just obvious, is it not?

Mr Byrne: I do not think that follows.

Q148 Chairman: Of course it is obvious.

Mr Byrne: I do not believe that is a sufficiently sophisticated way to look at this problem. To take the question of pay, it is perfectly obvious that given 10 years of good pay increases we are now in a different position with our frontline public servants and can say that over the next few years they will get pay rises of either zero or something under 1%.

Q149 Chairman: When in doubt call in the IFS; they know what they are talking about. I have a piece written by two experts from the IFS which appeared just this week in *Public Finance*. They go through the figures and make the obvious point that big cuts are coming. If you say that you will protect some services the bigger cuts will come in the unprotected services which is just logic. They say: “The cost of protecting some areas is that other departments’ spending will have to be cut more. We estimate that by 2012–13 the budgets of the unprotected areas are likely to be cut, on average, by 13% relative to what they are set to enjoy in 2010–11.” These are people who know what they are talking about. Are you really saying that you can cut the budgets of unprotected public services on that scale and it will have no effect on the quality of those services?

Mr Byrne: First, the IFS makes a number of assumptions in the way it arrives at that number. Crucially, it makes an assumption about the share of money available for the benefits bill and for departmental expenditure. You will be aware that when we write a budget we use an NAO assumption that basically takes in today’s level of unemployment which means that in the budget figures and NAO forecasts the number of people

¹ Business, Innovation and Skills

² Higher Education

unemployed up to 2014 is about 1.94 million. What we did for the first time in the budget was to say that we thought unemployment would be much lower than that, namely about 1.25 million. The only point I make is that if unemployment turns out as we predict that is a saving in the benefits bill of something like £10 billion. We can use that money either to pay down the deficit or for other things. That is just an example of how the IFS has made some simplified assumptions and you have to be careful about the way you use that figure. On the question of unprotected departments some things will have to stop. If you are asking whether public services delivered by unprotected departments will be “damaged” or those departments will be required to stop doing things they are currently doing the answer is yes, but in broad terms you can improve the quality of public services in the round with less money. That is something the business community has to do every year.

Q150 Chairman: But you started by telling us that the Prime Minister was right to say there would be no damage and now you have come round to say there will be damage in these unprotected areas.

Mr Byrne: If you are talking about public services in the round there will not be damage to the way we deliver them. There may be some things you have to stop doing but you cannot simply extrapolate from that and say, as Mr Alistair Darling puts it, there will be a plunge into the Dark Ages because we now have to take some difficult decisions. If you look at pay, IT, consultants and marketing, savings on energy et cetera it is perfectly possible to make careful savings in the administration of government that protect and enhance the quality of public services.

Q151 Chairman: We are all in favour of that, but every witnesses who has come before us so far in this inquiry has demanded honesty from both government and opposition and believes they are not getting it. The IFS knows what it is talking about. You may have a little quibble about its assumptions but you pray it in aid when you want to do so. Let us assume the IFS knows what it is talking about. It continues the argument by saying: “The government has not indicated whether its ‘protection’ of parts of the NHS and education would carry on beyond 2012–13. If it were continued for a further two years, the budgets of unprotected departments would be cut by an average of almost 25%.” That is just logical, is it not? You cannot tell me that a 25% budget cut in an unprotected service will not produce some sort of serious impact.

Mr Byrne: You are now into speculation about what the next spending review holds. We have not set our departmental expenditure limits beyond 2010–11 for the very good reason that we do not know with certainty the provision for the benefits bill and therefore how much is available for departments. It is perfectly correct we have said there are things we want to protect out to 2012–13, but given the level of uncertainty in the economy about growth rates and

unemployment I do not believe that now is the right time to take a view about what will happen to departments in the year after the Olympics.

Q152 Chairman: Government and the opposition are cheating the electorate, are they not? It is like a surgeon who asks his patient whether he should cut off his leg today or tomorrow. The patient wants to know why the leg is to be cut off, whether it will hurt and how long the pain will last. He does not really care whether it happens today or tomorrow; he wants to know what will happen. People want to know what is to happen to their public services over the next five-year period. Although we are talking in global terms we are asking them to vote without telling them on the basis of a claim that there will be no damage when we know there is to be damage. The holes in the road will not be filled.

Mr Byrne: There are uncertainties in the economy. We introduced comprehensive spending reviews not long after we came into office because we wanted to get away from the old Conservative way of conducting annual spending rounds. We wanted to provide public servants and managers with three-year certainty. Given what I have said about the difference between what might happen to unemployment benefits and the assumptions we had to make in the Budget, let us say for the sake of argument that there is a gap of £5 billion, unemployment reduces as we expect, interest rates stay good and there is a £5 billion windfall. Five billion pounds is bigger than the budget of at least five government departments, so as unemployment starts to come down and interest rates stay good you will have to reopen a three-year settlement, thereby destroying the certainty that is the very objective of comprehensive spending reviews.

Q153 Chairman: I can assure you that the IFS understands all of this, but even if you make the most benign assumptions about what may happen we have a hell of a problem and nobody dissents from that apart from you possibly. Nobody dissents from the fact that it will have serious implications for public services and we should tell people about it.

Mr Byrne: We have set out very clearly in black and white in chapter 6 on pages 108 through to 113 of the Budget those things the departments have to stop doing and those things they must delay.

Q154 Chairman: Will the March Budget fill in all of these details?

Mr Byrne: The March Budget will provide further details of how, for example, *Smarter Government* savings will be distributed between departments.

Q155 Chairman: Will it specify what hits departments will take?

Mr Byrne: It will not set departmental expenditure limits beyond 2010–11 because of the uncertainty that remains. It is not a comprehensive spending review.

Q156 Chairman: It is strange that broadly everybody who has come before us over the past few weeks—experts from the Audit Commission and National Audit Office and independent commentators—has to a man or woman given an account of events which leads to a conclusion different from yours. Is that not striking?

Mr Byrne: I do not think it is.

Q157 Kelvin Hopkins: Fiscal policy has two components: expenditure and revenue. I have some figures before me which suggest that up until the past month central government spending had increased year on year in real terms by about 5% to 8% but revenues fell in the same period by 10.2%. There is a chasm. We have fallen off a cliff edge in terms of revenue collection. If we could address that we could seriously overcome most of our problems, could we not?

Mr Byrne: Yes.

Q158 Kelvin Hopkins: We have to separate out cyclical deficits, which happen whenever there is a recession. You mentioned the late 1980s when public spending fell. That happened simply because unemployment was falling rapidly in the time before we joined the ERM, which was daft. Everything went well because the Tories were expanding the economy out of the recession in the early 1980s. Unlike other countries, we have also cut corporation tax substantially since 1997, unnecessarily I would say, to the point where we now collect £6 billion a year less in corporation tax than we did before. That £6 billion matches almost exactly the difference between tax revenues and spending. Would it not be a good thing to raise corporation tax?

Mr Byrne: I do not think it would for the very simple reason that over the next four years much of our deficit reduction plan depends upon the return of growth in the economy. If you look at China, this year its growth rate is about 8.5%; India's is not massively dissimilar. If we want to rebalance our economy towards investment and export-led growth over the next few years it is important that we are able to trade our way through this and attract more foreign direct investment. We are already the world's second best place for FDI.³ About \$1 trillion of FDI is now in the UK and that creates and supports about one million jobs. One of the reasons people like doing business in the UK is the regulatory environment, flexible labour market and also reasonably low rates of corporation tax. The argument I make is that if we want to continue to attract that investment in future, particularly as we try to exploit further markets, we need to remain a good environment in which to do business. Just 3.6% of UK trade is with China. We are at the very beginning of our relationship with that enormous growth market, but already the UK is one of the favourite homes for Chinese businesses locating in Europe. We want to preserve that competitive position because it places us well for global growth in years to come.

³ Foreign Direct Investment

Q159 Kelvin Hopkins: That sits alongside the fact we have a weaker economy than Germany and a massive trade deficit with Europe and the rest of the world. Let us look again at revenues. The statistics that came originally from Richard Murphy and others suggest that tax avoidance loses us £25 billion a year; tax evasion loses us £70 billion a year; and uncollected tax amounts to £27 billion to £28 billion. Half of that is not collected by HMRC simply because it does not have the resource to chase it. The estimate of the tax gap is £125 billion a year. Obviously, we will not collect all of that, but if we just addressed the tax gap and went for, say, one fifth of it—£20 billion or £25 billion—that would solve all our problems. We also have tax relief on savings to the rich which amounts to £20 billion and £30 billion. If we cut back on some of that we would have a massive increase in income and solve all our problems, but we refuse to face up to it. We never talk about revenues; we always talk about spending. Is that not the solution to our problems?

Mr Byrne: I strongly agree with your point about the tax gap. It is a constant job of work and in part is the reason we were so keen as part of the G20 accords to go further in closing tax havens. I believe that will remain an important feature of HMRC's policy reform work over the years to come. We have to be constantly on the look out for new ways to approach this. For example, the TUC has proposed some general anti-avoidance principles which warrant serious study, but on the point about tax reliefs for the well off what we have tried to do in introducing £19 billion of tax increases over the next three or four years is load over half of that new tax take on the top 5% of earners in the UK. That has been accomplished to some degree by the introduction of a new 50p rate, but in addition a lot of money comes in by way of the introduction of reform of pension relief. We have conducted a degree of rebalancing though perhaps not as much as I suspect you would like, but we have sought to introduce these new taxes in a fair way.

Q160 Kelvin Hopkins: I would like to go further than that. Apart from corporation tax, I am not talking of changing tax rates but about collecting the tax that could be collected and which would solve all our problems.

Mr Byrne: I agree that remains a problem.

Q161 Kelvin Hopkins: On the expenditure side, the personalisation of budgets with the splitting up of spending into tiny pots, giving them to elderly people to try to negotiate their way through services, will cost a lot of money. Over the 30-year period of PFI⁴ it is estimated that it will cost the public purse £300 billion. Nuclear weapons in my view are unnecessary. That would save £70 billion. Outsourcing in the form of contracting, subcontracting and sub-subcontracting costs money, as indeed does the privatisation of the

⁴ Private Finance Initiative

railways. If all of that is brought inhouse and integrated we would also save billions of pounds of public money. I could go on. There are things we can do without touching core public services at all.

Mr Byrne: Here I strongly disagree with you particularly on the personalisation of individual budgets. When I was social care minister I introduced individual budgets having spent a great deal of time with children's charities in particular who were able to introduce me to families whose care, frankly, had been the subject of a complete run-around by different carers anonymous to them who did not provide the quality of care their children needed. The introduction of individual budgets allowed them in some instances to hire extended family members to provide a consistent quality of love that hitherto had been pretty difficult to secure. I have met many people, both young people with disabilities but also older individuals, whose quality of life has been completely transformed by individual budgets and if anything I am determined to see them go further. My only observation as Chief Secretary is that they are remarkably cheaper to deliver than local council provision and we now have pilots to prove that. Equally, on outsourcing there are parts of public administration, particularly in the back office—pensions administration and finance administration—that can be executed much cheaper by the private sector and the third sector in some cases. I think that is an agenda that should remain an important part of public service reform.

Q162 Kelvin Hopkins: As to the question of trying to get the third sector to take up public services, in the past few days an article has appeared in the *Guardian* entitled "Charities 'in crisis' as spending cuts bite". The fact is that charities in the third sector are in a state of crisis and collapsing. It says that, "Struggling workers [are] leaving for jobs in supermarkets." Is not looking at the third sector simply a blind alley?

Mr Byrne: No, I do not think it is. Spending in the third sector under this government has doubled and as a result that sector is in a much stronger position. The head count has increased by about 25% and it is conducting far more work in public services. But the way to go about working with the third sector needs to change in many local authorities. I give you the very simple example of Birmingham City Council. At the moment that authority is, to the best of my knowledge, cutting back on the way it supports the third sector; it is laying off about 2,000 staff, yet it has just spent £1 million on a giant television screen that it has never switched on and is spending hundreds of thousands of pounds on consultants and temporary staff every week because it cannot get sufficiently organised to hire, train and properly look after permanent staff. There are a number of efficiencies people in public services should seek to make before they start to shut down frontline services. In a way that is really at the heart of my answer about how public services can improve in the years to come despite the tougher fiscal climate.

Q163 Mr Walker: Referring to the pressures between spending and tax rises, are there any areas of the economy which you still feel are undertaxed?

Mr Byrne: I would need to think about that question. I try to steer clear of questions of tax; otherwise, I will get into trouble with the Chancellor.

Q164 Mr Walker: Let us look at infrastructure which is important as is the protection of frontline public services: doctors, nurses, teachers and so on. In this country there is a need constantly to update and improve our infrastructure and I think there is general acceptance that perhaps over the past 30 or 40 years we have been relying too much on the Victorians and not paying our own way. What is the position on infrastructure investment? Let us take rail or road as an example. Where do these things fit into your list of priorities to receive some funding in the future?

Mr Byrne: We are spending a lot on capital this year. You are right to say that investment in infrastructure is an important part of how we grow in future and that is why ideas like high-speed rail are so interesting and why a third runway at Heathrow is needed. This year the amount being spent on capital is very high as we have brought forward a lot to help fight the recession, but our plan is to wind down the amount we spend on capital as part of the deficit reduction plan. I shall ask Mr Richardson to say a word about where those numbers are in the Pre-Budget Report. The level of capital spending we project in 2013–14 would still be twice as high as the level in 1996. Some very difficult decisions will have to be made on capital. Once you have built a school or hospital—we have built 127 of them—you do not need to rebuild them, but I cannot deny there will be difficult decisions to be made on that.

Q165 Mr Walker: But these schools and hospitals have been built and I understand some use has been made of PFI moneys. What risks to the nation's balance sheet does PFI pose as far as concern repayments? I do not intend to make a political point here because I know that John Major looked at PFI when we were in power.

Mr Byrne: When PFI schemes are presented to us obviously we look at value for money but also affordability. Therefore, we will take into account the level of spending required to service a PFI contract. We will approve only those schemes that we believe are affordable in the medium term.

Mr Richardson: Capital budgets they are set out in a number of places, but the clearest exposition would be in table B13 of the PBR at page 189. That sets out the numbers in billions of pounds for capital on both a gross and net basis.

Mr Byrne: We said in the PBR that we would focus capital spending in the next spending review in those areas that "generate high economic returns to achieve maximum long-term benefit to the taxpayer".

Q166 Mr Walker: When you are talking to department heads about their spending plans how do you manage those discussions? What disciplines

do you expect them to incorporate in their presentations to you so they are all competing in a sense on a level playing field and you are getting the same information from each department as opposed to what they want you to see?

Mr Byrne: They are all delighted to hear from me as you would expect. We expect them to deliver a number of things. First, we expect them to get the efficiency of their finance, IT and HR operation up to the upper quartile of public sector performance. Some departments at the moment are a long way off that and they will have to do some things in a radically different way in future. Second, we expect all departments to make a contribution to reducing the senior civil service by 20%. Third, we expect them to halve their consulting bill. Fourth, we expect departments to reduce their marketing spend by 25%. Fifth, we expect them to sell assets that they no longer need. Sixth, we expect them to start to procure things no longer on their own but collaboratively. Seventh, we expect departments to reduce their energy bills. There is a whole range of efficiencies that we believe could together add up to £11 billion worth of savings and on which departments are grilled. We will publish more about what each department is doing on that front at the Budget.

Q167 Mr Walker: Departmental power has been devolved to a lot of quangos as they are called. How are you dealing with quangos? Are you being fairly ruthless by telling them what they will get next year and what they will have to live with? Is it a consultative approach? How are you telling these people, who over the past few years had money pumped to them pretty much without any questions, that the good days are over and you expect them to pull their weight?

Mr Byrne: We have to separate the money that is routed to the public through quangos from the admin spends of quangos. I have set the target of reducing the admin spend of quangos by £500 million by 2012–13 and that will involve shutting down quite a lot of them. About 123 have already been identified for closure or rationalisation and I want to be in a position to announce more in the future.

Q168 Chairman: But we opened them up because it was believed to be a more effective way to conduct government. We are now closing them down because it is believed to be a more effective way of doing it.

Mr Byrne: I think there is a question about whether you really need 16 regional advisory committees related to agricultural workers, 101 such bodies on justices of the peace and 23 court boards.

Q169 Chairman: But these are ones that have survived every previous review of quangos.

Mr Byrne: Or an advisory committee on wine purchasing.

Q170 Chairman: We have had fun with this for years and years.

Mr Byrne: Then it is time to close them down.

Q171 Chairman: But we have had all this before from endless governments for endless years. To go back to Mr Walker's point on capital spending, we took evidence from Tony Travers, who is also someone who knows what he is talking about. This week he wrote a piece in which he says: "... the government is planning to take the axe to investment in transport, roads, house building, hospitals and other infrastructure. This decision is surely wrong, and cannot be explained away by pointing to 'record levels of investment' in recent years. Britain, by virtue of its history, has some of the creakiest public assets in the world. Competitor economies in the Far East are building railways, metros, roads and urban infrastructure at an accelerating rate. Are the 2010s really such a good time to be cutting back on public investment in basic infrastructure?" Is that not a good point?

Mr Byrne: But the point I make to you is that the spending we project on capital as a fraction of our national economy even by 2014–15 will be more than double the level we inherited in 1997. It is coming down this year from 3.5%, which is pretty much a record, but it is by no means being eliminated because of the point that lies behind your question and Mr Walker's. Historically, as a country we have under-invested in infrastructure and that is not a mistake we plan to repeat.

Q172 Chairman: I am trying to get you to admit that there will be holes in the road.

Mr Byrne: I know.

Q173 Chairman: We shall meet periodically and I shall tell you about the holes.

Mr Byrne: Is this in Cannock Chase?

Q174 Chairman: This is everywhere I go. Have you not been round in your ministerial car? Do you not notice that it bumps around a lot?

Mr Byrne: I would go by public transport.

Q175 Julie Morgan: How do you define a frontline job?

Mr Byrne: It is very difficult. The way we have defined it in terms of the protections we want to apply and make provision for in years to come is to say we will protect spending on the National Health Service at the level of inflation, increase spending on schools and 16 to 19 above the rate of inflation and provide police forces with enough money to protect the level of warranted officers and PCSOs. I accept that it is a crude way to define frontline services. For example, if you work in a jobcentre you will feel that you are in the frontline. Jobcentre and tax offices are areas where we want to make a saving of about £500 million by moving to digital delivery. That will involve DWP and HMRC shedding staff over the next few years. I accept that it is not a perfect or sophisticated definition of "frontline".

Q176 Julie Morgan: When you talk about the NHS and education to which frontline jobs are you referring?

Mr Byrne: In part that must be a question for individual trusts. I give you an example from Birmingham. My view, rather than Andy Burnham's, is that there is a very strong case in Birmingham for a single primary care trust whereas there are three at the moment. If one created one primary care trust one could make quite considerable savings in the number of people on boards, chief executives and those involved in finance, HR and IT. Therefore, some jobs in those areas may have to go. Is that frontline NHS? I believe it is a difficult definitional question.

Q177 Julie Morgan: There is fear among some people, for example police officers on the streets who deal with people on a daily basis, that to cut administrative jobs or back-up will increase the burden already on them. I just wondered whether you had been thinking about those sorts of issues.

Mr Byrne: If one takes the example of the police, Alan Johnson has said there needs to be about £428 million in productivity and efficiency improvements in the police by 2012–13. He has often spoken of the example of overtime and believes that about £70 million can be saved on that account. Equally, I am aware that in Birmingham the new chief constable is reorganising the basic command units which may well involve shedding staff in management or administrative roles. What we have tried to do in the case of policing is to see how much is being spent on warranted officers and how much on PCSOs and say that we will protect those budgets for the immediate years to come. But I believe that in schools, the NHS and in policing there will be job losses in management and back office positions.

Q178 Julie Morgan: You referred to reorganisation. Reorganisations appear to have gone on endlessly. How can you be sure that the reorganisations will be to the benefit of the frontline work?

Mr Byrne: It is a very different fiscal environment and departments have to agree some tough efficiency savings. To an extent it is not my job to tell a department how it should save money but to give it a figure and ask for its plans to deliver that saving. In broad terms what cabinet colleagues are doing is looking at how they can protect and enhance the quality of the services that are delivered but to thin out back office costs. New technology provides different ways of doing things. One can now share finance, IT and HR staff far easier than was possible a few years ago.

Q179 Julie Morgan: It is crucial that some management jobs are retained in order to direct services in the right way. Have you thought of the danger of cutting back? You have to be very specific when you cut back; otherwise, the frontline workers will not have the direction and support they need.

Mr Byrne: That is a very fair point. Historically, we have argued that in years gone by the NHS was under-managed. The NHS now, as I am fond of

saying, is the world's 33rd biggest economy; it is an economy almost the size of Argentina. It needs strong, good management, so we have to be careful not to overdo it.

Q180 Chairman: Does it not come back to the "honesty" point? We say "frontline" because it sounds cuddly; the same applies to "hard-working families". We never talk about those that are not hard-working. If I see a doctor that is great but I can see a doctor only if someone makes the appointment for me. Is the person who makes the appointment a frontline worker? "Frontline" requires "backline". We say these things because it produces a warm glow but just avoids telling people the truth, does it not?

Mr Byrne: I do not think it avoids telling people the truth, but sometimes one needs shorthand in politics.

Q181 Paul Flynn: Shared services have been a great success as far as concerns the Prison Service and others, but the Government did not proceed with a plan for shared services in the Ministry of Justice or other departments. Have you fallen out of love with the advantages of shared services?

Mr Byrne: No, and at the Budget I will present a list of departments that will move towards shared services.

Q182 Paul Flynn: On the recommendations of the Lyons Review about moving jobs out of London, there is a similar argument in relation to the use of shared services. I think the figure of 20,000 was quoted but it has not yet been achieved. The jobs that have been moved out, for instance in the Office for National Statistics, have not lived up to the promise. There is a completely inexplicable reluctance on the part of people to leave the concrete of London for the green fields of Newport, for instance. Is this something that you look to press ahead, because it is something that meets lots of the objects of government departments.

Mr Byrne: Newport is a very attractive place to do business. If anything we need to be more ambitious about moving jobs out of central London in the years to come. I hope to be able to present a revised goal at the Budget. We need to approach relocation in a different way from the past. It should not simply be a numbers game. Numbers are important but we should have further ambitions. If we want genuinely to contribute to regional economic development we should be looking much harder at what particular strengths different regions have and ask ourselves whether there are particular government departments or civil servants we should seek to move into those regions in a way that helps them strengthen their economic fundamentals in addition to saving money. That is the approach being taken by Ian Smith in the review of relocations that he is conducting for me at the moment. I believe it gives us a new advantage, not just in contributing to the employment situation in different parts of the country but also in strengthening their economic fundamentals for the future.

Q183 Paul Flynn: One of the great black holes of government that appears to have been created over recent years is the way billions of pounds have disappeared into consultants and IT schemes that have lost huge amounts of money. What are we going to do about that?

Mr Byrne: That is a very fair criticism. For that reason we have said about £500 million of savings need to come from reduced spend on IT, including the National Health Service's IT system. We have also said that the consulting budget needs to be halved right across departments because as a former consultant I believe too much public money is spent on consultants.

Q184 Paul Flynn: A difficult area is how the Government responds to world hysteria on various issues: SARS, CJD, the millennium bug, avian flu and recently swine flu. We spent £1 billion on preparations for swine flu because of a warning given by the World Health Organization. The argument is probably with that body. Poland spent virtually nothing and the outcomes in the two countries have been almost the same. I appreciate the argument that you are damned if you do and damned if you do not. If the virus had mutated as expected there might have been tens of thousands of deaths. The spending took place in the belief that there might be 65,000 deaths. We now know that at most there were only 400 deaths the majority of which, but not all, resulted from swine flu. Clearly, the threat was massively exaggerated and the result was to distort our priorities in the health service, frighten the whole country witless and take money out of the NHS. This is the fourth of fifth major hysterical scare that has afflicted the whole planet. Is there anything we can do to provide a service that detects these risks and gives an objective and intelligent warning? In this case it appears that the scare was driven by the needs of the vaccine manufacturers to get a return on their investment. Their tentacles of influence are everywhere. That might well be the explanation. It certainly was not based on the epidemiological evidence from Mexico. Should we not protect ourselves from this? It appears that in this case we have overreacted in our preparations.

Mr Byrne: We have a pretty good method of contingency planning in Britain. The Civil Contingencies Committee tries to bring good and objective civil servants and scientists together to make these preparations. In the case of swine flu obviously the civil servants included the Chief Medical Officer, Sir Liam Donaldson. I think that it was right to err on the side of caution, not least because if had been an epidemic there would have been tremendously serious health consequences. We should not overlook the fact that there would also have been tremendously serious economic consequences. To have a large number of workers taken out of the workforce in the middle of the worst recession for 60 years would have been very damaging. I am not sure there is a perfect answer to

this other than to try to bring together the best minds in the business. Ultimately, politicians have to take the decision and be held accountable for it.

Q185 Mr Prentice: You told us that the Government planned to cut the deficit by half in four years and that £25 billion would come from growth. What growth rate in the economy would deliver that?

Mr Byrne: The growth rate that we project in the Budget is 1% to 1.5% this year followed by a couple of years of 3% to 3.5%.

Q186 Mr Prentice: Do you believe that is deliverable? That almost seems like China's rate of growth.

Mr Byrne: It is pretty consistent with the growth rate we experienced when emerging from the past two recessions. I believe it is slightly lower than the Bank of England's estimate for next year.

Q187 Mr Prentice: You told us earlier that because life had been so good for public sector workers they would be prepared to make sacrifices. Those are my words, not yours. You said that over the past 10 years there had been a 25% real terms increase in public sector pay. People in the public sector compare themselves with the private sector and vice versa, so what was the real terms increase in private sector pay over the same period?

Mr Byrne: Twenty-two per cent.

Q188 Mr Prentice: I go back to Kelvin Hopkins' point about the tax gap. Speaking from memory, the document *Protecting Tax Revenues* produced by HMRC in December 2009 talked about a tax gap of £40 billion. To what extent can we squeeze down that gap? We are asking people to make sacrifices and yet a huge sum of money goes uncollected, so how realistic is it to squeeze that tax gap of £40 billion down to £10 billion?

Mr Byrne: Let me get a properly informed answer to this from the Financial Secretary because I agree with all of the instincts behind that question.⁵

Q189 Mr Prentice: Did you read the editorial on Monday about taxation and citizenship?

Mr Byrne: No.

Q190 Mr Prentice: Uniquely, the United States uses citizenship as the basis for taxation.

Mr Byrne: It is based on worldwide taxable income.

Q191 Mr Prentice: Yes. My question is: why can we not say to all UK citizens, whether they live in Belize or wherever, that they will be taxed on the basis of their worldwide income instead of on the basis of "domicile", "UK resident for tax purposes" and "UK residency" which allows smart people with smart lawyers to avoid paying tax?

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Mr Byrne: It is a great question.

Q192 Mr Prentice: Give me a great answer.

Mr Byrne: I am not a tax expert, so I will get you a great answer from Mr Stephen Timms.⁶

Q193 Mr Prentice: On the question of consultancy spend raised by Mr Walker and Paul Flynn, you tell us in *Smarter Government* that you will reduce the amount by 50% but it qualifies it by saying “for the longer term”. When will it happen?

Mr Byrne: By 2012–13.

Q194 Mr Prentice: What happens in those departments where people have been thinned out and they just do not have the capacity to deliver? Are you seriously suggesting that the option of resorting to outside consultants will no longer be there?

Mr Byrne: That is the reality we are in. To be honest, I do not see why departments cannot source the expertise they need from civil servants, but it requires us to change the way we hire and train civil servants. We need a much stronger mix of delivery skills. There are still not enough permanent secretaries or senior civil servants who have run things either in business or in the third sector and that must change over the next few years. I have always believed that you cannot separate good policy advice from good delivery skills. I learnt this in spades at the UK Border Agency. The agency was very concerned to send a signal to great staff coming up through the ranks that if they wanted to do really well they needed to get some delivery experience. The reason we started to recruit some of the best grades 5 and 7 was that there were not enough places in Whitehall where one could make the transition from policy advice to delivery.

Q195 Mr Prentice: I understand all that. My question is whether what you and the Government are planning is really deliverable. We are not to go out to consultancies because the expertise will be inhouse. With the publication of the capability reviews it is now in the public domain that there are failings across all government departments. You tell us in *Smarter Government* that you will consolidate the senior civil service over the next three years, whatever that means.

Mr Byrne: It means to cut them by 20%.

Q196 Mr Prentice: That thinning out should release savings of £100 million per year. You will have fewer people; departments will be thinned out and you will still be able to deliver all of this?

Mr Byrne: Yes, and we can do this by moving a lot more responsibility out of Westminster and Whitehall and into regions and local government.

Q197 Mr Prentice: You told Julie Morgan that you thought one rather than three PCTs would do in Birmingham. Is that because PCTs would just have a commissioning role and would no longer deliver

frontline health services, if I may use that expression, because that is part of the Government’s agenda, is it not?

Mr Byrne: No. I think there are a large number of occasions when PCTs should take on the direct delivery role. I would not want to assume that PCTs have a monopoly of wisdom on how community health services are delivered, and Andy Burnham has been very clear about that.

Q198 Mr Prentice: There seems to be a constant revolution. It is Maoist, is it not? If we look at reorganisation of the health service you are at it again. You cannot help but say you want to see one instead of three PCTs; you are never happier than when you are reorganising things.

Mr Byrne: I am just confronting the realities of how to protect the quality of services people deliver at the same time as halving the deficit over the next four years.

Q199 Mr Prentice: As to health I want to ask about capacity constraints. There is a guarantee, with which I am happy as a Labour MP, that people will be able to have cancer diagnoses within a week rather than two weeks. Are there any capacity constraints within the health service that will prevent that being delivered?

Mr Byrne: We believe it is deliverable. What we have tried to do is write these entitlements and guarantees alongside a conversation about money. We believe that the guarantees we have written are affordable within the funding settlement we provided for the Department of Health up to 2012–13. Andy Burnham has also said he believes that about £10 billion worth of efficiencies can be secured within the National Health Service, for example by reducing the kind of management costs I have talked about and bringing more expensive hospitals up to the level of good hospitals. The example I have provided is Birmingham. When Heartlands Hospital took over Good Hope Hospital the latter’s quality of care improved and a month-on-month deficit was returned to a surplus, so good management can make a difference to both the quality and efficiency of services.

Q200 Mr Prentice: Are we hoodwinking the public by using the term “guarantee”? On page 21 of *Smarter Government* all sorts of guarantees are listed: one-to-one tuition; a personal tutor for every secondary school pupil; a school leavers’ entitlement, and so on. What happens if the guarantees are not met? There is no legal remedy. You cannot enforce the guarantee?

Mr Byrne: I will ask Mr Jupp to say a word about redress because it is something the Chairman and I have talked about before on which the Committee’s advice would be very welcome. If one takes health as an example, the kind of process put in place to provide redress and enforcement of the entitlement is the NHS complaints procedure, followed by the Ombudsman and then judicial review, so ultimately for health there is legal enforceability. Obviously, the way in which these redress mechanisms work is

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different in different public services. For example, one of the conversations we have had in the past is about redress mechanisms in policing. Is the right to ask a local police commander to come to a meeting and have an argument about beat patterns sufficiently tough? That is where we are at the moment and it is a good start, but perhaps we can go further.

Mr Jupp: This Committee has in the past in part championed the way in which Government should simply highlight some existing rights and entitlements enjoyed by people and publicise and communicate them much better. Some of the things in the NHS Constitution and the Pupil and Parent Guarantee do that. Through that one gets quite a lot of change without enforcement mechanisms. We have seen that in the UK and in other countries. Alongside all the new rights and entitlements that have been developed we have been strengthening redress mechanisms in one way or the other. The obligation on PCTs to take all reasonable steps to provide an alternative provider if health guarantees have not been made is a simple way to try to resolve the problem quite quickly first and then there are back stops if that is not resolved.

Q201 Chairman: As you have said, this Committee has been an advocate of guarantees over the years; indeed, long before the Government became interested in them. For a long time we could not persuade you but you got there eventually. Our feeling all along was that with all their merits there would be some kind of cost attached to them. Therefore, as we are talking about fiscal squeeze I wonder whether you see this guarantee or entitlement approach carrying a cost and you can be open about it. As picked up in the previous question the danger is that the worst prospect would be if something was described as a guarantee, raised expectations because of that and it turned out not to be a guarantee. I think that is the bit on which we would like more reassurance.

Mr Byrne: On the funding side I hope that the provision of guarantees is a way to begin to retire the whole battery of indicators and targets currently operated by Whitehall which creates inflexibility for public servants who are trying to do the best thing. In the Total Place Mr Denham is running we have been testing the concept of providing frontline managers and public servants with more flexibility in the way they do their work. Some parts of the country, of which Coventry and Warwickshire are examples, say to us that if we relax and get rid of a whole lot of these indicators they can do things radically cheaper because the siloed way of doing business at the moment is expensive. I am very interested in that, but the social democrat in me would worry about what would happen to equity if we just got rid of a whole load of targets and national indicators. I believe that rights and entitlements is one way through this. This is not something we have made up; we have genuinely learned from your Committee and we have also studied the position in Finland, Sweden and to a degree Canada. The provision of rights and entitlements allows us safely

to get rid of indicators and targets and give frontline managers and public service workers a lot more flexibility and, frankly, job satisfaction in how they perform their tasks and the kind of innovation they can bring to work every morning.

Q202 Chairman: But are there costs?

Mr Byrne: I believe they can lead to savings. They can allow us to get rid of a lot of silos which appear to be very expensive. That is not a conclusion I have cooked up; it is genuinely what participants in the Total Place pilots tell us.

Q203 Mr Prentice: Going back to *Smarter Government*, you tell us that you will publish by the spring of this year details of how the fiscal stimulus announced in the Pre-Budget Report 2008 has been spent but disaggregated to local level. Just how local is “local level”?

Mr Byrne: I am trying to get it down to constituency level, but it may be local authority level.

Q204 Mr Prentice: I approve of that. My final question is about all this data that is to be released into the public domain. Do you see any dangers at all in putting this data into the public domain, or does it need interpretation, caveats or health warnings?

Mr Byrne: That is a very good question. Obviously, there is a boundary around personal data which cannot be released. The question of health warnings is a good one. A good example is financial data. I am quite keen that we get out much faster information about what public servants and people like me are spending money on. I would like to get into a position where the Civil Service, local authorities, NHS et cetera publish information as rapidly as possible—daily, weekly, monthly—about what they have spent taxpayer’s money on in as a great a detail as possible. It may be that more detailed explanations have to be provided about what the money was spent on. That is just an example I have in mind at the moment where we may need to add caveats and additional bits of information that currently are not available. I think the thrust of your question is right. I would probably need to look at what data is now being published on data.gov.uk to see whether or not it has addressed it.

Q205 Mr Prentice: I do not know what additional data will be put into the public domain but sometimes even the data now in the public domain makes me a bit nervous at neighbourhood level because it allows people to draw conclusions, perhaps erroneous ones. There is data on unemployment levels and benefit claims with details of ethnicity superimposed and so on. That is at a very local level. If you are pumping out more information you can have very graphic profiles of very small areas that people could exploit.

Mr Jupp: In most public services we are improving both the interpretive data with some description and the raw data. If you think about schooling, we

provide school report cards which are in a really accessible format and will also contain some commentary. Likewise, there are police report cards. There are recent crime maps which have had about a million hits in the first few months. They are provided in that way and will also provide guidance. But alongside that data.gov.uk already has about 2,500 data sets. There are caveats; there are ways in which we ensure individuals cannot be identified through it, but much of this data could have been available through FOI requests in one form or another and was available somewhere. This allows it to be used and interpreted. I am sure there will be some misinterpretation, but what we have seen from around the world and in the UK already is that the vast majority of it is used to come up with good solutions about how people can improve public services.

Q206 Mr Walker: Mr Byrne, you are a hard man of business. Now you are Chief Secretary sometimes do you wonder when you look at the department what has been going on there for the past few years? I think there is a steely determination in your voice to start taking a scythe to the quangos you talked about and what you regard as waste. On occasions have you felt frustrated that things have been allowed to reach the level they have got to?

Mr Byrne: I have come across examples where departments could have acted faster.

Q207 Mr Walker: What skill sets do you believe departments lack? Like many colleagues, I believe there is great nobility in the career of a civil servant who wants to serve his or her country. I share the Chairman's and Committee's concerns that we do not want to bring everyone from outside the Civil Service to fill senior jobs. There must be some disciplines within the Civil Service where there is a shortage of skills around managing finances and expenditure. Would that be a correct analysis?

Mr Byrne: This is a very important argument. I have worked in both public service and in business. I think we need more people from business backgrounds working in public service, and vice versa. There is still too great a divide that one does not observe in America. But civil servants have unique skills that people coming in fresh from business often struggle with, particularly in the way basic requirements like accountability to Parliament are understood. There is no one right answer. I would like to see a better mix of people at senior levels, but I should also like to see the Civil Service do a better job at giving younger civil servants delivery experience and training. The truth is that when one looks at director general level in the Civil Service a very large number of people are recruited from outside. At one level that is good but on another it makes me worry that we are not equipping younger civil servants with enough delivery experience on their way up through the Civil Service. There has been a great process of professionalisation led by Sir Gus O'Donnell. If you look at qualified

finance professionals within departments since 2004 the number has risen dramatically, but we can go a lot further.

Q208 Mr Walker: From my limited experience of business, the finance director should be someone of very little humour who reins in the excesses of the chief executive who is a great visionary and spends money that simply does not exist in the business. I am sure any government would like to see more people fulfilling that role of corporate financial director within the Civil Service. Has progress been made in getting those types of people into post?

Mr Byrne: Sir Gus O'Donnell has overseen a pretty dramatic transformation of this over the past few years. My example of finance professionals is a good one. If you look at the consulting bill over the past few years it has reduced by about 30% since 2005-06 and that is due in no small part to the fact that government and the Civil Service led by Sir Gus O'Donnell have done a very good job at professionalising finance, IT, HR and other core disciplines. Having been a minister for five years now, my only observation is that we still need to do more just to encourage younger civil servants to spend a bit of time out in the business community or running a difficult agency.

Q209 Mr Walker: Do you ever see the chief executives of large consultancy firms and say, "Come on, mates: you are having a laugh. If you want to continue to do business with the Government we must have another look at the way you do things and structure yours costs. You are doing very well out of us and we do not believe that is reflected in your pricing"?

Mr Byrne: That is not something I need to do; it is a matter other departments must do, and the discipline of halving their consulting bill over the next couple of years is a pretty good forcing mechanism for that.

Q210 Paul Flynn: How will social impact bonds work?

Mr Byrne: That is a very interesting question. They may work in a number of different ways. One of the reasons we need to get some pilots going quickly is to understand how they can pan out. The basic problem I am trying to solve is that investments made in prevention by one agency often lead to savings made several years later that are harvested by a different agency. For example, in Birmingham it has been found that every pound invested in alcohol and drugs dependency can save £4 in the criminal justice system. We have to try to find a way to give the guys who have to make the preventative investment a share of the upside. There must be a couple of different ways to do this. But that is why I am grateful to Mr Straw and Mr Denham for agreeing to pilot this. The agenda is quite an exciting one. It is a pretty old problem in public service reform and I hope this helps us to solve it.

Q211 Kelvin Hopkins: Just to reinforce the point you made implicitly and explicitly, growth is absolutely crucial to the solution to these problems. If we can maintain growth at a reasonable rate all our problems will be solved.

Mr Byrne: I completely agree.

Q212 Chairman: When we have conducted these sessions we have played what we called the “Sweden versus Canada game” and people have come down on one side or the other. Canada faced with the need to make cuts engages in heavy targeting to meet strategic priorities and so on; Sweden believes that it must cut across the board. These are very different approaches. I want to know whether you are a “Sweden” man or “Canada” man.

Mr Byrne: I am a British man. There are things we can learn from both. The lesson from Canada is the work it did to build a consensus over the scale of the task. That was very important in Canada securing that reduction. What is good about Sweden is that it made some pretty clear decisions about what it wanted to protect and found a way radically to devolve power from the centre by the use of rights and entitlements. That is what I take away from the examples of Canada and Sweden. We have studied

pretty much every fiscal consolidation since 1974—there have been about 73—and we have tried to apply some fairly clear lessons in our own deficit reduction plan.

Q213 Chairman: So, it is neither Sweden nor Canada but a kind of hybrid?

Mr Byrne: Yes.

Q214 Julie Morgan: My question is not related to the subject we have discussed today. Can you give a quick update of where we are with Equitable Life? I know you had a briefing on it yesterday.

Mr Byrne: I believe I set this out yesterday at length to the all-party group. Mr Chadwick’s third interim report will be published next week and he will invite responses to it. He will publish his final report at the end of May. The commitment I gave to colleagues yesterday was that there would be a government response within a fortnight, but a little later this afternoon I shall provide a letter summarising what Mr Chadwick and I said to colleagues.

Chairman: As I said at the beginning, thank you for making yourself available whenever we have asked you to come. We have had some good sessions with you and enjoyed them, but we shall not do it again.

Written evidence from Rt Hon Liam Byrne MP, Chief Secretary to the Treasury

Q188 Mr Prentice: *I go back to Kelvin Hopkins’ point about the tax gap. Speaking from memory, the document Protecting Tax Revenues produced by HMRC in December 2009 talked about a tax gap of £40 billion. To what extent can we squeeze down that gap? We are asking people to make sacrifices and yet a huge sum of money goes uncollected, so how realistic is it to squeeze that tax gap of £40 billion down to £10 billion?*

The Government is committed to reducing the tax gap and the tax gap analysis shows that HMRC already collects over 90% of the tax that is due. The UK tax gap in 2007–08 is estimated at £40 billion—or around 8% of theoretical tax liabilities. This compares well with those of other countries: for example the US has measured its tax gap at 13% of tax liabilities and Sweden at 10%.

The tax gap could not be completely closed without placing disproportionate burdens on all taxpayers. However, the Government is committed to doing all that it can. “Protecting Tax Revenues 2009” sets out in detail what we are doing. Particular measures include strengthening the tax avoidance disclosure regime, that has already helped close over £12 billion in avoidance opportunities, and taking concerted international action to tackle tax havens.

Q191 Mr Prentice: *Yes. My question is: why can we not say to all UK citizens, whether they live in Belize or wherever, that they will be taxed on the basis of their worldwide income instead of on the basis of “domicile”, “UK resident for tax purposes” and “UK residency” which allows smart people with smart lawyers to avoid paying tax?*

The current rules link liability to UK tax on worldwide income and gains to the extent of a person’s connections with the UK. Someone who is UK resident or UK domiciled has significant connections to the UK and it is right that they should make an appropriate contribution to the UK tax system. Many UK citizens live overseas and may have no connection to the UK other than their citizenship. Making them liable to tax on their worldwide income would risk bringing undeserving cases into the UK tax net. Equally, some of those currently liable to UK tax because of their residence or domicile status may not be UK citizens and would cease to be liable to UK tax on their worldwide income if citizenship were made the basis for tax liability. That is not something the Government could defend.

March 2010

Memorandum from Tony Travers

The Committee is addressing the following four issues:

1. *The nature of expected cuts to public expenditure (targeted or across-the-board)*

The Government could adopt a number of approaches to reducing net public spending, including some or all of the following:

- Cuts to programmes on the basis of an agreed and worked-through plan that took account of overall government priorities and which made smaller cuts in some spheres of provision while making deeper ones elsewhere.
- Increasing charges and co-payments for services.
- Reducing or stopping universal benefit payments for people and households on higher incomes.
- Major reductions in “back office” costs, either by delivering economies of scale or by “outsourcing”.
- Stop providing some discretionary services.
- An across-the-board, flat-rate, spending reduction affecting all services.

In addition, there would be one-off options to reduce the impact of spending and borrowing, though such actions would not actually cut spending:

- Asset sales.
- Use of reserves and investments.

Finally, the favourite option for governments in need of cutting spending with minimal immediate impact would be to:

- Reduce capital investment.

“Cuts to programmes on the basis of an agreed and worked-through plan” would be the most intellectually-coherent approach to take. However, national politicians have thus far found it politically difficult to publish details about the changes to public expenditure (or taxation) likely to be needed to reduce public borrowing. Consequently, public service managers are, for the time being, having to guess the scale and timing of the spending cuts that will almost inevitably take place. The more suddenly cuts are imposed, the more likely they are to be “flat-rate” and “across the board” rather than as the result of any kind of planning.

The Government has already announced a sharp cut in capital investment in the period from 2011–12 to 2013–14. Typically, governments find it easier to stop or reduce capital projects rather than to confront the electorate with the consequences of revenue spending reductions. As a result, parts of Britain’s infrastructure are over-stretched and badly-maintained.

2. *Possible effects on the size and organisation of central government, frontline public services and other public sector bodies*

It would be up to the government of the day to decide how the organisation of central government, frontline services and public sector bodies were affected by any effort to reduce public spending. There is always a risk that the rhetoric of “culling quangos”, “reducing waste” and “cutting bureaucracy” will impede rational thought about the location and depth of spending cuts. Paradoxically, it is necessary to have a good quality bureaucracy to make cuts to the bureaucracy.

Structural reorganisations, the abolition of appointed bodies and reductions in the number of civil and other public servants may play a part in reducing public expenditure. But, one way or another, any substantive cuts in spending are likely to mean less money for key services such as the NHS, education, the police and social care, including frontline provision. This reality needs to be acknowledged. Alternatively, politicians would need to make clear they intended to introduce major tax increases that would be likely to affect most households, possibly significantly.

3. *The relative merits of different approaches to making public spending cuts*

Whichever approach to public spending cuts is adopted, it should have an effect that lasts for more than one year. Asset sales are less useful than, say, means-testing benefits. Public assent will need to be sought if such cuts are not to appear unjust or unexpected. In recent years, politicians have offered the public a move towards Scandinavian public welfare standards with levels of taxation closer to those found in America. In the near future, the opposite trend is more likely. Unless the Government explains what is happening, there would be a serious risk people will feel politicians are—even more than normal—over-promising and under-delivering.

4. *How government and public services could most effectively adapt to a tighter fiscal environment (in particular by determining the areas that government should and should not be involved in)*

Experience suggests it is unrealistic to expect the State to withdraw from service provision where the electorate has come to expect public provision or regulation. Indeed, there are such wide expectations of government in Britain that it would require cross-party agreement if there were to be spheres of activity where the public sector would have no role. Such a change would require many years to bed in.

However, the Government could stop making additional commitments to push up service standards, or to initiate new services, or to pay for additional subsidies. For the existing service base, the Government could signal where it was and was not willing to see higher charges and/or co-payments. It could also indicate which real terms spending figures were or were not to be protected.

December 2009

Written evidence from the National Union of Teachers

INTRODUCTION

1. The National Union of Teachers (NUT) is pleased to submit views to the short inquiry by the Public Administration Select Committee (PASC) into public administration and the fiscal squeeze.

PRINCIPLES AND STRATEGY

2. Public spending must not be seen as a liability. Instead, public spending targeted at the country's key strategic objectives should be seen as a valuable investment. Economic recovery will not come as a result of public spending cuts but will be helped by sustained public sector investment.

3. The debate must not be influenced by an assumption that private sector delivery of public services represents better value for money. For example, the use of the Private Finance Initiative (PFI)—justified in relation to the supposed transfer of risk to the private sector—has resulted in the Government having to provide funding for private sector companies unable to raise the necessary finance.

PUBLIC SPENDING AND EDUCATION

4. Public sector workers including teachers represent a substantial proportion of the workforce as a whole. Better public sector pay and prospects will benefit the economy due to the increased spending power and skills thereby generated.

5. If we want to develop and support a high quality education service, we must invest in teachers. Pay levels and prospects need to attract and retain good graduates to teaching as a career, not as a temporary expedient. This is an investment that we cannot afford not to make.

6. Recent years have seen substantial cuts in the real value of teachers' pay. From 2005 to 2008, teachers' pay increases were significantly below Retail Prices Index (RPI) inflation—in September 2008, RPI inflation at 5% was more than double the value of the teachers' pay award of 2.45%. Some of the cut was restored by the September 2009 pay increase but, overall, teachers' real pay has already been cut over the period since 2005.

7. Teaching needs to recruit a significant proportion of each year's graduate cohort. Incomes Data Services (IDS) research for the NUT showed a gap of 21% in September 2008 between starting pay for teachers and starting pay for other graduates. This gap in starting pay grew wider over the first few years of their careers as teachers' pay progressed by significantly less than other graduates. The improvement in teacher recruitment resulting from the economic crisis has to be seen in this context.

8. Investment in education must take account of teachers' conditions of service as well as their pay. Teachers' conditions of service are pupils' conditions of learning. The DCSF Teachers' Workload Survey for 2009 showed that classroom teachers work on average more than 50 hours a week, while the working hours of senior school staff are higher still. Despite the Government's commitment to reduce class size, primary class sizes in the UK are among the highest in developed countries. OECD data for September 2008 showed that UK class sizes averaged 25.8 compared to the OECD average of 21.5. Among the 31 countries listed, only Japan, South Korea and Turkey had higher class sizes.

SCHOOL AND COLLEGE FUNDING

9. When Chancellor of the Exchequer, in his March 2006 Budget Gordon Brown set out a commitment that spending per pupil in the state sector should match spending per pupil in the private sector. At that time spending in the public sector of £5,000 per pupil compared to £8,000 per pupil in the private sector. OECD's class size data show the extent to which the private sector is, for example, able as a result to offer smaller classes.

10. The latest DCSF spending per pupil figures in England show a projected real terms increase of £990 or 19% between 2006–07 and 2010–11. The equivalent figure in the private sector is also, however, likely to increase between these dates. Whether the gap in per pupil spending closes at all by 2010–11 remains to be seen.

11. Spending in the state sector has failed to maintain its upward trajectory. Real terms funding per school pupil aged 3–19 in England (revenue and capital) rose by 7% in 2008–09, but is projected to fall by 1% in 2010–11. Even when looking at revenue funding alone, removing the impact of the Government's decisions on capital funding, real terms funding increases have fallen from 6.4% in 2008–09 to 3.3% in 2009–10 and just 0.9% in 2010–11.

12. There have also been significant funding problems in the post-16 sector. Overall funding allocations notified to schools and colleges in early 2009 included virtually no planned growth in student numbers, even though it was already clear by then that the economic downturn would cause an increase in student numbers due to the decline in employment opportunities for young people. Additional funding for 16 and 17 year olds announced in the 2009 Budget was still inadequate to meet demand.

13. The post 16 sector fears that it will receive significantly worse funding settlements in coming years than the schools sector. The NUT represents teachers in sixth form colleges, which are recognised as adding greater value than any other form of post 16 institution. The FE funding system means that group sizes are already significantly higher in sixth form colleges than in school sixth forms due to a “funding gap” estimated as being up to 20% per student. This successful sector should not be placed under further pressure by inadequate funding settlements.

EFFICIENCY SAVINGS

14. The DCSF discussion paper “Securing Our Future; Using Our Resources Well” continues to emphasise the expectation that schools and colleges will make “efficiency savings” and see their budgets calculated accordingly.

15. Schools and colleges already make efforts to use their resources well. The response to the DCSF paper has suggested that it is unwise to assume that they are able to make further extensive efficiency savings. The Children, Schools and Families Select Committee has also expressed scepticism about the scope for efficiency savings. In particular, there is little room for savings in pay costs which represent the large majority of spending.

PUBLIC SERVICE PENSIONS

16. Over recent months, public service pensions have come under increasing attack, both politically and in the media. This has been exacerbated by current economic circumstances, leading some to argue that the pension arrangements of public service workers are unaffordable and unsustainable.

17. Much of the discourse has been characterised by misinformation and an emotive attack on the public sector as a whole. Too often public debate has concentrated on the pension arrangements of a few highly paid people in the public service rather than the vast majority of low or moderately paid public servants.

18. The reality behind “gold-plated” pensions is that most public service pensioners receive a pension broadly comparable with the average private sector worker. In the Teachers' Pension Scheme, for example:

- Average teachers' pension in payment £9,900.
- 53% of pensions in payment are less than £10,000 per annum.
- For teachers with under 20 years service the average pension in 2006–07 was £3,750 per annum.
- Only 0.64% of pensions in payment are over £30,000 per annum.

(Source: Teachers' Pension Scheme Resource Accounts 2008–09)

19. Public service pensions have already been through a process of evaluation and reform. The principles for pension reform in the Teachers', NHS and Civil Service schemes were agreed by the Government and the TUC in the Public Services Forum (PSF) on 18 October 2005. It was recognised that changes in demographics, employment patterns, and the legal and regulatory framework required public service pension schemes to be modernised and to be sustainable. The PSF agreement explicitly recognised that each scheme covered would have a cost envelope that would be respected. In the Teachers' Pension Scheme, for example, there is a 14% ceiling on the employers' contribution rate from the 2008 actuarial valuation onwards and similar arrangements have or are being introduced in other public service pension schemes.

20. The NUT is concerned that current debate around public service pensions is ill-informed and unfair. In our view the central problem is not public sector pensions *per se*, rather it concerns the private sector's retreat from proper pension provision. If that problem remains unresolved many millions will be condemned to a bleak old age. We believe that the current debate should be grounded in a broader, more objective assessment of the reality of public sector pensions.